

STB Activities Speech

July 2013

For those who are not familiar with the Surface Transportation Board, I'd like to start by giving you a little background about our agency. The Board is charged with regulating the economic activities of America's freight-railroad system. In the decades since that system was largely deregulated by the Staggers Act of 1980, it has become a model of business efficiency. The nation's railroads are among the most well-regarded and profitable entities in this country. Other nations marvel at their operations, achievements, and progress. At the same time, we know that the story for shippers and railroads is an uneven one.

Deregulation worked so well that many shippers feel there is now a lack of real competition. They argue that mergers have left the country dominated by two regional duopolies that increasingly offer high, take-it-or-leave-it rates to customers that have no other transportation alternative.

Our job at the STB is to strike a balance among all stakeholders enabling carriers to maintain economic viability while ensuring efficient, competitive, and cost-effective transportation for shippers. We strive to help parties innovatively solve their freight-

transportation disputes so that freight keeps moving, businesses keep growing, and commerce flows.

It's this innovation that's been driving my tenure at the Board. Much has changed since the current rules on rail competition were put in place. I'm taking a hard look at current regulations and have asked our stakeholders how, if, and where the Board should update its rules and procedures in light of the many changes in the rail industry that have occurred since deregulation.

I want railroads to continue to invest in their infrastructure and provide the most efficient, environmentally sound freight transportation possible. And I also want American companies and farmers to be able to ship their goods anywhere and anytime at reasonable rates. The Board is here to ensure that happens.

Now to some specifics about our work.

In 2011, the Board held a two-day public hearing on competition issues, in which nearly almost all of our stakeholders provided comments or testimony. Based on the input that we received from that hearing, the Board initiated two significant rulemakings, both centered on examining ways to provide shippers with better rates, while not significantly hurting the railroad industry's bottom line and ability to reinvest in the freight rail network.

The first rulemaking involves a proposal to increase rail-to-rail competition through greater use of reciprocal switching. Soon after the hearing was held, the Board received a petition for rulemaking from the National Industrial Transportation League, in which that group proposed that shippers lacking effective transportation alternatives would be granted access to a competing railroad if there is a working interchange within 30 miles. The Board conducted a lengthy preliminary analysis of NIT League's proposal and found that, before we could rule on whether to adopt it, we needed more empirical information from stakeholders about the effect it would have on railroad finances and operations. Accordingly, we asked our stakeholders to study the impact on rates and service for shippers that would qualify under the proposal; the impact on rates and service for captive shippers who would NOT qualify; the impact on the railroad industry's financial condition and network efficiencies; and finally, for proposals on competitive-access pricing. We asked our stakeholders to report back to us.

Opening comments in response to this order were filed on March 1 and reply comments on May 30. The Board staff is now poring over this evidence, and once we have fully studied it, we will decide where to go next on NIT League's proposal.

The second proposal arising from the competition hearing involved reforms to the Board's methodologies for resolving rate disputes, to ensure that all captive shippers have a meaningful way to challenge rates. Captive shippers have long told us that they don't

bring rate disputes to the STB because of high litigation costs associated with the Board's complex Stand Alone Cost (SAC) test traditionally used to resolve big rate cases.

A few years ago, the Board addressed this problem by modifying and creating new processes shippers could use to challenge the reasonableness of a railroad's rate. Specifically, the STB created a Simplified Stand Alone Cost, or Simplified-SAC, methodology. This methodology is based on the traditional SAC process, but with certain variables assumed, making it a quicker and simpler process. In addition, the STB created a new methodology, called the Three Benchmark test, in which the rate at issue is compared to the rates from a group of similar traffic. However, because the methodologies used in these simplified procedures are less precise than those used in the traditional SAC cases, the Board capped the amount of relief available under them. Specifically, shippers can only obtain up to \$5 million in relief using the Simplified-SAC test and only \$1 million using the Three Benchmark test.

Despite adoption of these new methodologies, the number of rate cases brought under them is still small, and shippers pointed out during the competition hearing that there are still high barriers to filing a rate case.

Accordingly, last summer the Board proposed a series of reforms to make the process of challenging a rate less cumbersome. Just two weeks ago, the Board adopted those rules. Let me give you a quick overview of what these new rules will do.

