

STB Chairman Daniel R. Elliott III  
**California Short Line Railroad Association Annual Meeting**  
**August 19-20, 2013**

Thank you for your invitation to speak to you today. I appreciate the opportunity to tell you about the work that we're doing at the Surface Transportation Board.

As you know, the Board is charged with regulating 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. Our railroads are among the most well-regarded and profitable entities in this nation. Other nations marvel at their operations and achievements.

Shortline railroads have played a significant role in the resurgence of our rail industry and are a vital engine of our Nation's economic growth. The industry directly employs approximately 18,000 workers, and countless industries and communities rely on shortline railroads as their link to national and international commerce. Presently, there are about 570 shortline and switching railroads providing service over approximately 50,000 miles of track in the U.S.

Our job at the STB is to strike a balance among shippers and railroads that enables carriers to maintain economic viability while ensuring efficient, competitive, and cost-effective transportation for shippers. I want railroads to continue to earn revenues that support their substantial investment in infrastructure and to provide the most efficient, environmentally sound freight network possible. By the same token, 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.

Much has changed since the current regulatory framework was put in place in the early and mid-1980s, including the consolidation of larger railroads and the emergence of a robust shortline industry. 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. Let me tell you about some of the efforts the Board has taken in this vein.

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

Soon after the hearing was held, the Board received a petition from the National Industrial Transportation League—more commonly known as NIT-League—in which that group proposed that shippers lacking effective rail-to-rail transportation alternatives would be granted access to a competing railroad, through what is known as “reciprocal switching,” if there is a working rail interchange within 30 miles of the shipper at issue.

The Board conducted a lengthy, preliminary analysis of NIT-League’s proposal and found that, before we could rule on whether to adopt this proposal, we needed more concrete information from stakeholders about the proposal’s effect on railroad finances and operations. We then 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 for proposals on competitive-access pricing. Opening comments were filed on March 1 and replies were filed on May 30. The ASLRRA filed comments in this proceeding, raising several issues of particular concern to the short line railroad industry. We appreciate the association’s participation and its perspective. The Board is holding a hearing on this matter, as noted in an order last week. I encourage you to participate.

Our second initiative following the hearing proposed several reforms to the methods the Board applies to resolve 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.

You may recall that, a couple of years ago, the Board simplified its evidentiary procedures to provide rail customers with a lower-cost, expedited alternative to the SAC test. However, because the methodologies used in the simplified procedures are less precise than those used in the full-SAC cases, the Board capped the amount of relief available under them. Specifically, shippers could 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 high barriers to filing a rate case still remain.

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

First, the Board reasoned that in many rate disputes, there was little advantage to shippers in using the Simplified-SAC test. And since very few shippers attempted to use the Simplified-SAC approach, we considered ways to encourage shippers 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. However, to make the Simplified-SAC test more accurate, the Board made some technical changes to the methodology, specifically to the way we calculate Road Property Investment.

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 costs 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. In our new rules, we've modified the manner in which the revenue from this cross-over traffic is allocated. "Cross-over" traffic is traffic that, under the SAC test, moves on both a hypothetical railroad and real-world railroad. Despite this change, the Board is nonetheless concerned that it may be possible for parties to alter the results of the SAC test using cross-over revenue. Accordingly, we'll look more closely at the use of cross-over traffic in a future proceeding and see if there are additional changes that can be made to make our results in SAC cases more solid.

Finally, the Board changed the basis for the interest rate charged on reparations for unreasonable rates.

Despite these changes, the Board is still concerned over the fact that barriers may yet exist to grain shippers in bringing rate complaints, as none have brought a rate complaint to the agency in over 30 years, even though numerous grain shippers are captive to a single railroad.

So, as announced last month, we will begin a new proceeding this fall on rate relief for grain shippers that will seek input from interested parties on the ability of grain shippers to effectively seek relief for unreasonable rates. We'll look at proposals for modifying existing procedures, or new alternative rate relief methodologies. We appreciated receiving the views of the ASLRRA in Ex Parte 715, and we look forward to your comments in future proceedings we undertake on competition in the rail industry.

In a more technical proceeding, the Board recently proposed several changes to its key costing methodology, the Uniform Rail Costing System, also known as URCS. We're proposing to adjust the manner in which 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."

This is important because URCS enables the Board to determine a railroad's variable costs of providing rail transportation service, the jurisdictional threshold in rate disputes between railroads and their customers, and whether challenged rates are reasonable.

As you may know, the STB only has jurisdiction to hear rate complaints when the rate at issue is 1.8 times greater than the railroad's variable costs for that shipment. The variable costs are calculated using URCS, so if URCS over-calculates 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 challenged.

