

**BEFORE THE
SURFACE TRANSPORTATION BOARD**

STB Ex Parte No. 711 (Sub-No.1)

Reciprocal Switching

**REPLY COMMENTS OF THE
ASSOCIATION OF AMERICAN RAILROADS**

ENTERED
Office of Proceedings
January 13, 2017
Part of
Public Record

Kathryn D. Kirmayer
Timothy J. Strafford
Association of American Railroads
425 Third Street, SW
Washington, DC 20024
(202) 639-2506

Samuel M. Sipe, Jr.
Anthony J. LaRocca
Steptoe & Johnson LLP
1330 Connecticut Avenue, NW
Washington, D.C. 20036
(202) 429-6486

Raymond A. Atkins
Sidley Austin LLP
1501 K Street, N.W.
Washington, DC 20005
(202) 736-8000

*Counsel for the Association of
American Railroads*

January 13, 2017

TABLE OF CONTENTS

I.	INTRODUCTION.....	1
II.	SUPPORTERS OF THE PROPOSED RULES CORROBORATE THAT THE FORCED SWITCHING PROPOSAL IS AN UNDISGUISED AND UNLAWFUL FORM OF RATE REGULATION.....	5
A.	The Supporters View the Proposed Rules Primarily as a Vehicle to Obtain Lower Rail Rates	5
B.	Section 11102(c)(1) Does Not Provide a Remedy for Shipper Rate Complaints	7
C.	The Proposed Rules Are Inconsistent with Existing Rate Reasonableness Standards	10
D.	The Proposed Rules Would Undermine Differential Pricing by Artificially Manipulating Demand for Rail Service	11
III.	IN SEEKING LOWER RATES, SHIPPERS IGNORE THE HARM TO NETWORK EFFICIENCY, SERVICE, INVESTMENT AND REVENUE ADEQUACY.	15
IV.	THE SHIPPERS' PROPOSALS FOR EXPANDING THE SCOPE OF FORCED RECIPROCAL SWITCHING ARE INAPPROPRIATE AND UNLAWFUL.....	20
A.	Definition of "Reasonable Distance"	20
B.	Existence of a Working Interchange.....	26
C.	Market Dominance	30
D.	Procedural Schedules	33
E.	Shipper Proposals on Compensation for Forced Switching.....	35
V.	CONCLUSION	40
	Appendix A: List of Letters from Public Officials Expressing Concern About Forced Switching	

**BEFORE THE
SURFACE TRANSPORTATION BOARD**

STB Ex Parte No. 711 (Sub-No.1)

Reciprocal Switching

**REPLY COMMENTS OF THE
ASSOCIATION OF AMERICAN RAILROADS**

I. INTRODUCTION

The opening comments filed by shipper interests in this proceeding do nothing to contradict the conclusion established in the rail industry's filings that the Board's proposed reciprocal switching rules are unlawful for multiple substantive and procedural reasons. The shippers accept the Board's erroneous assertion that it has unfettered discretion to proffer an interpretation of the switching provision of the statute that is a 180 degree departure from its long held interpretation. And they appear untroubled by the fact that the Board has offered nothing in the nature of a reasoned justification for its departure from its long held view of reciprocal switching. Instead of addressing the substantive merits of the Board's proposal or the soundness of its decision, the shippers embrace the proposed rules as a means of circumventing existing rate regulation standards and plead for even further expansion of the regulatory windfall that the Board has proposed.

Through their preoccupation with reciprocal switching as a vehicle for obtaining reduced rail rates, the shippers shine a spotlight on a central flaw in the Board's new conception of reciprocal switching: switching is no longer viewed by the Board as a remedy to address a market failure or an abuse of market power; instead it is viewed as a way to fulfill shippers' desire for lower rates through government intervention into railroad operations. Contrary to its

long held view, the Board proposes to offer certain favored shippers, especially those that can satisfy the Board's market dominance test, the opportunity to obtain a mandatory switching order simply because they want to be served by a second carrier and pay lower rates. Shippers are untroubled by the fact that alternative carriers have not had the economic incentive to invest in the infrastructure necessary to serve them or by the prospect of ordering the incumbent owner both to share the value of its investment with a competitor and to provide service to a competitor. These firms that so readily embrace government mandates to use private property of others for their convenience would doubtless object vehemently if they were subject to government rules requiring them to share their property with competitors and provide service to competitors.

