

ENTERED
Office of Proceedings
May 8, 2019
Part of
Public Record

Before the U.S. Surface Transportation Board

STB Docket No. EP 754
Oversight Hearing on Demurrage and Accessorial Charges

Comments of the
U.S. Department of Agriculture

Greg Ibach
Under Secretary
Marketing and Regulatory Programs
U.S. Department of Agriculture
Washington, D.C. 20250

Date: May 8, 2019

Authority and Interest

The Agricultural Adjustment Act of 1938 and the Agricultural Marketing Act of 1946 charge the Secretary of Agriculture with the responsibility to represent the interests of agricultural producers and shippers in improving transportation services and facilities by, among other things, initiating and participating in Surface Transportation Board (STB or Board) proceedings involving rates, charges, tariffs, practices, and services.

Introduction

The U.S. Department of Agriculture (USDA) appreciates the Board examining the issue of demurrage and accessorial charges in its correspondence and in this public hearing. It is an important issue to the agricultural community. Many agricultural shippers are concerned with new and increasing charges and their unfair structure, which imposes steep penalties on customer performance without reciprocal penalties on railroad performance. These charges are especially perturbing during this time of disruptive change as the railroads drastically overhaul their operations.

USDA is concerned many of these charges are being unfairly applied, and that there is a lack of clarity and transparency in terms of policy and data. Recent additions to demurrage and accessorial charges raise questions of commercial fairness and reasonableness, over which clarity from the Board would be of great value. Additionally, the record for these sorts of charges is incomplete and, other than what the Board has requested for this hearing and through previous correspondence, there is limited data available to judge their reasonableness, especially if seeking to track changes in these charges over time. These comments elaborate on USDA's concerns and conclude by offering several recommendations for the Board's consideration, which would add much needed clarity and balance.

Discussion

Importance of Commercial Fairness and Reciprocity

It is worth stating from the beginning that USDA does not oppose the reasonable application of demurrage and accessorial charges. The rail network is complicated and interconnected. Therefore, there are times when delays can cause backups and impose costs on the railroad and other shippers. For the good of all, such delays should be discouraged. Thus, in certain circumstances there can be good reason to charge evenhanded accessorial and demurrage charges to encourage both shippers and railroads to use rail assets efficiently. Everyone benefits if shippers and railroads each do their part to facilitate the efficient utilization of rail assets and maximize coordination.

However, the Board has a critical role in ensuring the incentives are right for both carriers and shippers. Towards this end, USDA commends the Board for raising the issue of reciprocity in its non-docked public correspondence. While railroad documentation on demurrage and accessorial charges often provides pages upon pages of charges shippers face under a variety of scenarios, there is very little in these tariff documents concerning either the railroad's responsibility or financial repercussions from a failure on its part. Thus, the burden is largely put only on the shipper's behavior, which is one-sided and counter to the principle of commercial fairness. Furthermore, if left unchecked, this could open a window through which railroads increasingly exploit these practices to the detriment of shippers and basic fairness.

The lack of reciprocity is also contrary to economic efficiency. It is worth recognizing that no rail system will ever eliminate all delays and their associated costs, but the relevant question is about which party bears the costs of those delays.

As stated previously, demurrage and accessorial charges on shippers can be justified, to a degree, when the shipper is the party who can most readily minimize the delay, so long as such charges are based upon the practical reality of efficiently operating agricultural facilities (i.e., sufficient free time to load trains). However, the shipper is not always in that position. For instance, if the railroad is in possession of a shipper's grain-filled cars and those cars are late due to the railroad's lack of service, then a cost is inflicted on the shipper. The shipper bears the costs of time, uncertainty, and shifting markets while he waits for delivery of his grain cars. In this case, the railroad should compensate the shipper for his loss through a reciprocal fee.

It is not only an issue of properly recognizing fault, but also getting the incentives right to maximize efficient utilization of assets. As a result of competition, private companies in many other industries give refunds for late shipments. In contrast, the one-sidedness is clearly demonstrated in the lack of compensation available to shippers when delays in their operations are due to railroad inefficiencies as opposed to the heavy-handed penalties shippers face for allegedly delaying railroad operations.

