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SERVICE DATE — APRIL 5, 2021

SURFACE TRANSPORTATION BOARD

DECISION

Docket No. EP 763

MONTANA RAIL LINK, INC.—PETITION FOR RULEMAKING—CLASSIFICATION OF
CARRIERS

Decided: March 30, 2021

AGENCY: Surface Transportation Board.

ACTION: Final Rule.

SUMMARY: The Surface Transportation Board (STB or Board) is adopting a final rule amending the thresholds for classifying rail carriers.

DATES: The rule is effective June 4, 2021.

FOR FURTHER INFORMATION CONTACT: Amy Ziehm at (202) 245-0391. Assistance for the hearing impaired is available through the Federal Relay Service at (800) 877-8339.

SUPPLEMENTARY INFORMATION: Under 49 C.F.R. part 1201, General Instructions § 1-1(a), rail carriers are grouped into one of three classes for purposes of accounting and reporting.¹ The Board's classification of rail carriers affects the degree to which they must file annual, quarterly, and other operational reports, see, e.g., 49 C.F.R.pt. 1243 and also is used in a variety of other contexts, including differentiating the legal standards and procedures that apply to certain transactions subject to Board licensing, see, e.g., 49 U.S.C. §§ 10902, 11324, 11325, and prescribing labor protection conditions, see, e.g., 49 U.S.C. §§ 10903(b)(2), 11326, among others.

The class to which any rail carrier belongs is determined by its annual operating revenues after application of a revenue deflator adjustment. 49 C.F.R. pt. 1201, § 1-1(b)(1). Currently, Class I carriers have annual operating revenues of \$504,803,294 or more, Class II carriers have annual operating revenues of less than \$504,803,294 and more than \$40,384,263, and Class III carriers have annual operating revenues of \$40,384,263 or less, all when adjusted for inflation.

¹ The agency “has broad discretion to require rail carriers to report financial and operating data, and to prescribe an underlying accounting system to produce that information.” Mont. Rail Link, Inc. & Wis. Cent. Ltd., Joint Pet. for Rulemaking with Respect to 49 C.F.R. Part 1201 (1992 Rulemaking), 8 I.C.C.2d 625, 631 (1992); see also 49 U.S.C. §§ 11144, 11145, 11161-64.

§ 1-1(a) (setting thresholds unadjusted for inflation); Indexing the Annual Operating Revenues of R.R.s., EP 748 (STB served June 10, 2020) (calculating revenue deflator factor and publishing thresholds adjusted for inflation based on 2019 data).² The revenue classification levels for railroads set forth at 49 C.F.R. part 1201, General Instructions § 1-1(a) were adopted in 1992 by the Board's predecessor, the Interstate Commerce Commission, in the 1992 Rulemaking.

Background

On February 14, 2020, Montana Rail Link, Inc. (MRL), filed a petition for rulemaking to amend the Board's rail carrier classification regulations. In its petition, MRL requested that the Board increase the revenue threshold for Class I carriers to \$900 million. (Pet. 1.) MRL contended that it continues to be a regional carrier operationally and economically but may exceed the Class I revenue threshold within two years. (*Id.*) Citing principles drawn from the 1992 Rulemaking, in which the revenue thresholds were last raised, MRL asked that the Board address "whether a regional carrier such as MRL should be treated as a Class I carrier, taking into account (1) the financial and operational differences between MRL and existing Class I carriers, and (2) the cost-benefit analysis of imposing Class I requirements on MRL." (*Id.* at 12.)

MRL submitted eight letters in support of its petition.³ No replies to MRL's petition were received.

On May 14, 2020, the Board initiated a rulemaking proceeding to consider MRL's petition and consider issues related to the Class I carrier revenue threshold determination. The Board invited "comment about whether it should amend 49 C.F.R. part 1201, General

² Instruction § 1-1(a) currently defines Class I carriers as those with annual operating revenues (in Year 1991 dollars) of \$250 million or more. To prevent this threshold from being influenced by the effects of inflation, each year the STB calculates a "deflator" factor that converts the value of today's dollar into its equivalent 1991 value. This deflator factor is then applied to a carrier's current revenues and the result is compared to the \$250 million threshold. The railroad revenue deflator formula, which is based on the Railroad Freight Price Index developed by the Bureau of Labor Statistics, is as follows: Current Year's Revenues × (1991 Average Index/Current Year's Average Index). 49 C.F.R. pt. 1201, § 1-1 Note A. The Board publishes annually an updated deflator factor. In addition, the Board applies the reciprocal of the deflator factor to identify where the \$250 million threshold lies expressed in current dollars. The current Class I revenue threshold, as noted above, corresponds to \$504,803,294 in 2019 dollars. The Class II/Class III threshold, which is listed in Instruction § 1-1(a) as \$20 million, corresponds to \$40,384,263 in 2019 dollars.

