STB EX PARTE NO. 552 (SUB-NO. 1)

RAILROAD REVENUE ADEQUACY - 1996 DETERMINATION

Decided August 14, 1997

Three Class I railroads, Illinois Central Railroad Company, Norfolk Southern Railroad Company, and Soo Line Railroad Company are found to be revenue adequate, having a return on investment that exceeds the target cost of capital for 1996.

BY THE BOARD:

This annual determination of railroad revenue adequacy is made in accordance with the standards developed in *Standards for Railroad Revenue Adequacy*, 364 I.C.C. 803 (1981), *Standards for Railroad Revenue Adequacy*, 3 I.C.C.2d 261 (1986), and *Supplemental Reporting of Consolidated Information for Revenue Adequacy Purposes*, 5 I.C.C.2d 65 (1988). Pursuant to those procedures, which are essentially mechanical, a railroad will be considered revenue adequate under 49 U.S.C. 10704(a) if it achieves a rate of return on net investment (ROI) equal to at least the current cost of capital for the railroad industry. We perform the annual revenue adequacy exercise because we have been directed to do so by Congress.

In *Railroad Cost of Capital - 1996*, 2 S.T.B. 344 (1997), we determined that the 1996 railroad industry cost of capital was 11.9%. By comparing this figure to the 1996 ROI data obtained from the carriers' Annual Report R-1 Schedule 250 filings, we have made revenue adequacy calculations for each of the Class I freight railroads that were in operation as of December 31, 1996.

A summary of our findings for all Class I railroads is set forth in the appendix to this decision. We find three carriers, Illinois Central Railroad Company, Norfolk Southern Railroad Company, and Soo Line Railroad Company, to be revenue adequate for 1996. Our findings with respect to the Class I carriers will be final on the effective date of this decision.

Environmental and Energy Considerations

We conclude that this action will not significantly affect either the quality of the human environment or the conservation of energy resources.

Regulatory Flexibility Analysis

Pursuant to 5 U.S.C. 603(b), we conclude that our action in this proceeding will not have a significant economic impact on a substantial number of small entities. The purpose and effect of the action is merely to update the annual railroad industry revenue adequacy finding. No new reporting or other regulatory requirements are imposed, directly or indirectly, on small entities.

Vice Chairman Owen, *commenting*:

In the past, I have stated that it would be appropriate to revise the *methods* within which we determine railroad revenue adequacy. I still believe that at a very minimum new standards should be developed that will provide a more realistic determination of a carrier's overall economic health.

As a threshold matter, however, I am not convinced whether the government or the industry should be expending valuable resources addressing the issue. Indeed, I believe that the premises upon which the agency is charged to determine railroad revenue adequacy - - 49 U.S.C. 10101a(3),10704(2)(3) - - are flawed, given today's regulatory climate and industry economics.

Specifically, but for the Board's determination of "adequacy", which is based, I believe, on methodologies that are outdated, no one really doubts that the industry, as a whole, is doing far better economically than our determination suggest.

This annual, ritualistic application, of the "adequacy standards", results in no more than a mere illusion of a carrier's economic vitality. Indeed, in a practical sense, a finding of inadequacy, or for that matter adequacy, has no effect on a railroad's ratemaking authority. Moreover, given the limited amount of traffic, over the rates for which we have jurisdiction, a finding of adequacy has no meaningful impact on a carrier's future financial performance. In other words, there is nothing, in a practical sense, that we can do to improve a carrier's total economic health with either a finding of adequacy or inadequacy.

It is a carrier's ongoing positioning in relevant markets that sets the pace for achieving revenue adequacy. There is very little that the Board can do about that, notwithstanding certain statutory directives to the contrary.

The time has come to discontinue this inquest, *albeit* statutorily derived. I would prevail upon Congress, at its earliest convenience, to repeal the statutory directives requiring the Board's determination of railroad revenue adequacy. The agency's resources, the industry's resources, and the taxpayer's dollars are all better utilized elsewhere.

It is ordered:

This decision is effective on August 28, 1997.

We find:

Three carriers, Illinois Central Railroad Company, Norfolk Southern Railroad Company, and Soo Line Railroad Company, are revenue adequate for 1996.

By the Board, Chairman Morgan and Vice Chairman Owen. Vice Chairman Owen commented with a separate expression.

APPENDIX

Railroad	ROI	Finding
Burlington Northern and Santa Fe Railway Company	8.6%	Inadequate
Consolidated Rail Corporation	8.4%	Inadequate
CSX Transportation, Incorporated	8.9%	Inadequate
Grand Trunk Western Railroad, Incorporated	NM	Inadequate
Illinois Central Railroad Company	15.2%	Adequate
Kansas City Southern Railway Company	7.2%	Inadequate
Norfolk Southern Railroad Company	13.0%	Adequate
Soo Line Railroad Company	23.5%	Adequate
Union Pacific Railroad Company	8.3%	Inadequate

NM = ROI is negative; therefore it is not meaningful.