Some language taken directly from one railroad's April 1, 2019 tariff offers an illustrative example. A "car day" is defined as the twenty-four-hour period "commencing 0000 hours" after the railroad places the car and continuing until the shipper releases it back. Compare that "precision" to the definition of the "service window," which is the block of time the railroad "anticipates" it will pull a customer's cars, but "these times are not guaranteed and delivery outside of these projected times will not impact the obligation to pay demurrage and storage charges." There is clearly an imbalance here in the flexibility afforded railroads compared to the down-to-the-minute strictness expected of shippers. This imbalance and similar ones appearing in current railroad tariffs could be corrected by inserting provisions that require the railroad to pay a charge, issue a credit, or waive demurrage and storage charges if the railroad does not pull the car within a certain time period after it is released.

In the same tariff, charges are calculated based on car days accrued compared to credits earned. It should be favorably noted the railroad cited now gives two credits, instead of one, for each day after the original expected time of arrival that loaded cars arrive. However, that is the only place in the tariff where the shipper is compensated for the railroad's delays.

Further, "compensated" is too generous a description, at that. On the one hand, shippers are billed if car days exceed credit days. On the other hand, charges are only "not assessed" if credit days exceed charges. If the penalty for delays was truly reciprocal, the railroad would also be credited and debited for its own performance and billed by the shipper when it has not earned enough credits that month. In general, "credit days," in many cases, do not begin to compensate agricultural rail users adequately for the actual operational and market impacts and costs incurred when carriers fail to deliver or pull loaded trains on time (e.g., the costs of having facility personnel paid overtime to unload trains that do not arrive on time; the costs of resorting to truck transportation, if available, and replacing commodities for scheduled railroad shipments that do not arrive on time; the costs of plant slowdowns or shutdowns due to late trains; the costs of lost arbitrage opportunities and revenues; etc.).

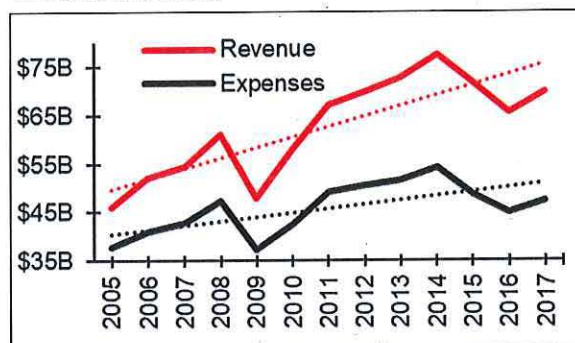
The Board should continue to emphasize the importance of commercial fairness and practicality in railroads' demurrage and accessorial charges. To better achieve that outcome, the railroads should clearly spell-out in these tariffs how they will handle issues of their own making (not the customer's), such as failure to pick-up or deliver a rail car on time beyond a reasonable time.

Unclear What Constitutes "Reasonable"

USDA is also concerned that recent demurrage and accessorial charges may go far beyond just getting the incentives right to facilitate efficient utilization of rail assets. It is possible such charges are being used by railroads for the purpose of unfairly increasing their revenues in a less than transparent manner. In a broad sense, this may be somewhat akin to the revenue enhancement measure and "double-dipping" aspects of the railroad industry's computation of fuel surcharges as a percentage of the base rates that were determined to be unreasonable practices under the STB decision in Ex Parte No. 661. USDA believes STB should investigate whether demurrage and access charges are being applied in similarly unreasonable ways, and regardless of the outcome, provide guidance to ensure their commercially-fair, reasonable, and reciprocal application.

Railroads have pushed to lower their operating ratios for over a decade, purportedly to become more efficient while increasing shareholder value. These goals are worthy in their own right but should not be prioritized over other objectives such as the railroads' common carrier obligation, customer service and fairness to rail customers. R1 data collected by STB shows while both revenues and expenses have been increasing over time, revenues have increased at a faster rate (See Figure 1). New and increasing charges mean an increasingly expensive rail system, which especially affects those with no other transportation option, such as many agricultural shippers.

FIGURE 1: OPERATING REVENUES AND EXPENSES WITH TRENDLINES



Source: Surface Transportation Board.