³ Letters of support were from the Montana Contractors' Association, Montana Agricultural Business Association, Montana Grain Elevator Association, Montana Petroleum Association, Inc., Montana Taxpayers Association, Montana Chamber of Commerce, Treasure State Resources Association, and Montana Wood Products Association.

Instructions § 1-1(a), to increase the revenue threshold for Class I carriers, and, if so, whether \$900 million or another amount would be appropriate.” Mont. Rail Link, Inc.—Pet. for Rulemaking—Classification of Carriers, EP 763, slip op. at 2 (STB served May 14, 2020).

The Board received two comments in response to its May 14, 2020 decision. On June 15, 2020, the American Short Line and Regional Railroad Association (ASLRRA) filed in support of MRL’s petition, arguing, among other things, that Class II carriers such as MRL are distinctly different from Class I carriers and should continue to be classified in their current category. (ASLRRA Comment 2-4, June 15, 2020.) ASLRRA stated that there is a “massive” revenue gap between the largest Class II and the smallest Class I carrier, (*id.* at 3), and that the accounting, financial, and other burdens imposed on a Class II carrier by becoming a Class I carrier would outweigh any resulting benefits, (*id.* at 2-4). Also on June 15, 2020, the Transportation Trades Department, AFL-CIO (TTD), a coalition of 33 affiliate unions, filed in opposition to MRL’s petition. Among other things, TTD raised concerns about the impact on MRL employees with respect to labor protective conditions if the Class I threshold were raised and argued that MRL had not shown that raising the threshold is appropriate or necessary. (TTD Comment 1-2, June 15, 2020.) MRL filed a reply on July 2, 2020, reiterating that its operating and financial profiles are distinct from those of the current Class I carriers (noting, for example, that in 2018 it operated only about 720 miles of mainline track, nearly all of which is in one state, whereas the smallest current Class I carrier operated 3,397 miles of track across 10 states and two countries) and that significant burdens would be imposed on MRL if the threshold is not increased, while limited, if any, benefits would accrue to the public. (MRL Reply 2, 5, July 2, 2020.)

On September 30, 2020, the Board issued a Notice of Proposed Rulemaking to amend its rail carrier classification regulations. The proposed amendments would raise the Class I revenue threshold from \$504,803,294 (as adjusted for inflation) to \$900 million and have the effect of excluding MRL and other similarly situated carriers from Class I status unless they have met the proposed revenue threshold for three years. Mont. Rail Link, Inc.—Pet. for Rulemaking—Classification of Carriers (NPRM), EP 763 (STB served Sept. 30, 2020). The Board sought comment on the proposed amendments.

Comments on the NPRM

In response to the NPRM, the Board received comments from ASLRRA on October 29, 2020, and from TTD and the National Grain and Feed Association (NGFA) on November 2, 2020. On December 1, 2020, MRL submitted its reply.

ASLRRA fully supports the Board’s proposed amendments and references and reiterates the arguments it made in support of MRL’s proposal in its June 15, 2020 comment. (ASLRRA Comment 2, Oct. 29, 2020.) According to ASLRRA, the Board’s proposal recognizes that Class II carriers, such as MRL, are operationally and financially different from Class I carriers and would enable regional railroads to continue to serve their customers efficiently. (*Id.*) ASLRRA further notes that the Board’s proposal would not deprive regional carriers of the benefit of the

Short Line Rehabilitation Tax Credit, which has provided MRL almost \$3 million per year in additional funds to invest in infrastructure, and the Railroad Industry Agreement, which provides a mechanism for short lines to work together to increase rail traffic. (Id.; ASLRRRA Comment 4, June 15, 2020.)

TTD opposes the Board's proposed amendments. (TTD Comment 1, Nov. 2, 2020.) TTD also reiterates its concern that the proposed amendments would deny employees certain protective conditions that would have otherwise applied. (Id. at 2.) TTD argues that its position in its June 15, 2020 comment was not that status quo conditions would worsen for employees, but rather that maintaining MRL's Class II status would deny employees coverage that they would otherwise be entitled to if MRL became a Class I carrier. (Id. at 2.) TTD states that the Board should give greater consideration to how the proposed amendments may impact the application of employee protective conditions. (Id.) TTD also states that it believes that MRL and the Board have failed to document the undue burden that Class I status would place on MRL, or a similar carrier. (Id.) TTD argues that MRL has provided no information that suggests that the costs of becoming a Class I carrier would be overly burdensome. (Id.) TTD requests that the Board either withdraw its NPRM or, in the alternative, alleviate only reporting/accounting burdens on MRL, instead of "permitting the evasion of protective conditions." (Id. at 3.)