First, the Board reasoned that there was little to be gained by shippers who used the traditional SAC test instead of the Simplified-SAC test. So, since very few shippers attempted to use the Simplified-SAC approach, we considered ways to encourage them to use it more often. To do this, the Board removed the \$5 million limitation on relief for cases brought under the Simplified SAC test. With no limit on relief for such cases, the Board is hopeful that more shippers will use this methodology to challenge rates. To make the Simplified-SAC test more accurate, the Board made some technical changes to the methodology.

The Board also increased the relief available under its other simplified rate reasonableness methodology, the Three-Benchmark test, from \$1 million to \$4 million. Having now processed a number of these cases, the Board believes that the \$1 million in relief was not in line with the amount it would cost to litigate such a case.

In addition to the changes in the relief caps, the Board also made certain technical changes to the Full-SAC test, regarding “crossover” traffic. This is traffic that, under the SAC test, moves on both a hypothetical railroad and the real-world railroad. Because of the way revenue from this crossover traffic was being allocated between the hypothetical and real-world railroads, the test was causing illogical results. Accordingly, in our new rules, we have modified the manner in which the revenue from this crossover traffic is allocated. We also have changed the basis for the interest rate charged on reparations for

unreasonable rates, and will look more closely at the use of crossover traffic, in a future proceeding.

Despite these changes, the Board is still concerned that there may be barriers to grain shippers in bringing rate complaints. As we note in the decision, no grain shipper has brought a rate complaint to the agency in over 30 years, despite the fact that a great number of these shippers are captive to a single railroad. So, as we announced two weeks ago, we will begin a new proceeding this fall on rate relief for grain shippers.

Specifically, we will seek input from interested parties, including members of the National Grain Car Council, on grain shippers' ability to effectively seek relief for unreasonable rates. We will look at proposals for modifying existing procedures, or new, alternative rate-relief methodologies. I encourage those in the audience to submit any ideas or thoughts you may have on how to improve the rate complaint process for grain shippers.

On other fronts, the Board recently proposed several changes to its key costing methodology, the Uniform Rail Costing System, or URCS. We're proposing to adjust how URCS calculates certain system-average unit costs to better reflect railroad operations. Our proposal will automatically reflect economies of scale relative to shipment-size increases, eliminating the current need for a separate mathematical adjustment referred to as the "make-whole adjustment."

As you may know, the STB only has jurisdiction to hear rate complaints when the rate is 1.8 times greater than the railroad's variable costs for that shipment. The variable costs are calculated using URCS, so if URCS overcalculates those costs, it could mean that some rates cannot be subject to challenge when, in actuality, they should be. Put more simply, making this modification to URCS will ensure that rates that should be subject to challenge are, indeed, subject to challenge.

We also are examining interchange commitments, or paper barriers, as they are sometimes called. The Board has begun a rulemaking that would require the purchaser of a rail line with an interchange commitment to provide more information on that matter so affected shippers could more adequately assess its competitive impacts.

We're also getting a lot done outside of the realm of rate cases and competitive access.

In May of 2012, we proposed new rules to clarify liability for railcar demurrage. Conflicting decisions by the Courts of Appeal for the Third and Eleventh Circuits created uncertainty regarding the party ultimately responsible for demurrage. Under our proposal, a person receiving rail cars from a rail carrier—for either loading or unloading—who detains the cars beyond the “free time” provided in the carrier’s tariff will generally be responsible for paying demurrage if that person had actual notice of the demurrage tariff prior to railcar placement. The comment period for the proposed rules concluded last fall, and the matter is now under active consideration by the Board.

As I've mentioned to the various groups before which I've spoken, I've worked hard to emphasize alternative dispute-resolution efforts between railroads and shippers. I see the Board's role as encouraging greater cooperation—and through it more harmony—between railroads and shippers.

It is certainly better for solutions to freight disputes to come directly from parties instead of having solutions imposed upon you by the STB. A large part of my tenure has been dedicated to channeling our tremendous human resources to solving disputes before they result in formal case filings.