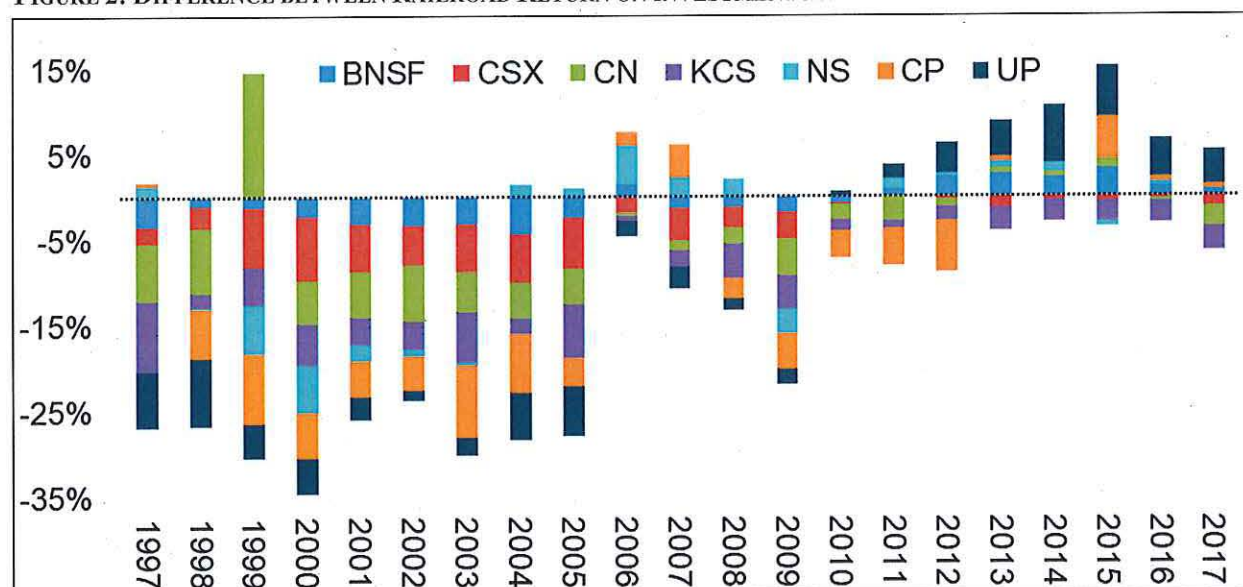
Railroads argue demurrage and access charges are about efficiency. However, in economic theory, efficiency is a broader concept than the way railroads often define it, which focuses only on reducing railroad operating costs. Efficiency in economic theory is about the weighing of costs and benefits across both sellers and buyers, firms and their customers, or in this case, railroads and shippers. In other industries, competition is the mechanism that balances those costs and benefits. In the rail industry, competition is inherently more limited, given the duopolies that exist in the Eastern and Western U.S. In recent decades, railroad consolidation, pricing power, and rail industry profitability has tipped the scales more and more in favor of railroads, with little regard for commercial fairness to shippers. As a result, there is much less assurance that business decisions adequately account for customer needs.

In terms of net social welfare, unconstrained rail pricing power is beneficial to society only to a point. This was recognized in the transportation policy established in the Staggers Act that included fairness to shippers as one of the supporting pillars of the landmark legislation. Differential pricing is the most efficient way for railroads to price above marginal cost and recoup their fixed costs. In this way, railroads are able to achieve what is generally known as revenue adequacy, whereby total costs equal their total revenues, including reasonable profits.

However, when railroads have the unconstrained ability to earn revenues beyond their total costs, the scales are no longer balanced. Beyond the revenue adequacy point, the benefits of higher prices and revenues to railroads are outweighed by the costs they impose upon shippers and society through more expensive and, ultimately, less available service.

Multiple railroads are currently well beyond revenue adequacy and have been for years (see Figure 2). If railroads are using demurrage and accessorial charges as a mechanism to raise additional revenue beyond what the STB defines as revenue adequacy, this would be inefficient from an economic standpoint and may push some shippers off rail onto other, less economical modes of transport. At worst, especially for remote shippers without alternative options, unreasonable demurrage and accessorial charges could put some of them out of business. When railroads fail to pass-on efficiency gains in the form of lower prices when already revenue adequate, this results in merely lining the pockets of railroad investors who are already earning above average rates of return. More importantly, regarding the point of economic inefficiency, the benefits to those investors are less than the costs imposed upon shippers and society in general, resulting in the few getting rich at the expense of many.

