

**BEFORE THE
SURFACE TRANSPORTATION BOARD**

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FINAL OFFER RATE REVIEW

INDUSTRIAL MINERALS ASSOCIATION – NORTH AMERICA COMMENTS

The Industrial Minerals Association – North America (“IMA-NA”) respectfully submits its comments in the above-captioned proceeding in accordance with the Notice of Proposed Rulemaking (“NPRM”) regarding a “Final Offer Rate Review” (“FORR”), served on September 12, 2019. In the NPRM, the Surface Transportation Board (“STB” or “Board”) proposes a new procedure for challenging the reasonableness of railroad rates in smaller cases. In this procedure, the Board would decide a case by selecting either the complainant’s or the defendant’s final offer, subject to an expedited procedural schedule that adheres to firm deadlines. IMA-NA commends the Board for taking this action to make rate cases more accessible to its members but also asks it to adopt a similar final offer rate review process without any limits on recovery over the two-year period. The Canadian rate review model has flourished with this dual rate review process with a monetary limit on the shorter procedural schedule and no monetary limit on the longer procedural schedule. This two-tiered approach

would make the rate case process available to small and large shippers alike, whereas now it is generally not available to any shippers except for coal.

IDENTITY AND INTEREST

The IMA-NA is a trade association that represents companies that mine, process and sell industrial minerals throughout North America. IMA-NA represents a wide variety of minerals in North America, including: ball clay, barite bentonite, borates, calcium carbonate, diatomite, feldspar, industrial sand, kaolin, soda ash, talc, wollastonite and other minerals. The industrial minerals produced by IMA-NA member companies are the raw material feedstock that are incorporated into a broad range of products, including among other things, containers, flat and specialty glasses, paint and coatings, ceramics, and a broad range of building products. Additionally, industrial minerals are used to make foundry molds and cores, which are in turn utilized to make metal shapes for the manufacturing of automobiles, SUVs and trucks, rail cars and almost all other items that have metal castings. The demand for many of these minerals from manufacturers is global, and the continued pressure its member companies are feeling from the railroads in the form of constant rate increases is making it more difficult to compete in that global market.

In this global market, IMA-NA has seen with certain minerals that it is now cheaper for its members' global competitors to ship via vessel from Europe and elsewhere to portions of the United States than it is for IMA-NA members to ship via rail in the United States with the skyrocketing rail rates. These unchecked rates imposed by the railroads are having a negative overall impact on the U.S. economy, and matters could get worse if they are not held accountable.

Industrial minerals are low margin, high volume products. IMA-NA member companies are heavily dependent upon a reliable and cost-effective transportation network, especially rail, and are major shippers with the major rails. To help highlight that, in 2014, the nonmetallic minerals, except fuels category, made up \$1.5 billion in total freight rail premiums.

As a result, IMA-NA has a very strong interest in having an accessible rate case process and in streamlining the market dominance process as proposed in EP 756. IMA-NA commends the Board for taking an interest in promoting policies that remove barriers to accessing regulatory protection remedies and are pleased that the Board has proposed a new rate review process.

THE BOARD'S FINAL OFFER RATE REVIEW PROPOSAL

The proposal sets forth a 135-day timeline from the filing of the complaint to the final Board decision. The discovery period would run for 21 days, and then the parties would file simultaneous submissions 14 days after discovery ends. Subsequently, simultaneous replies would be filed by the parties 10 days after the initial submissions. Finally, the Board decision would be issued 90 days after the replies. The relief as proposed would be capped at \$4 million over a two-year period.

Following discovery, as noted, the parties would simultaneously file their submissions, which would be comprised of their market dominance presentations and final offers, and each party would also submit an analysis addressing the reasonableness of the challenged rate and support for the rate in the party's offer. Each party's final offer should reflect what it considers to be the maximum reasonable rate. *See* 49 U.S.C. § 10704(a)(1). The party submitting the offer could choose how to present and support its offer, including the methodology it uses. The Board's criteria for determining rate reasonableness of and choosing between the offers would be based on its consideration of the rail transportation policy in 49 U.S.C. § 10101, the Long-Cannon factors in 49 U.S.C. § 10701(d)(2), and appropriate economic principles.

Among other aspects of the rail transportation policy, the Board would take into account the policy "to allow, to the maximum extent possible, competition and the demand for services to establish reasonable rates for transportation by rail," the policy "to maintain reasonable rates where there is an absence of effective competition and where rail rates provide revenues which exceed the amount necessary to maintain the rail system and to attract capital," and the policy "to promote a safe and efficient rail transportation system by allowing rail carriers to earn adequate revenues, as determined by the Board." 49 U.S.C. § 10101(1), (3), (6).