NGFA does not oppose the proposed amendments but argues that the Board needs to guard against exempting Class II carriers from regulatory oversight and standards as it increases the revenue thresholds. (NGFA Comment 2-5.) NGFA states that it does not oppose increasing the Class I revenue threshold to \$900 million for freight carriers and acknowledges that MRL's petition is supported by its Montana affiliate, the Montana Grain Elevator Association. (Id. at 2.) NGFA also states that denoting MRL as a Class I carrier would make it ineligible for assistance such as the short line rehabilitation tax credits; the Federal Railroad Administration's Railroad Rehabilitation and Infrastructure Express Program, which provides funds to Class II and III carriers to repair tracks; and the Railroad Industry Agreement, which outlines ways Class I and short line carriers are allowed to collaborate to resolve issues concerning car supply, service quality, routing, and interchange requirements. (Id. at 2-3.)

Nonetheless, NGFA argues that MRL is a significant regional carrier that has a virtual monopoly on all rail traffic in the state of Montana and that MRL often exercises that market power with its customers in a manner not dissimilar from Class I carriers. (Id. at 3-4.) NGFA contends that regulatory oversight should apply to Class II carriers. (Id. at 3-5.) For example, NGFA argues that (1) simplified standards being considered by the Board for rail customers to challenge unreasonable rail rates, such as Final Offer Rate Review,⁴ should apply to Class II carriers; (2) the Board should examine whether to require larger Class II carriers like MRL to submit data sufficient to enable rail customers to analyze whether to bring a rate challenge under

⁴ The Board, in September 2019, proposed a new rate reasonableness review process that features certain attributes of a final offer selection process. See Final Offer Rate Review, EP 755 (STB served Sept. 12, 2019).

the STB's Three-Benchmark methodology; and (3) the Board should consider applying to at least Class II carriers any new rules related to reciprocal switching.⁵ (Id. at 4-5.)

In reply, MRL reasserts that it continues to function as a Class II carrier, not a Class I carrier, and requests that the Board adopt the amendments put forth in the NPRM. (MRL Reply 4, Dec. 1, 2020.) In response to TTD's argument that increasing the Class I threshold will deprive MRL employees of enhanced labor protections, MRL argues that the current level of labor protection is fair and appropriate because its operating and financial characteristics continue to be that of a Class II carrier, even with rising revenues. (Id. at 1-2 (citing Pet. 7 n.4).) MRL also argues that TTD gives no rationale to support why MRL should be excused only from the Class I accounting and reporting requirements and not the Class I labor protection requirements. (MRL Reply 2, Dec. 1, 2020.) MRL reiterates that the Class I accounting and reporting requirements would impose a significant burden on MRL, without any significant offsetting public benefit. (Id.) As to NGFA's comments about MRL having a monopoly on traffic in Montana, MRL argues it does not generally have ratemaking authority for its freight movements because BNSF Railway Company, its sole interchange partner, sets the freight transportation rates for approximately 96% of MRL's traffic, excluding switching. (Id. at 3.) MRL asserts that NGFA's argument that the Board's regulatory oversight should apply to Class II carriers is beyond the scope of this rulemaking. (Id.)

Final Rule

After considering the record, the Board agrees that MRL and any other Class II carriers that may be approaching the current revenue threshold are properly classified as regional carriers rather than as Class I carriers. The operational characteristics of regional carriers, like MRL, significantly differentiate them from Class I carriers. See NPRM, EP 763, slip op. at 4. The record establishes that even the largest Class II carriers, such as MRL, have much smaller rail networks and service territories than Class I carriers, have local or regional service territories, and lower traffic densities, (MRL Reply 3, Dec. 1, 2020; MRL Reply 2, July 2, 2020; ASLRRRA Comment 2, June 15, 2020); are heavily dependent in many critical ways on their Class I interchange partners, (ASLRRRA Comment 2, June 15, 2020); and have more limited and less diverse traffic bases than Class I carriers, (MRL Reply 2, July 2, 2020; ASLRRRA Comment 3, June 15, 2020). Similarly, even the largest Class II carriers generate far less revenue than the smallest Class I. (MRL Reply 1, July 2, 2020; ASLRRRA Comment 3, June 15, 2020.)

