

BEFORE THE
SURFACE TRANSPORTATION BOARD

Ex Parte No. 646 (Sub-No. 3)

WAYBILL DATA RELEASED IN THREE-BENCHMARK RAIL RATE PROCEEDINGS

Joint Reply Comments

submitted by

American Chemistry Council, The Fertilizer Institute, National Grain and Feed Association, The National Industrial Transportation League, Consumers United for Rail Equity, American Forest and Paper Association, Glass Producers Transportation Council, Alliance for Rail Competition, and Montana Wheat and Barley Committee

On May 3, 2010, the above-listed parties (“Interested Parties”) submitted Opening Comments in support of the Notice of Proposed Rulemaking (“Notice”), served by the Surface Transportation Board (“Board”) in this docket, on April 2, 2010. In the Notice, the Board proposed to revise its Three-Benchmark rules for small rail rate cases by permitting parties to select comparable movements to the issue traffic from the unmasked Waybill Sample data of the defendant carrier for the 4 years that correspond with the most recently published Revenue Shortfall Allocation Method (“RSAM”) figures. The Interested Parties now submit these Reply Comments in response to the various Opening Comments filed by the Association of American Railroads (“AAR”), Canadian Pacific Railway Company (“CP”), and jointly by Norfolk Southern Railway Company and CSX Transportation, Inc. (“NS/CSX”) (collectively the “Railroad Parties”).

I. THE RAILROAD PARTIES' PROCEDURAL OBJECTIONS ARE MISPLACED.

A. The Railroad Parties Disingenuously Claim An Inability To Meaningfully Comment On The Board's Proposals.

The Railroad Parties all allege that the Notice is procedurally inadequate to comply with the Administrative Procedure Act ("APA"). Specifically, they assert that the Notice lacks the required factual detail and rationale to permit meaningful comment on the Board's proposal to permit the selection of comparable movements from four years of Waybill Sample data.¹ This allegation is extremely disingenuous.

There are similarities between the Railroad Parties' challenge to the adequacy of the Notice in this proceeding and a challenge to the adequacy of a Notice of Proposed Rulemaking for nuclear power plant fire protection programs in *Connecticut Light and Power Company v. Nuclear Regulatory Comm'n*, 673 F.2d 525 (D.C. Cir. 1982) ("*CL&P*"). The NRC provided very few technical details to justify the new rule, and instead asserted that "the position of the staff and the licensees regarding the provisions of this rule is documented and well known." *Id.* at 531. In the final rule, the NRC also had relied on technical studies that were not mentioned in the Notice. *Id.* at 532. Although there were repeated requests during the comment period for the NRC to identify the technical studies upon which the proposed rules were based, the Court characterized the NRC's response as "unhelpful" and the comments submitted to the agency as "noticeably general." *Id.* Despite its harsh criticism of the agency, the Court affirmed the NRC's final rules because:

Nonetheless, this rule-making process took place against a background of five years during which the Commission explored safety proposals in a public forum and exposed the important technical studies to adversarial comment. Given this context, we conclude that the technical background of the rules was

¹ AAR Comments at 3; CP Comments at 2-4; NS/CSX Comments at 6-7.

sufficiently identified to allow for meaningful comment during the rule-making process.

Id. See also, *Tabor v. Joint Board for the Enrollment of Actuaries*, 566 F.2d 705, 709-10 (D.C. Cir. 1977) (A statement of purpose for newly adopted rules is unnecessary if the purpose is “obvious and unmistakable”).

The present Notice similarly takes place against a background in which the agency explored the use of both single and multiple years of comparison movements to calculate the R/VC_{Comp} benchmark in a public forum in which the proposal was exposed to adversarial comment. This history, which the Interested Parties described in their Opening Comments, at 3-6, establishes that Board precedent applying the R/VC_{Comp} benchmark long ago determined that comparison movements should be drawn from multiple years of Waybill Sample data, and not a single year. The Notice merely would continue that practice. Moreover, even if the Railroad Parties could claim ignorance of this precedent, the Opening Comments of the Interested Parties have given them ample opportunity to provide meaningful comment in their Reply Comments.