I know from having read the Shortline Association's comments in various proceedings that your organization is concerned about the fact that URCS is based on Class I costing information, and that if this information were used in a proceeding involving a shortline, the Board's reliance on this data could be problematic. I do understand this concern and would indeed like to consider ways to address it. However, to do so would likely require significant changes to URCS. In addition, any changes to URCS to account for shortline costs would likely require that the shortlines themselves provide such costing data, and I worry that any such attempt to collect this data could impose a burden on many shortlines. However, I do want to assure you that I am aware of this problem and have given it some thought.

I also wanted to briefly talk about the issue of interchange commitments, or paper barriers as they are more commonly known, and the proposed rules we issued last November. I know that paper barriers are a matter of particular importance to the

shortline community and that ASLRRRA participated throughout this proceeding. The Board's rules currently require that a party seeking STB authority to sell or lease a line disclose an interchange commitment in the transaction. The proposal requires a party to file additional information on the interchange commitment's impact on shippers and on the purchaser or lessee railroad. The goal of the disclosures is to encourage transactions that are in the public interest, while ensuring that we have enough information to judge whether competitive issues require a harder review.

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

In May 2012, we proposed new rules to clarify liability for railcar demurrage. Conflicting decisions by the Courts of Appeal for the 3rd and 11th Circuits created uncertainty regarding the party ultimately responsible for demurrage. Under our proposal, a party receiving rail cars from a rail carrier for 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 party has had actual notice of the demurrage tariff prior to rail-car placement. After the comment period closed, the Board published an initial regulatory flexibility analysis to provide further information and opportunity for public comment on the impact, if any, that the rules would have on small rail carriers—an action that responded, in particular, to concerns presented in ASLRRRA's comments. The Board is now awaiting the results of an industry survey being conducted by ASLRRRA and has extended the comment period so that the association can submit its report.

The Board also has a pending proceeding to define what is a “small business” for purposes of the Regulatory Flexibility Act. The Regulatory Flexibility Act is a law that requires that requires Federal agencies to consider the impact of their regulatory proposals on small businesses. The question then is what is a “small business”? In July, we proposed a new definition of “small business”. Rather than continuing to use a definition issued by the Small Business Association, the Board proposes to define “small business” as including only those rail carriers with revenues that would bring them within the definition of a Class III railroad. I know that the Shortline Association has submitted comments in that proceeding, so I cannot discuss it further, but I want to assure you that my fellow Commissioners and I will consider your comments carefully before making a final decision.

I should also mention the decision that the Board issued a decision just last week issued a decision involving fuel surcharges. In that case, a shipper had claimed that the manner in which BSNF had been calculated fuel surcharges was improper. The Board ruled in favor of BNSF. BNSF had established its fuel surcharge based on the cost of fuel set forth in an index published by the Department of Energy. Because the STB had deemed this a permissible practice in a prior decision in 2007, the Board found the railroad had acted within its rights. However, during the course of the proceeding, it became apparent that the Department of Energy’s fuel cost index may not be reflective of the railroad industry’s actual cost of purchasing fuel. Accordingly, in a few weeks, we will be

starting a new proceeding to look at the issue of how a railroad should calculate fuel surcharges more closely, including whether we should allow railroads to use this Department of Energy fuel index. Given that there may be significant differences between the Class I's and shortlines on this issue, I would encourage you to submit comments.

While I have focused on freight rail issues, I would be remiss without mentioning our recent actions in the high-speed passenger rail area. In June, we authorized the California High-Speed Rail Authority to construct a 65-mile, high-speed passenger rail line between Merced and Fresno, California, which will be the first section of the planned, statewide California High-Speed Train System. The Board's authorization is subject to environmental conditions and the condition that the High-Speed Authority build the route designated by the Federal Railroad Administration as environmentally preferable.

Initially, the question of many outside the industry was, "Why is the Board involved with a California high-speed passenger rail plan?"

Under the law, the Board has jurisdiction over transportation by rail carrier between a place in a state and a place in the same state, as long as that intrastate transportation is carried out, quote, "as part of the interstate rail network." The Board concluded that the

High-Speed Train System would be part of the interstate rail network, with its extensive connections to Amtrak intercity rail service.

In addition to our formal proceedings, I also want to take this opportunity to talk some about the Board's Alternative Dispute Resolution processes. As I've mentioned in the past, 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 and among railroads and shippers.