Furthermore, pursuant to the Long-Cannon factors, the Board would give due consideration to (i) the carrier's efforts to minimize traffic transported at revenues that do not contribute to going concern value, (ii) the carrier's efforts to maximize revenues from traffic that contributes only marginally to fixed costs, and (iii) whether one commodity is paying an unreasonable share of the carrier's overall revenues, all the while recognizing the policy that rail carriers earn adequate revenues. 49 U.S.C. § 10701(d)(2).

Finally, the Board stated that it would consider appropriate economic principles, and this general criterion would allow the Board to apply, among other things, the agency's expertise and general principles developed in its rate case precedent over decades. *See, e.g.,* R.R. Revitalization & Regulatory Reform Act of 1976 ("4R Act"), Pub. L. No. 94-210, 90 Stat. 31 (directing the ICC to "give due consideration to appropriate economic principles" in adopting new accounting system requirements relevant to its authorities); *see also Rate Guidelines -- Non-Coal Proceedings ("1996 Guidelines")*, 1 S.T.B. 1004, 1007 (1996) ("Our challenge is to reflect these economic and equitable principles, as best we can, in a practical, readily administrable test.").

As with the Board's other rate reasonableness procedures, it would consider the defendant railroad's need for differential pricing to permit it to collect adequate revenues. *See Simplified Standards for Rail Rate Cases ("Simplified Standards")*, EP 646 (Sub-No. 1), slip op. at 73 (STB served Sept. 5, 2007), *aff'd sub nom. CSX Transp., Inc. v. STB*, 568 F.3d 236 (D.C. Cir.), *vacated in part on reh'g*, 584 F.3d 1076 (D.C. Cir. 2009).

The Board explained, if a party adopts a position that is contrary to these guiding criteria, it would risk the likelihood that the Board would choose the other party's offer. In addition to the benefits of a final offer procedure with expedited time limits, most notably its bringing economy to rate cases and encouraging the parties to take reasonable positions, the Board reasoned that the criteria here—the rail transportation policy, the Long-Cannon factors, and appropriate economic principles—would allow for the parties to submit final offers using their preferred methodologies, including revised versions of the Board's existing rate review methodologies or new methodologies altogether. The Board stated that these principle-based,

non-prescriptive criteria are intended to allow for innovation with respect to rate review methodologies and that the use and creation of precedent through an adversarial process simultaneously creates incentives for methodological improvements over time (while overall complexity is constrained by procedural limitations and reasonableness is encouraged by a final offer selection structure).

The Board also stated that, if it finds that the complainant's market dominance presentation and rate reasonableness analysis demonstrate that the defendant carrier has market dominance over the transportation to which the rate applies and that the challenged rate is unreasonable, the Board would then choose between the parties' final offers. In making the rate reasonableness finding and choosing between the offers, the Board emphasized that it would take into account the criteria described above. As in the final offer procedure used as part of the Three-Benchmark methodology, this would be an "either/or" selection, with no modifications by the Board. *See Simplified Standards*, EP 646 (Sub-No. 1), slip op. at 18. The Board noted this approach would work as intended only if the parties know that the agency would not attempt to find a compromise position. *Id.* The incentives created by a final offer selection procedure could not be preserved if the Board retained the discretion to formulate its own "offer." *Id.*

Although the proposed FORR procedure is designed to apply to smaller cases, the Board asked whether it should establish different levels of relief and provide supporting rationale for such alternatives. In support of this request, the Board mentioned that final offer arbitration in Canada provides for two different procedural tracks. If the matter involves freight charges of \$2 million CAD or less (subject to an inflation adjustment), an expedited "summary" procedure of 30 days applies, and if the matter involves freight charges of greater than that amount, a longer procedure of only 60 days applies. *See Canada Transp. Act*, S.C. 1996, c. 10, as amended, § 164.1 (Can.). The Board stated it might consider an approach that, for example, would permit a complainant submitting a FORR complaint to use a longer procedure than the 135-day timeline described above if it seeks relief above the \$4 million cap. As such, the Board sought comment on the advisability of such a two-tiered relief procedure in which the top tier would

contain no limit on the size of the relief, in total, including both reparations and the two-year prescription period.