Based on this record, including the comments and reply received in response to the NPRM, regional carriers, such as MRL, do not possess the comparative attributes of Class I carriers. Considering the operating and financial characteristics of these carriers, it is appropriate to continue to classify these railroads as Class II carriers, rather than classifying them as Class I

⁵ The Board, in July 2016, proposed to modify its regulations governing competitive rail access, including reciprocal switching. See Pet. for Rulemaking to Adopt Revised Competitive Switching Rules (Reciprocal Switching), EP 711 (Sub-No. 1) (STB served July 27, 2016).

carriers and imposing on them the burdens associated with a Class I classification. Doing so maintains an appropriate balance between ensuring the availability of accurate cost information and avoiding imposing additional regulatory requirements on railroads when expanded regulation is not necessary; this also furthers the rail transportation policy. See 49 U.S.C. §§ 10101(2), (13). Additionally, the Board determines that \$900 million is a reasonable demarcation between Class I railroads and Class II railroads because it is sufficiently above the current Class II annual revenue level and below the revenue level of the smallest Class I carrier, maintaining an appropriate division between the two classes of carriers for the foreseeable future. See NPRM, EP 763, slip op. at 5-6. No commenter raised specific concerns with the Board's proposed \$900 million figure.

TTD's argument that the Board should not change the revenue threshold due to the impact on labor protections remains unpersuasive. (See TTD Comment 2, Nov. 2, 2020.) MRL's employees have long been subject to the labor protections applicable to Class II carriers, and that will not change as a result of this rulemaking. With respect to TTD's argument that MRL employees will be denied the additional labor protections that would be available to them if MRL were classified as a Class I carrier, the Board finds that because MRL is more appropriately classified as a Class II carrier based on its operational and financial characteristics, it is also appropriate for MRL to continue to provide the labor protections of a Class II carrier. Nothing in the record, including TTD's comments, indicates that MRL's employees are being inadequately protected today. Moreover, there is nothing that indicates that MRL's operational or financial characteristics have changed significantly as it approached the current revenue threshold.

The Board also disagrees with TTD's assertion that there is no record evidence of the undue burden that Class I status would place on MRL or similarly situated carriers. There is no question that Class I railroads face much more substantial financial reporting and accounting requirements under the Board's regulations than Class II or III railroads do. NPRM, EP 763, slip op. at 5. Among other requirements, Class I carriers must submit annual R-1 reports, see 49 C.F.R. § 1241.11, quarterly operating reports, see 49 C.F.R. pt. 1243, and service performance data, see 49 C.F.R. pt. 1250. Each of these reports, while important to the Board's regulation with regard to larger carriers, has an associated compliance burden. MRL's petition discussed the increased burden it would face complying with just a subset of the Class I reports.⁶ (Pet. 8-9; see also ASLRRRA Comment 2-4, June 15, 2020.) The NPRM also recognized that the regulatory compliance burden of a Class I designation by the Board extends beyond the Board's regulations, see NPRM, EP 763, slip op. at 5, and MRL's reply provided several examples of these regulatory impacts, including in programs administered by the Federal Railroad Administration, (MRL Reply 2-3). Moreover, as the NPRM indicated, the Board is concerned

⁶ In its petition, MRL estimated it would have to expend at least \$150,000 annually to prepare the required reports, in addition to the costs associated with converting its accounting system, training employees, and maintaining and recording the reports. (Pet. 9.)

not just with the absolute burden, but also with the relative lack of benefits associated with such reporting by carriers with MRL's characteristics. NPRM, EP 763, slip op. at 5.⁷

While NGFA does not oppose the proposed amendments, NGFA does express concern that MRL operates as a monopoly, and NGFA maintains that regulatory oversight should apply to Class II carriers. (NGFA Comment 3-5.) As a Class II carrier, MRL will continue to be subject to Board regulation and the applicable provisions of the Interstate Commerce Act, including those governing rate reasonableness and reasonable practices. NGFA's argument that specific proposed regulations, such as those related to particular rate case processes and reciprocal switching procedures, should apply to Class II carriers is beyond the scope of this proceeding.⁸

For the foregoing reasons, the Board will adopt as a final rule the amendments to its rail carrier classification regulations as proposed in the NPRM, without modification. The final rule set forth in the Appendix will raise the Class I revenue threshold to \$900 million and round the current Class II/Class III threshold to \$40.4 million. The final rule also will amend Note A to replace the 1991 Average Index with the 2019 Average Index, as the new threshold levels will be calculated in 2019 dollars.

Regulatory Flexibility Act

The Regulatory Flexibility Act of 1980 (RFA), 5 U.S.C. §§ 601-612, generally requires a description and analysis of new rules that would have a significant economic impact on a substantial number of small entities. In drafting a rule, an agency is required to: (1) assess the effect that its regulation will have on small entities; (2) analyze effective alternatives that may minimize a regulation's impact; and (3) make the analysis available for public comment. §§ 601-604. In its final rule, the agency must either include a final regulatory flexibility analysis, § 604(a), or certify that the proposed rule would not have a "significant impact on a substantial number of small entities," § 605(b).