In this vein, I continue to encourage shippers to utilize the Board's Rail Customer and Public Assistance Program. The RCPA program is an entity within the Board designed to resolve service disputes between shippers and railroads on an informal basis, as well as provide information to stakeholders on STB law and processes. The RCPA has proven to be an invaluable resource to our stakeholders, particularly for those situations that have not risen to the level of bringing formal litigation. The best part about the program is that there is no cost to the user, and any communication made with RCPA is kept confidential—the RCPA staff only passes along your complaint to the railroad if you give it permission to do so. The RCPA staff successfully resolves a number of service disputes every year. I would encourage anyone wanting to know more about this program to check our website.

In addition to the continued success of the RCPA program, I am also happy to announce that last month the Board adopted new rules that enhance our other two Alternative Dispute Resolution processes: mediation and arbitration.

The changes to the arbitration program were the most significant. Although the Board has had an arbitration process in place since the late 1990s, it's never been used. We accordingly did away with that process and replaced it with an essentially brand-new process. Let me give you some specifics on how the new arbitration process works.

First, arbitration will be voluntary. Shippers and railroads can agree in advance to arbitrate certain types of disputes with a limit on potential liability and relief of \$200,000. The types of disputes that parties can opt to arbitrate are those involving demurrage; accessorial charges; misrouting or mishandling of rail cars; and disputes involving a carrier's published rules and practices as applied to particular rail transportation. Parties can opt in or out of the program at any time, but if they do opt out, there is a 90-day waiting period to prevent a party from opting out solely to avoid arbitrating a particular case. Parties can also arbitrate on a case-by-case basis, without opting into the overall program, or they can arbitrate issues—outside of the four I just mentioned—if they agree to do so. Parties also are free to arbitrate an issue involving more than the \$200,000, if they agree to do so. The only restriction is that parties can't arbitrate matters

in which the Board is required by statute to issue a license or authorization, or a matter involving labor protection.

The Board has already received its first request to opt in, and I'm glad to say that it was from a railroad—Union Pacific. UP has agreed to arbitrate three of the four matters we selected as proper for arbitration, including demurrage. However, for the program to be success, we will need more stakeholders to opt in. That's why, a couple of weeks ago, I sent letters to a number of shipper organizations informing them about the arbitration program and encouraging them to ask their members to consider opting in. If this is the first you've heard about the new arbitration program, I strongly encourage you to visit the STB's website and click on the "Litigation Alternatives" link. It will give all the information you will need about our arbitration process.

The main point is that there's a lot of flexibility built into this program—we really want parties to use arbitration wherever and however it's appropriate for the situation, and we want them to be able to tailor our framework to their needs.

As for our mediation process, we made a few significant changes to that, as well. In the past, the Board's rules did not permit us to refer cases to mediation, even if the dispute seemed like one in which mediation could lead to a resolution. But the new rules now allow the Board to order parties to participate in mediation, even if the parties do not agree to mediation. The Board will be able to order mediation at any time once a

procedure has been initiated. Again, the only restriction is that mediation can't be used in a proceeding in which the agency is required to grant or deny a license or authorization, or in cases involving labor protection.

Of course, shippers and railroads can still seek resolution of a dispute through formal proceedings before the Board. The cases that do go formal are often the most difficult, complex, and time-consuming. But the Board has a highly educated, highly motivated staff working through these difficult cases in an efficient but careful way.

While it has been a productive year, there are still challenges ahead. Like many federal agencies, budgets are becoming even tighter, and we are being charged to do more with less. We are fortunate in that we haven't seen a wave of retirements, despite the fact that a large portion of our workforce is eligible to retire. This is due in no small part to the fact that the STB has been named the Best Place to Work in the federal government for the past four years.

While we work on these key issues I've discussed, it's important that we conduct ourselves in a manner that is as open and transparent as possible. We will continue to hold oral arguments on important and controversial cases. We've found that doing so gives the parties and the Board a valuable opportunity to talk face-to-face before we rule on a dispute, and gives our stakeholders more insight on the Board Members' thought processes.

My goal is that the Surface Transportation Board continues to serve as an honest broker for shippers, railroads, and Congress.

We all share a common interest in preserving a national railroad system that serves our economy efficiently, expeditiously, and equitably.

While there are still serious disagreements over rates and service, there is a lot going on at the Board not only in settling these disputes, but also in enabling fair and innovative industry practices to thrive within an updated regulatory framework.

Thank you again for your gracious invitation and I would be pleased to answer any questions.