In explanation of why the FORR would be effective, the Board stated that a final offer approach could be an effective way to implement procedural limitations. Dr. Richard L. Schmalensee, Chair of the Committee for a Study of Freight Rail Transportation and Regulation of the Transportation Research Board (“TRB Committee”), recommended that the STB seek process improvements based on the final offer arbitration procedure used in Canada. See Tr. 24-25, STB Public Roundtable, Oct. 25, 2016 (emphasizing the importance of time limits and raising the idea that, among other things, the Board retain final authority over the outcome of a proceeding). The report from the TRB Committee, Nat’l Acads. Of Sciences, Eng’g, and Med., *Modernizing Freight Rail Regulation* (2015) (“*TRB Committee Report*”), also outlined several advantages of a final offer approach—for example, “[t]he imposition of time limits is intended to bring economy to the process and to ensure that shippers are not precluded from access to rate relief as a consequence of slow processing and high litigation costs,” and “the time limit in conjunction with the final-offer rule injects uncertainty into the process, which limits the likelihood that any one party will take an extreme position and encourages the settlement of disputes.” *TRB Committee Report* 138. And the Board stated in *Simplified Standards* that “[a] final offer procedure for determining the comparison group is in the public interest because it will encourage both parties to submit a reasonable comparison group. Any final tender that is skewed too far in one direction might well result in the selection of a more reasonable final tender presented by the opposing party.” *Simplified Standards*, EP 646 (Sub-No. 1), slip op. at 18; see also *U.S. Magnesium, L.L.C. v. Union Pac. R.R.*, NOR 42114, slip op. at 9-12 (STB served Jan. 28, 2010) (selecting one party’s comparison group as “more reasonable” while also recognizing that both parties’ submissions were imperfect).

By lowering the costs of litigating smaller rate cases, the Board noted that complainants with smaller rate cases, who otherwise might have been deterred from challenging a rate due to the cost of bringing a case under the Board’s existing rate reasonableness methodologies, would have a more accessible avenue for rate reasonableness review by the Board. The Board

reasoned that reduced litigation costs would make it possible for such complainants to prove meritorious cases. And, a final offer procedure may help to encourage private settlements of disputes, an outcome that was similarly suggested in the *TRB Committee Report*.

Based on this reasoning, the Board issued this FORR NPRM to establish a procedure similar to the one described by the STB Rate Review Task Force: a final offer procedure to determine rate reasonableness for smaller cases, thereby providing faster, less costly review of claims of unreasonable railroad rates. Also, the Board sought comments on whether this procedure would work for larger cases subject to a longer timeline.

RAIL RATE REVIEW HISTORY

The STB regulates the rates railroads charge shippers over which they have market dominance. 49 U.S.C. §§ 10501, 10701(d)(1). Because such captive shippers are unable to fend for themselves in the market, Congress allows them to challenge a rail rate as unreasonable before the Board, 49 U.S.C. § 10707(b)-(c), which can impose retrospective relief in the form of reparations, 49 U.S.C. § 11704(b), and prospective relief by prescribing a new rate, 49 U.S.C. § 10704(a)(1).

In 1985, the Interstate Commerce Commission (“ICC” or “Commission”), the Board's predecessor, decided to resolve rate disputes under “constrained market pricing” (CMP) principles, under which the Commission would find reasonable a rate that (1) reflects the amount a captive shipper would have to pay to receive efficient service, (2) affords the railroad adequate revenues, and (3) does so without cross-subsidizing any service or facility from which the shipper receives no benefit. *Coal Rate Guidelines, Nationwide*, 1 I.C.C.2d 520, 523-24 (1985), *aff'd sub nom. Consol. Rail Corp. v. United States*, 812 F.2d 1444 (3d Cir.1987). Under these principles, shippers able to demonstrate that the railroad has market dominance had the choice of one of several methods to prove that the challenged rates were unreasonable. They could opt to examine the railroad's entire network for revenue adequacy or management efficiency, or alternatively, they could choose to examine only a subset of the network using the “stand-alone cost” (SAC) test-the choice of almost all shippers.

A SAC case simulates a “stand-alone railroad,” a fully efficient hypothetical competitor railroad that serves the complaining shipper and other traffic sharing common facilities. *BNSF Ry. Co. v. STB*, 453 F.3d 473, 477 (D.C. Cir. 2006). A challenged rail rate is unreasonable to the extent it exceeds the costs (including a reasonable profit) of running the stand-alone railroad. *Id.* A SAC presentation thus furthers CMP principles by promoting efficiency and eliminating cross-subsidization. It accomplishes the former by forcing the railroad to bear the cost of any inefficiencies, and the latter by preventing the shipper from paying for any facilities from which it receives no benefit. Due largely to the difficulty of modeling an efficient stand-alone railroad, however, the STB stated in 2007 that this process has proven to be both expensive and time-consuming—each “full SAC” case can cost a shipper up to \$5 million to litigate. *Simplified Standards*, STB Ex Parte No. 646 (Sub-No. 1), slip op. at 31. In fact, coal companies are virtually the only shippers who deliver sufficiently large loads along fixed routes to justify using full SAC procedures. *See 1996 Guidelines*, 1 S.T.B. at 1008 n. 7 (noting “prevalence” of coal rate challenges).