In addition, from the very outset of the *Simplified Standards* proceeding in Ex Parte No. 646 (Sub-No. 1), the debate over using Waybill Sample data to determine the R/VC_{Comp} benchmark has centered around the issue of regulatory lag. Indeed, it is the Railroad Parties themselves who first framed this issue in *Simplified Standards* and have doggedly pursued it ever since. All three Railroad Parties revive the regulatory lag argument in their comments in this proceeding. Whereas, in *Simplified Standards*, the Railroad Parties argued that regulatory lag was a problem even for one year of Waybill data, they argue here that the problem is compounded by four years of Waybill data.² This latest argument was previously aired and

² It is unclear whether the Railroad Parties’ are now advocating for using only the most recent year of waybill data in lieu of the Board’s proposal to use the most recent four years, or whether they still oppose even one year of data, unless such data is indexed to the current year.

rejected by the Board in *E.I. du Pont de Nemours and Company v. CSX Transportation, Inc.*, Docket Nos. 42099 *et al.* (served Jan 15, 2008), and aired again in the briefing of *CSX I*, but not decided. Thus, it should be abundantly clear to any observer of this proceeding that regulatory lag is a central issue on remand. Neither the Railroad Parties nor the Interested Parties can genuinely claim any loss or disadvantage in responding to the Notice on that issue.

Despite precedent that lends support to the adequacy of the Board's Notice, and the apparent ability of the Railroad Parties to submit meaningful comments on the major issues, it would not be in the public interest to unnecessarily risk further appeal of the proposed rule on procedural grounds once again. Even in *CL&P*, at 528, the Court was highly critical of the NRC, stating that "[t]he Commission complied [with the APA] but barely...." The Interested Parties have no desire to repeat this process a third time, if, in this case, an appeals court should conclude that the Board's Notice falls short of even the standard in *CL&P*. Therefore, if necessary, the Interested Parties would much prefer that the Board render this argument moot by more explicitly expressing its rationale, even if that requires an additional round of comments.

B. The Proposed Rule Is Not a Change to an Existing Rule.

A second component of the Railroad Parties' procedural objection is based upon the patently inaccurate premise that the Notice proposes to change the *current* rule from one year of Waybill Sample data to four years.³ There is no *current* one-year rule and there never has been.

The Railroad Parties erroneously presume that one year became the current rule when the D.C. Circuit overturned the Board's decision to permit four years of waybill data in *Simplified Standards for Rail Rate Cases*, Ex Parte No. 646 (Sub-No. 1) (served Sept. 5, 2007) ("*Simplified Standards*"), *aff'd sub nom. CSX Transp. Inc. v. STB*, 568 F.3d 236 (D.C. Cir. 2009) ("*CSX I*"),

³ CP Comments at 6 ("The Board's proposal to jettison the existing rule..."); NS/CSX Comments at 5 ("[I]f a Three Benchmark proceeding were filed today, the Board would release to the parties the most recent Waybill Sample – the Waybill Sample for 2008...").

and *vacated in part on reh'g*, *CSX Transp. Inc. v. STB*, 584 F.2d 1076 (D.C. Cir. 2009) (“*CSX II*”). In vacating the four-year rule, however, the DC Circuit’s decision in *CSX II* created a void. That void was not, and could not have been, filled by a one-year rule because the Board never adopted a one-year rule in *Simplified Standards* or any other proceeding. Thus, it is false to claim that the proposed rule is a *change* to the current rule that requires a reasoned explanation.

In fact, as the Interested Parties demonstrated in their Opening Comments, at 3-6, Board precedent applying the R/VC_{Comp} benchmark long ago determined that comparison movements should be drawn from multiple years of Waybill Sample data. If anything, the Board’s four year proposal merely would continue that practice. A decision to use a single year of Waybill Sample data would be the significant *change* from Board precedent that would require a cogent and rational explanation. *Motor Vehicles Mfrs. Ass’n v. State Farm Mut. Auto. Ins. Co.*, 463 U.S. 29, 48 (1983).