FIGURE 2: DIFFERENCE BETWEEN RAILROAD RETURN ON INVESTMENT AND COST OF CAPITAL.



Source: Surface Transportation Board. Note: CP 2015 value removed

To summarize, the issue is not that all demurrage and accessorial charges are unreasonable. With reciprocity, these types of charges can be justified to a degree. Where to draw the line on these charges is the difficult question facing the Board, but the line needs to be drawn. Through the combination of charges and rates, from an economic theory standpoint railroads are earning inefficiently high profits, and shippers are bearing the cost.

These practices raise questions for which USDA hopes the Board can provide much-needed clarity, such as:

- What guidance can the Board provide to railroads and their customers to ensure demurrage and access charges are commercially fair, are based on what rail customers

realistically and practically achieve when efficiently operating their facilities, and are reciprocal?

- How, and beyond which point, should a railroad's demurrage and accessorial charges be considered unreasonable practices?
- What sorts of recourse do shippers have available to challenge these charges?

Limited Tariff History and Data

Data provide transparency, which underpins regulatory clarity and reduces uncertainty by shedding light on contentious issues. In addition, well-structured data help regulators and stakeholders arrive at insights quickly and practically. However, at present, locating and analyzing the railroads' tariff documents, in their current format, can be slow and cumbersome. USDA believes providing this content in a more accessible and restructured format would afford the Board and its stakeholders with a better avenue for analysis than currently available, with the added benefits of equal access and more immediate insights.

Information to assess the reasonableness of demurrage and accessorial charges is quite limited. Current demurrage, accessorial, and other charge documentation is available (in the case of one Class I railroad, though, it requires those seeking such information to register and log in to its website) but requires considerable effort to make it usable and does not provide historical context. However, a full and proper inspection is not possible, given the limited tariff history railroads make available. Many railroads post only the current effective tariff with the just-expired version (or worse, only the current effective tariff), which does not easily enable shippers and others to understand and track changes over time, such as changes in amounts and new conditions.

In addition to expanding the historical coverage of tariff documents, full transparency requires these documents be usable so that any interested party can easily find and understand the tariff requirements. Currently, locating these tariff documents is a time-consuming and manual process. They are not always located in one place nor is their relationship to each other clearly understood. To that end, USDA supports the use of plain language where possible, as opposed to legalese and jargon, and methods that make the information easier to understand and act on.

To their credit, some railroads have already taken steps to do this, and USDA commends them for doing so. For instance, the Union Pacific Railroad has published a 3-page accessorial charge reference guide that succinctly provides the name or type of charge, the tariff authority where it is referenced, and the current charge. In another example, the Canadian Pacific Railway uses visual icons to indicate wording changes, price increases or decreases, and new items added. CSX Transportation provides a stand-alone document that has the sole purpose of listing the specific changes between the current and expired versions of its supplemental services tariff. These approaches help make information readily available and allow stakeholders to reach insights more quickly.

Beyond a wider historical range of tariff documents, additional data such as the revenue from accessorial and other charges are needed to fully track and assess the scope and nature of these charges. Only a subset of the data is presently available, namely "demurrage revenue" included in R-1 filings. Even if a railroad posits possible charges under certain circumstances, this does not show the full magnitude of how these penalties impact shippers. The tariffs show possible penalties, but additional data would help all parties observe their actual extent. USDA believes

these data could be captured through the addition of variables for demurrage and accessorial charges, as well as other service indicators, to the Carload Waybill Sample. Explicit separation, like what the Board did to parse out fuel surcharges beginning with the 2009 waybill, adds much needed transparency.

USDA believes the Board should encourage all railroads to make their demurrage and accessorial charge requirements more accessible and useable moving forward and provide three years of historical data (2016 – 2018) in order to provide a basis by which to judge the reasonability of recent changes. From a cost and practicality perspective, USDA does not see this as an overly-burdensome request. The more that data can be made usable, the more transparent markets become, and the more efficiently they operate.