The shippers' focus on switching as a vehicle for obtaining rate reductions highlights the unlawfulness of the Board's proposed rules. The statutory switching provision does not address the level of rail rates and cannot be used to avoid the detailed, substantive requirements of the separate statutory provisions that directly address rate regulation. Those rate regulation provisions were central to the Staggers Act and they have been central to the Board's regulation of rates on market dominant traffic ever since Staggers was enacted. The statute provides one and only one pathway for a shipper to seek regulatory intervention in response to complaints about rail rates and it sets out specific requirements that must be met.¹

To allow a shipper unhappy with rate levels to seek a rate reduction through a grant of reciprocal switching would be to evade the statute's rate reasonableness provisions. Unfortunately, in formulating its proposed reciprocal switching rules, the Board has encouraged such attempted evasions. In doing so, it has failed to adhere to the congressional directive that it rely on market forces to establish reasonable rail rates and intervene only to correct an abuse of

¹ See discussion at pages 8-10, *infra*.

market power. It has ignored the policy goal to minimize federal regulatory control over the national rail system to the maximum extent possible. It has disregarded the requirement that it promote railroad revenue adequacy and has disregarded the central role that differential pricing must play in the achievement and sustainment of revenue adequacy. Apparently emboldened by the Board's proposed rules, the shippers ignore these precepts of Staggers as well.

In their opening comments, the shippers go even further by making clear that they want the Board to expand the scope of the proposed rules by allowing "switching" at interchanges 100 miles or more from shipper facilities, so that the rules would in effect govern the prescription of many through line-haul rates.² AAR's witness Michael Baranowski showed on opening that approximately 76 percent of non-exempt carloads in the 2014 Waybill Sample data would be potentially affected by the Board's Prong 1 reciprocal switching proposal using a 10-mile distance threshold.³ The shippers' interchange proposals would further expand the number of shippers that could seek forced switching. Through this device, the shippers would also circumvent statutory limits on the prescription of through routes and would have the Board thoroughly undermine the principles governing the Board's *Bottleneck* Decisions.⁴

Without any consideration of the impact on railroads, the broader shipper community or the rail network, the commenting shippers would have the Board expand the scope of new reciprocal switching rules in other ways that are inappropriate and unlawful. The shippers suggest, without any support in the statute, regulations or case law, that railroads could be forced

² See discussion at pages 20-26, *infra*.

³ Opening Comments of the Association of American Railroads, Verified Statement of Michael R. Baranowski, *Reciprocal Switching*, STB Ex Parte No. 711 (Sub-No. 1), at 5 (filed Oct. 26, 2016) ("AAR Op.").

⁴ *Central Power & Light Co. v. S. Pac. Transp. Co.*, 1 S.T.B. 1059 (1996) ("*Bottleneck I*"), clarified, *Central Power & Light Co. v. S. Pac. Transp. Co.*, 2 S.T.B. 235 (1997) ("*Bottleneck II*"), *aff'd sub nom. MidAmerican Energy Co. v. STB*, 169 F.3d 1099 (8th Cir. 1999).

to *physically* restructure their property so that forced switching can occur in places where facilities do not currently exist to support switching.⁵ They also seek to expand the number of shippers eligible for forced switching by eliminating or watering down the requirement in Prong 2 that a shipper seeking forced switching must show that the incumbent railroad has market dominance.⁶ As to the Board's Prong 1, the shippers seek to expand its availability by effectively, and unlawfully, shifting the burden of proof to railroads to show that requests for forced switching are not in the public interest.⁷

The proposed switching rules are not a lawful exercise of the Board's statutory authority. Moreover, as AAR has observed recently in other contexts, the Board appears to have embarked on a broader program to reintroduce economically unsound regulatory controls into the rail sector. The Board's proposed switching rules themselves have no economic support and indeed would contradict sound rail economics by undermining differential pricing. Elsewhere, as noted in AAR's comments in *Expanding Access to Rate Relief*, STB Ex Parte Docket No. 665 (Sub-No. 2), the Board's pursuit of a more aggressive regulatory agenda also appears to be founded at least in part on a misunderstanding of the central importance of deregulation and demand-based differential pricing in the rail sector as enacted in the Staggers Act and reinforced by ICCTA.⁸ Regardless of the source of the impetus to expand the scope of the Board's regulatory activity, the dangers of pursuing that course should be obvious.