II. BOARD PRECEDENT PROVIDES A LONG-ESTABLISHED RATIONALE FOR ITS PROPOSALS.

In their alleged “speculation” over the rationale underlying the Board’s proposal to draw comparison movements from four years of Waybill Sample data, the Railroad Parties ignore the obvious rationale that exists in Board precedent dating back to the origins of the R/VC_{Comp} benchmark in 1987. *See*, Interested Party Comments at 3-6. The only plausible reason for ignoring this precedent is that, in those cases, the agency explicitly rejected the Railroad Parties’ arguments for limiting the comparison movements to a single year of Waybill Sample data.

In *McCarty Farms v. Burlington Northern Inc.*, 4 I.C.C. 2d 262 (1988), the Board expressly reversed an earlier decision to draw comparable traffic from a single year of waybill data because “one year of data should not be used to establish a standard which will have application to the movements of traffic for many years” due to “[t]he risk that data for any one

year could be non-representative of the long-term trend....” *Id.* at 277. The Board instead concluded that “the best approach...to determine the reasonableness of rates for any year...is to use an average of several years’ of data.” *Id.* In support of this conclusion, the Board reasoned that “[e]valuation of R/VC ratios over several years tends to balance out cyclical fluctuations and provide a better estimate of maximum reasonableness from a long run perspective.” *Id.* See also, *South-West R.R. Car Parts Co. v. Missouri Pac. R.R. Co.*, Docket No. 40073, 1988 ICC LEXIS 370 (Dec. 1, 1988) (using 5 years of data “to smooth out cyclical fluctuations”).

In *Simplified Standards*, the Board decided that rates prescribed under the Three-Benchmark standard would be effective for five years, subject only to a \$1 million relief cap. A one-year rule would run the very same risk that the agency found unacceptable in *McCarty Farms*, namely, that a single year of data would not be representative of the long-term trend, and thus would be inappropriate for prescribing rates over a five year period.

Indeed, the Railroad Parties’ own comments reaffirm the rationale underlying the agency’s original rejection of one year of waybill data in favor of multiple years. NS/CSX, at 11, cited to several rail rate studies to show that “rail rates not only fluctuate over time, but that they fluctuate from one year to the next.” They also stated that “the Board should take note of the dramatic changes that can occur over a six-year period.” *Id.* at 14. CP, at 5, observes that “[i]n the dynamic rail marketplace, both the rates and the costs of participating carriers change significantly over time.” Citing to the same studies as NS/CSX, CP asserts that “there is substantial quantitative proof that railroad rates and costs fluctuate significantly over any given period of three to six years.” *Id.* If rates and costs change so significantly from one year to the next, it makes far more sense to draw the comparison movements from an average of several years of waybill data in order to smooth out these fluctuations, especially when prescribing rates

over a five year period. Otherwise, the Board risks prescribing rates that are locked in at the peak or the valley of a business cycle.

III. THE RAILROAD PARTIES INAPPROPRIATELY ELEVATE TEMPORAL CONSIDERATIONS ABOVE ALL OTHER COMPARABLE FACTORS.

A fundamental flaw in the Railroad Parties' logic is their conclusion that temporality is not only a relevant factor in selecting comparable traffic, but that it is the *most* relevant factor.

NS/CSX, at 14-15, make this argument most directly:

For a rate comparison methodology like the Three Benchmark approach to have any validity, the statute requires at a minimum that the comparison group movements be similar to the movements at issue. Put differently, if the Board were asked to consider the reasonableness of a rate set in 2010, an analysis of whether the rate was "comparable" to unadjusted rates from 2008, 2007, 2006 or 2005 would not provide a meaningful basis to evaluate the reasonableness of the 2010 rate. Rather, such an analysis is by definition a consideration of whether the 2010 rate would have been reasonable in 2008, 2007, 2006, or 2005. [footnote omitted] Logically, the Board cannot use outdated rates and costs in the Three Benchmark approach without any mechanism to bring them to levels that reflect the pricing *as of the date of the complaint*....