Recognizing the expense of full SAC cases, the ICC soon began searching for a simplified alternative. Throughout the 1980s and early 1990s, it considered but ultimately discarded several alternatives.

By 1995, when Congress replaced the Commission with the Board, the Commission still had not settled on a simplified alternative. As a result, when Congress passed the ICC Termination Act of 1995, it gave the newly-created Board a year to “establish a simplified and expedited method for determining the reasonableness of challenged rail rates in those cases in which a full stand-alone cost presentation is too costly, given the value of the case.” Pub.L. No. 104-88, § 102(a), 109 Stat. 803, 810 (1995) (codified as amended at § 10701(d)(3)). Responding to this directive, the Board issued a set of simplified guidelines, which introduced a “three benchmark” system, *1996 Guidelines*, 1 S.T.B. at 1041, whereby the reasonableness of a challenged rate was assessed not by simulating any alternative railroad, but simply—at least as “the starting point for a rate reasonableness analysis”—by comparing it to similar existing rates, *id.* at 1022. When this approach went unused for years, the Board held hearings to find out

why. During those proceedings, shippers testified that the three-benchmark guidelines were too vague and that the question of whether a case was even eligible for resolution under the three-benchmark system was so uncertain as to require litigation. *Simplified Standards for Rail Rate Cases* (“*Simplified Standards NPRM*”), STB Ex Parte No. 646 (Sub-No. 1), at 3 (served July 28, 2006) (notice of proposed rulemaking).

In 2006, the Board issued the *Simplified Standards NPRM*, proposing (1) the retention of a slightly modified three benchmark system for the smallest cases, (2) the creation of a simplified SAC procedure more complicated than the three-benchmark system but simpler than full SAC, for use in medium-size cases, and (3) clear eligibility thresholds for each procedure. *Id.* The rule allowed each shipper to elect the three-benchmark method, simplified SAC, or full SAC for any case. To channel larger cases to SAC, the rule limited the relief available to \$1 million over five years for a three-benchmark case and \$5 million over five years for a simplified-SAC case. *Id.* at 5; *see also id.* at 27-28. This limit applied to whatever combination of retrospective and prospective relief the Board would impose. *Id.* at 28.

In 2013, the Board increased the relief available under the three-benchmark methodology and removed the relief limit on the simplified-SAC methodology, among other things, to increase their use by shippers, which had been negligible up to this point. *See Rate Regulation Reforms*, EP 715 (STB served July 18, 2013), *remanded in part sub nom. CSX Transp., Inc. v. STB*, 754 F.3d 1056 (D.C. Cir. 2014). Notwithstanding the Board’s efforts to improve its rate review methodologies and make them more accessible, only a few three-benchmark cases have ever been brought to the Board, and no complaint has been litigated to completion under the simplified-SAC methodology.

Moreover, over the last decade, non-coal carload shippers have brought numerous SAC cases to the Board to challenge their rates. The SAC process has proven to be essentially ineffective with respect to non-coal carload shippers, and the Board became increasingly frustrated with a broken process that had seemed to have run its course for all shippers except

for coal. An example of this frustration was made quite clear in one of the SAC-carload cases during this period in a dissent in 2016 by now Chairman Begeman:

While TPI filed one of the first carload traffic rate cases to be considered under the Stand Alone Cost (SAC) rate methodology, two other parties have since filed carload rate cases, lost their cases, sought reconsideration, and lost on reconsideration. In those decisions, I expressed my doubts about the SAC process, and my particular concern over whether carload traffic rates can even be judged under SAC (see Sunbelt dissent and DuPont reconsideration dissent). I cannot argue against today's finding that "TPI has not shown the challenged rates to be unreasonable under the SAC test." It remains to be seen, however, if any carload traffic shipper could make such a showing using the SAC methodology.

Although I will not oppose the ultimate finding here despite my strong reservations about SAC, and my disagreement on the market dominance approach used in this case, I cannot agree with all of the calls made in this portion of the case.