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

Our Rail Customer and Public Assistance Program—which we refer to as “RCPA”—has proven itself to be a worthy resource to our stakeholders, and most of you know the program's success in helping stakeholders *informally* settle disputes with their rail carrier at no cost. RCPA also serves as an information resource for our stakeholders that need information about STB processes and railroad law. The number of disputes and public informational inquiries handled by this program was around 1,400 last year. RCPA's team of skilled attorneys and industry analysts provides informal guidance on the laws,

regulations, and matters administered by the Board, and I encourage you to reach out to them and to make use of their expertise.

In addition to the continued success of the RCPA program, I'm happy to announce that, earlier this summer, the Board adopted final mediation and arbitration rules establishing a new arbitration program under which shippers and railroads may agree in advance to voluntarily arbitrate certain types of disputes—with clearly defined liability limits—in matters coming before the agency. Let me give you some specifics on how this works:

Arbitration will be voluntary, but binding. Parties such as shippers and railroads can agree in advance to arbitrate certain types of disputes with a limit on potential liability and relief of \$200,000. Parties can opt into the program at any time. Parties can also arbitrate on a case-by-case basis without opting into the overall program. Parties can also opt out, but they can't quit an arbitration they are in the middle of—it will take 90 days to release them from the program. I might add that, in mid-June, Union Pacific Railroad became the first party to opt into our new arbitration program. I have also been in touch with many in the shipping community to encourage them to opt in as well.

I understand that there may be reluctance on the part of railroads to opt into the arbitration program, as arbitration may be viewed as a process that only benefits shippers, with no upside for carriers. However, I do not believe that to be the case. In deciding which matters should be eligible for arbitration, the Board specifically selected matters

that are generally considered a nuisance to litigate by both shippers and railroads. These include disputes over demurrage, accessorial charges, misrouting or mishandling of rail cars, and application of a carrier's published rules and practices to particular rail transportation. In my discussions with carriers, these are issues that are just as much an aggravation to litigate for railroads (if not more so) as for shippers.

It should also be noted that the amount of relief that is available through arbitration is capped at \$200,000, and that arbitral decisions have no precedential value, so carriers need not worry that if they opt in, they may be leaving a decision of crucial importance to be determined through arbitration. Rather, the arbitration program is designed to resolve disputes that are individualized and limited in scope. In addition, parties can choose to opt into arbitration for only some of the four eligible matters. For example, if a carrier simply wants to arbitrate demurrage issues, but not the other three, it can opt in just for that issue.

I think that the arbitration program would be of particular benefit to the shortline industry—rather than wasting money by hiring lawyers, such as myself, you can take the money saved through arbitration and put it back into your networks.

For mediation, we made a few, similar changes. The new rules establish procedures under which the Board may order parties to participate in mediation in certain types of disputes, on a case-specific basis, even if both parties don't agree to mediation. The

Board will be able to order mediation, or grant a mutual request for mediation, at any time in an eligible proceeding.

We will appoint Board staff as mediators, unless the parties want to use a non-Board mediator. They can do that, but in that instance they'll share the costs. The Board is especially well-suited to mediate disputes because we have staff experts who understand the issues backwards and forwards, thus making each side more comfortable with the process. Not to mention that the use of Board mediators is free-of-charge to the parties!

These new rules reflect our preference for alternative dispute resolution instead of formal proceedings, wherever possible. We've even launched a new "Litigation Alternatives" webpage to the Board's website, at [www.stb.dot.gov](http://www.stb.dot.gov), for information on our activities in this area.

While we work on these many key issues, it's important that the Board conduct itself in ways that are as open and transparent as possible. We all share a common interest in preserving a national railroad system that serves our economy efficiently and expeditiously. I suspect you are all waiting to see what happens with the Short Line Railroad Rehabilitation and Investment Act, which remains pending in committee in both houses of Congress. We are watching these bills as well. Despite our proximity to Capitol Hill and our good working relationship with House and Senate committees, it can

be difficult to anticipate the pace and shape of legislative action. I'm sure you are well-aware of the recent challenges of passing major legislation.

And, of course, Congressional priorities can be affected by unanticipated events, like the tragic derailment in Lac-Megantic, Quebec. While the growth of the hydraulic fracturing industry presents an economic opportunity for the rail industry, in particular for shortline railroads with access to the Nation's shale gas formations, the transportation of steadily increasing volumes of crude oil raises potential environmental and safety issues. We are monitoring new developments closely.

In conclusion, while it's been a productive year, there are still many challenges. Like many federal agencies, budgets are becoming even tighter, and we are being charged to do more with less. The fact that the STB has been named the Best Place to Work in the federal government for the past four years has helped retain our talented workforce and aided in the recruitment of the best. I think that this speaks volumes as to the diligence and dedication of our staff.

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