(underline in original; italics added) After stating the comparability requirement in the first sentence, NS/CSX proceed to describe that requirement *solely* in temporal terms tied to the date of the complaint. Similarly, the AAR, at 4, asserts that using four years of waybill data "to challenge a carrier's existing rates would have little or no economic rationale in the context of *current market conditions*." (emphasis added) *See also* CP Comments at 4-5. Thus, the Railroad Parties would make temporal comparability a threshold consideration that, if not satisfied in accordance with their definition, requires the Board to reject a party's comparison group.

NS/CSX expressed this view even more explicitly in their discussion of the Board's proposal to permit the parties to justify selection of comparison movements from a temporal subset of the four-year Waybill Sample as one of the many comparison factors to be considered.

NS/CSX, at 19, reject that proposal as insufficient to address their temporal concerns, because “parties must consider numerous comparability factors in proposing a comparison group, and the Board can reject a proffered comparison group for any one of those factors, even if it results in the use of more outdated information.” In other words, they contend that the temporal factor should be elevated above all other factors in the selection of the comparable group.

But, as discussed above, the agency long ago rejected an exclusive focus upon current market conditions in favor of multi-year data in order *not* to lock in rates at current levels when prescribing rates for five years. Thus, the Board has in fact considered temporal factors in the selection of comparison movements by defining temporality based upon the most recent four years of the Waybill Sample, unless a party can justify selection from a more limited temporal subset of that data. This is a rational and informed decision.

IV. THE RAILROAD PARTIES’ PROPOSAL TO ADJUST HISTORICAL RATES TO CURRENT LEVELS WOULD COMPROMISE THE RELIABILITY OF THE THREE-BENCHMARK APPROACH.

The Railroad Parties indicate that their objections to drawing the comparison group from four years of Waybill Sample data would be mitigated if the Board would permit carriers to adjust the historical rates to current levels.⁴ For the reasons discussed in the preceding section, no adjustment is necessary or warranted because that would defeat the Board’s objective to smooth out market fluctuations with a multi-year approach. In addition to that argument, any adjustment to current market levels is unjustified and inappropriate because it would create a mismatch among the three benchmarks that distorts the results of the Three-Benchmark approach.

As noted above, the R/VC_{comp} benchmark predated the Three-Benchmark approach as the methodology for deciding small rate cases. When the agency first formally proposed the Three-Benchmark approach in Ex Parte No. 347 (Sub-No. 2), *Rate Guidelines—Non-Coal Proceedings*,

⁴ CP Comments at 6-7; NS/CSX Comments at 16-18.

1995 ICC LEXIS 301 (Nov. 22, 1995), it added the RSAM and $R/VC_{>180}$ benchmarks in response to criticism of using the R/VC_{comp} benchmark as the sole approach to small cases. Consistent with its decisions in *McCarty Farms* and *South-West Car Parts* to draw comparable traffic from multiple years of waybill data, the agency decided to use a 4-year average of the RSAM and $R/VC_{>180}$ benchmarks "so as to smooth out annual variations and minimize the impact of any year that may have been aberrational for that carrier." *Rate Guidelines—Non-Coal Proceedings*, 1 S.T.B. 1004, 1032-33 (1996). As a result, all three benchmarks would be derived from the same Waybill Sample data for precisely the same reasons. By attempting to mark-up the R/VC ratios of the comparison group to market conditions in a single year, the Railroad Parties' market adjustment would undermine the agency's carefully considered decision to use a 4-year average of all three benchmarks.