This case was filed in May 2010 and is but one example of how long the SAC rate case process can take. Therefore, it wasn't a surprise that Congress directed the Board to take actions to help expedite the SAC process in the STB Reauthorization Act of 2015. Some progress is being made. We have issued new rules to shorten rate review timelines in future SAC cases. We are also reviewing public comments that we sought at Congress's direction to assess whether procedures to expedite litigation in courts could help expedite SAC cases, in addition to other ideas to improve the SAC process.

But we need to do more than improve the Board's handling of SAC cases. Vice Chairman Miller and I are in agreement that the Board must focus its attention on finding SAC *alternatives*. Despite some economists' views that it is the "gold standard," I have yet to hear from even one rail shipper who believes the SAC methodology is a reasonable way to judge rail rates. After all, the SAC process is too costly, too time consuming, and too unpredictable.

We need to ensure that the Board's rate complaint procedures are accessible to *all* captive shippers of *all* types of commodities—whether large or small and whether shipped by unit train or carload. It may not be easy (or very fast) to ultimately develop a new approach, but it has to be a top Board priority. We finally are seeking comment on procedures that could create a new rate reasonableness methodology for use in very small disputes. We should next seek public comment on ideas for SAC alternatives, and I agree with Vice Chairman Miller that we should do so as soon as the report the Chairman commissioned in 2014 to examine alternatives for rate regulation is made public. Doing so would enable us to best fulfill the Reauthorization Act's mandate to

study and report to Congress on whether there are viable alternatives to SAC. Stakeholder input is needed in this effort.

Total Petrochemicals & Refining USA, Inc. v. CSX Transportation, Inc., NOR 42121 (STB served September 14, 2016) (dissent).

Based on this history, it is now evident that large non-coal shippers and all small shippers have nowhere to turn if they believe their rates are unreasonable. Right now, there are no rate cases being actively litigated before the Board. The Board and its shipper stakeholders are now at a crossroads. Something has to be done to comply with the intent of Congress to have a process in place that gives rail shippers protection from unreasonable rates when the railroad is market dominant.

FORR SHOULD ALSO INCLUDE AN UNCAPPED METHOD

The Board has taken a strong first step in seeking to fix this broken rate case process by proposing to streamline the market dominance approach in EP 756. Now, it must take the necessary second step by providing a rate case process that is accessible to small shippers and non-coal large shippers. The FORR with the \$4 million limit takes care of the small shippers' access to rate cases; however, the Board also needs to take care of the large shippers with no access to the Board's rate case process by implementing FORR without any monetary limits over the two years with a longer procedural schedule.

The Canadian rate case model discussed in the NPRM demonstrates that FORR will work well as a two-tiered system and will not disrupt the economic stability of the US Class I railroads. The Canadian railroads that are subject to this similar rate case process, except for the use of arbitrators as the decision makers, have flourished financially over the last decade. There can be very little dispute that the Canadian rate case final offer model that uses an even shorter timeline than the one proposed here has not adversely affected the CN and Canadian Pacific railroads' bottom line. In addition, the TRB Committee that is made up of some of the most distinguished economists in the United States proposed a similar final offer model in the *TRB Committee Report*. The economic analysis by these leading economists that led to the

recommendation of their final offer process provides further support for an uncapped FORR as an alternative to SAC. The Board has ample evidence that this model is effective and will not cause an onslaught of rate cases based on the history of this process in Canada, which has mainly led to a fair resolution of rates through negotiations between the parties and a reasonable number of cases being handled each year.

Consequently, the Board should adopt this approach using a monetary cap for cases with a shorter procedural timeline and no monetary cap for cases with a longer procedural timeline. The 135-day timeline appears to be overly long when viewed in comparison to the 30-day timeline used in Canada and the shorter timeline proposed in the Rate Reform Task Force report of 90 days. At the very least, the Board should shorten the time periods to 90 and 180 days for the capped and uncapped cases respectively.

This could be a great moment in regulatory history for the STB, by providing shippers that are subject to the market dominance of the railroads with a rate case process that actually works, does not cost millions of dollars, and occurs in a reasonable timeframe. The Board would not be taking any risk by implementing this solution because it is a proven commodity as the Canadian model has demonstrated. Therefore, IMA-NA urges the Board to take this vital step to fix a broken system.

CONCLUSION

IMA-NA thanks the Board for its attempts to fix the rate case process in this proceeding and the *Streamlined Market Dominance Process* proceeding. IMA-NA urges the Board to finalize both NPRMs with the suggested changes IMA-NA has made in its comments in these two matters. A two-tiered FORR and a more streamlined market dominance process may allow the Board to successfully regulate in the manner Congress intended.

Respectfully submitted,

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