⁷ TTD does not argue that there would be potential benefits to classifying carriers like MRL as Class Is (other than TTD's labor-related arguments addressed above). Nor has TTD made the case for its hybrid approach that would treat MRL and similar carriers as Class II railroads for accounting purposes but as Class I railroads for other purposes. As the decision indicates, there are material differences between larger Class II railroads and Class I railroads. TTD has not demonstrated that particular regulatory issues exist that would warrant ignoring these material differences.

⁸ The Board notes that NGFA has raised similar concerns in other dockets, which are currently under consideration. See, e.g., NGFA Comment 10, Nov. 12, 2019, Final Offer Rate Review, EP 755; NGFA Comment 4-5, Oct. 26, 2016, Reciprocal Switching, EP 711 (Sub-No. 1); NGFA Reply 20, Jan. 13, 2017, Reciprocal Switching, EP 711 (Sub-No. 1).

Because the goal of the RFA is to reduce the cost to small entities of complying with federal regulations, the RFA requires an agency to perform a regulatory flexibility analysis of impacts on small entities only when a rule directly regulates those entities. In other words, the impact must be a direct impact on small entities “whose conduct is circumscribed or mandated” by the proposed rule. White Eagle Coop. v. Conner, 553 F.3d 467, 480 (7th Cir. 2009).

The amendments to the Board’s regulations adopted here are intended to update the Board’s class classifications and do not mandate or circumscribe the conduct of small entities. For the purpose of RFA analysis for rail carriers subject to the Board’s jurisdiction, the Board defines a “small business” as only including those rail carriers classified as Class III rail carriers under 49 C.F.R. part 1201, General Instructions § 1-1. See Small Entity Size Standards Under the Regulatory Flexibility Act, EP 719 (STB served June 30, 2016) (with the Board Member Begeman dissenting). Here, no substantive changes are being made to the Class III threshold, as the Board is only updating the regulations to reflect the current Class III threshold in 2019 dollars (rounded) as opposed to 1991 dollars. Therefore, the Board certifies under 5 U.S.C. § 605(b) that these proposed rules, if promulgated, would not have a significant economic impact on a substantial number of small entities within the meaning of RFA.

Paperwork Reduction Act

The Board’s proposal does not contain a new or amended information collection requirement subject to the Paperwork Reduction Act of 1995, 44 U.S.C. §§ 3501-3521.

Congressional Review Act

Pursuant to the Congressional Review Act, 5 U.S.C. §§ 801- 808, the Office of Information and Regulatory Affairs has designated this rule as a non-major rule, as defined by 5 U.S.C. § 804(2).

List of Subjects

49 C.F.R. Part 1201

Railroads, Uniform System of Accounts.

It is ordered:

1. The Board adopts the final rule set forth in the Appendix to this decision. Notice of the final rule will be published in the Federal Register.

2. A copy of this decision will be served upon the Chief Counsel for Advocacy, Office of Advocacy, U.S. Small Business Administration.

3. This decision is effective on June 4, 2021.

By the Board, Board Members Begeman, Fuchs, Oberman, Primus, and Schultz.

APPENDIX

For the reasons set forth in the preamble, the Surface Transportation Board amends title 49, chapter X, part 1201 of the Code of Federal Regulations as follows:

PART 1201—RAILROAD COMPANIES

1. The authority citation for part 1201 continues to read as follows:

Authority: 49 U.S.C. 11142 and 11164

2. In subpart A, amend the General Instructions, by revising § 1-1(a) and Note A to § 1-1 to read as follows:

Subpart A—Uniform System of Accounts

GENERAL INSTRUCTIONS

1-1 *Classification of carriers.* (a) For purposes of accounting and reporting, carriers are grouped into the following three classes:

Class I: Carriers having annual carrier operating revenues of \$900 million or more after applying the railroad revenue deflator formula shown in Note A.

Class II: Carriers having annual carrier operating revenues of less than \$900 million but in excess of \$40.4 million after applying the railroad revenue deflator formula shown in Note A.

Class III: Carriers having annual carrier operating revenues of \$40.4 million or less after applying the railroad revenue deflator formula shown in Note A.

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NOTE A: The railroad revenue deflator formula is based on the Railroad Freight Price Index developed by the Bureau of Labor Statistics. The formula is as follows:

$$\text{Current Year's Revenues} \times (2019 \text{ Average Index} / \text{Current Year's Average Index})$$

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