To be most effective, data need to be as comprehensive as possible and collected at an appropriate interval. As the Board indicated in its earlier correspondence with the Class I railroads, data solely on demurrage revenue are insufficient and must be paired with revenue on other accessorial charges. Furthermore, USDA believes quarterly reporting would strike a balance between providing data at a meaningful interval without being a burden on railroads.

With such information readily available, fewer disputes may arise surrounding business practices conducted with limited transparency. Rather than conducting protracted and costly proceedings at the highest administrative levels, transparency through data ensures that judging the reasonableness of railroad practices becomes a more routine and straightforward matter for STB, shippers, and railroads alike. This is much the way data signals from a simple traffic light routinely aid the orderly flow of traffic, preventing what otherwise would deteriorate very quickly into four-way chaos.

Recommendations

USDA understands the Board has a difficult job assessing the often-contrary positions of railroads and shippers while ensuring a balance of economic fairness to both sides. A financially healthy, high-performing rail industry is important for the entire country, as is the economic health of rail customers. The Board has the difficult task of balancing the scales without tipping them too far in either direction, and USDA believes there are actions available to the Board that will provide that balance. Actions devoted to transparency, clarity, reducing uncertainty, and providing information are robust because stronger action results only in more balance.

USDA believes the Board should first focus on providing clarity to the industry on what constitutes reasonable accessorial and demurrage practices. For example, USDA believes it is patently unreasonable for shippers to be charged for problems over which they had no control. At the very least, providing clarity would help shippers better estimate their likelihood of being able to challenge demurrage and accessorial charges as being commercially unfair and non-reciprocal before the Board. In turn, railroads, too, would have a better idea of which charges would not meet this standard, and therefore hopefully would be more disciplined and cautious in implementing them in the first place.

Even then, challenging these charges is not always feasible for all shippers. The scales are certainly tipped in the favor of railroads when it comes to proving the reasonableness of accessorial charges compared to shippers proving unreasonableness. If nothing else, the reasonableness of an accessorial charge should be based on the costs of the delay. However, shippers have no way of knowing or even estimating the costs of a delay in order to assess

reasonableness. Shifting the burden of proof more onto railroads would provide more balance in these types of complaints. Doing so would not be a policy of targeting one side or the other; it would be a policy of balance by expecting each party to bring forth the information to which each has access.

In addition to providing clarity and reducing uncertainty, USDA believes STB should provide more information to the market. USDA encourages STB to continue requiring Class I railroads to submit in 2020 and future years the demurrage and accessorial charge data it has collected for this proceeding. Previous data collection efforts, such as Ex Parte No. 724 on rail performance metrics or the mandatory fuel surcharge reporting requirements in Ex Parte No. 661, have greatly benefitted industry stakeholders by providing unprecedented ease to assess the current state of rail performance and understand how the data compares across railroads and over time. Data reporting from Ex Parte No. 661 has provided the Board and the community with a transparent method to monitor fuel surcharge practices. The Board could consider requiring the railroads to provide this revenue data quarterly, similar to the reporting frequency in Ex Parte 661. These actions with respect to data on demurrage and accessorial charges would provide more transparency and balance.

It is also important to capture a sense of “what” is changing (in addition to “how much”). This requires examination of the actual tariff documents, which are often difficult to find and only available for a limited amount of time on railroad websites. To foster transparency and preserve inspection for all, USDA recommends the Board require the railroads to file their demurrage and accessorial charge tariffs for posting on the Board’s website, which should list any material changes from the prior version. Doing so enables easy one-stop access and provides a permanent record.

Finally, USDA recommends the Board add additional revenue categories (variables) for demurrage and accessorial charges to the Carload Waybill Sample, along with other service indicators, as recommended previously by the Transportation Research Board in *Modernizing Freight Rail Regulation* (2015). Coupled with the current shipment level variables in the Waybill, these additions would enable tracking these values over time, and would enable much more fine-grained analysis of the effects of these charges.

Respectfully submitted,



Greg Ibach
Under Secretary
Marketing and Regulatory Programs
U.S. Department of Agriculture
Washington, D.C. 20250