The three benchmarks that comprise the Three-Benchmark approach function as part of a formula to determine the maximum reasonable rate. The RSAM benchmark divided by the $R/VC_{>180}$ benchmark creates a "Multiplier" that is applied to the R/VC_{comp} benchmark in order to account for a carrier's revenue adequacy in the rate prescription. The Multiplier will be greater than one, resulting in an increase to the R/VC_{comp} , and hence a higher prescribed rate, if the carrier is revenue inadequate. The further from revenue adequacy, the larger the Multiplier. Conversely, the Multiplier will be less than one, resulting in a decrease to the R/VC_{comp} , and hence a lower prescribed rate, if the carrier is revenue adequate. The further above revenue adequacy, the lower the Multiplier.

A market adjustment to current levels for the R/VC_{comp} benchmark, without also adjusting the RSAM and $R/VC_{>180}$ benchmarks, would create a glaring inconsistency in the application of the Waybill Sample data. At current rate levels, a carrier may be closer to, or further from,

revenue adequacy, than it was during the four-year average of the waybill data used to calculate the Multiplier. Consequently, the Multiplier is likely to be either too high or too low when applied to an R/VC_{Comp} benchmark that has been indexed to current levels. This also would be true if the Board used only the most recent year of Waybill Sample data. This creates a far more significant reliability problem than the Railroad Parties contend is caused by drawing the comparison group from four years of historical waybill data.

The potential distortion caused by applying a Multiplier based upon a four year average of waybill data to an R/VC_{Comp} benchmark that either is drawn from the most recent year of Waybill Sample data, or is indexed to current levels, can be illustrated from the Board's most recent RSAM and $R/VC_{>180}$ calculation in *Simplified Standards for Rail Rate Cases – 2007 RSAM and $R/VC_{>180}$ Calculations*, STB Ex Parte No. 689 (served May 12, 2009). Based upon the RSAM and $R/VC_{>180}$ values provided in Tables I and II of that decision, the table below calculates the Multiplier that would apply to each Class I carrier in a current Three-Benchmark case based upon the 4-year average of the Waybill Sample data and compares it to a Multiplier that would be based solely upon the most recent year, which is 2007.

Railroad	4-Year Average Multiplier	2007 Multiplier
BNSF	1.17	1.09
CSXT	1.30	1.24
GTC	1.37	1.10
KCS	1.34	1.21
NS	0.88	0.89
SOO	1.08	.74
UP	1.41	1.21

For every carrier, except NS, the four year average of the Multiplier is higher—and in some cases much higher—than the single most recent year. The four year average for NS is lower by

just one one-hundredth of a percent. Applying a Multiplier based on a four-year average to an R/VC_{comp} based upon current rate levels (whether indexed or based on the most recent single year of waybill data) produces an apples-to-oranges equation that overstates the maximum reasonable rate.

V. EXPANDING THE WAYBILL SAMPLE SIZE WOULD NOT JUSTIFY DRAWING COMPARISON MOVEMENTS FROM ONLY A SINGLE YEAR OF WAYBILL DATA.

The Railroad Parties disingenuously speculate that the STB's primary rationale for permitting the parties to draw their comparison groups from four years of Waybill Sample data is the potential that fewer years, or even one year, would not provide a sufficient number of movements from which to develop a comparison group. This is a strawman argument that should be dismissed.

As the Interested Parties observed in their Opening Comments, at 6-7, there is a practical need for four years of Waybill data in order for the Three-Benchmark approach to work in many small rate cases. But that is not, and indeed cannot be, the primary reason for the Board's proposal. As noted above and in the Interested Parties' Opening Comments at 3-6, the agency provided the primary rationale underlying its decision to draw comparison movements from four years of Waybill Sample data in precedent dating back to 1987.

The Railroad Parties suggest expansion of the Waybill Sample as an alternate means to generate a larger pool of traffic from which to select comparison movements. Although the Interested Parties do not object to this idea, its adoption would not justify using only one year of Waybill Sample data; nor would it change the primary underlying rationale for drawing comparison movements from four years of Waybill Sample data.

Respectfully submitted,



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