Unauthorized forced switching rules, which the shippers encourage here, would lead to a weakened rail sector, unable to replenish its assets and unable to grow to meet the nation's

⁵ See discussion at pages 26-29, *infra*.

⁶ See discussion at pages 29-33, *infra*.

⁷ See discussion at pages 33-35, *infra*.

⁸ Comments of the AAR, *Expanding Access to Rate Relief*, STB Ex Parte No. 665 (Sub-No. 2), at 3, 11-12 (filed Nov. 14, 2016).

economic needs or to adapt to changing market conditions. The Board should heed the rail transportation policy established by Congress to “minimize the need for Federal regulatory control over the rail transportation system” and to resort to regulation only “when regulation is required.” 49 U.S.C. § 10101(2). Accordingly, the Board’s proposed switching rules must be withdrawn.

II. SUPPORTERS OF THE PROPOSED RULES CORROBORATE THAT THE FORCED SWITCHING PROPOSAL IS AN UNDISGUISED AND UNLAWFUL FORM OF RATE REGULATION

A. The Supporters View the Proposed Rules Primarily as a Vehicle to Obtain Lower Rail Rates

The supporters of forced switching are unabashed in viewing the Board’s proposed rules primarily as a vehicle to obtain lower rail rates.⁹ For example, the Alliance for Rail Competition, *et al.*, view the use of switching as a mechanism to obtain lower rates as “entirely legitimate.”¹⁰

⁹ Although the shippers also assert that the purpose of the new switching rules proposed by the Board is “to facilitate rail-to-rail competition,” that claim is a mere pretext. *See, e.g.*, Comments Submitted by the Shipper Coalition for Railroad Competition, *Reciprocal Switching*, STB Ex Parte No. 711 (Sub-No. 1), at 2 (filed Oct. 26, 2016) (“Shipper Coalition Op.”). The shippers’ real objective is to obtain reduced rates without having to invoke the statutory rate reasonableness provisions established by Congress.

¹⁰ Opening Comments of Alliance for Rail Competition, *et al.*, *Reciprocal Switching*, STB Ex Parte No. 711 (Sub-No. 1), at 10 (filed Oct. 26, 2016) (“ARC Op.”). *See also* Comments of Diversified CPC International, Inc., *Reciprocal Switching*, STB Ex Parte No. 711 (Sub-No. 1), at 6, 11 (filed Oct. 26, 2016) (forced switching would resolve the problem of competitive rail rates and control costs) (“Diversified CPC Op.”); Comments of the Dow Chemical Company, *Reciprocal Switching*, STB Ex Parte No. 711 (Sub-No. 1), at 7 (filed Oct. 26, 2016) (“Dow Op.”) (“enhanced competition creates the potential for better service at more efficient rate levels”); Comments of Jason Tininenko, Transportation Manager, Freeport-McMoRan Inc., *Reciprocal Switching*, STB Ex Parte No. 711 (Sub-No. 1), at 7-8 (filed Oct. 26, 2016) (forced switching would resolve the “anti-competitive situation” where a “Class I carrier controls the pricing on the line haul portion of the movement, and can control who the short line railroad can interchange with and the switch fee it pays to the short line”); Comments of Shell Chemical LP, *Reciprocal Switching*, STB Ex Parte No. 711 (Sub-No. 1), at 1 (filed Oct. 26, 2016) (forced switching would improve incentives to “maintain a competitive price”) (“Shell Op.”); Comments of The Chemours Company, *Reciprocal Switching*, STB Ex Parte No. 711 (Sub-No. 1), at 1 (filed Oct. 26, 2016) (suggesting forced switching would reduce rail rates at “captive” locations).

ARC states that “[f]or many single-served shippers, the possibility of shifting their business to another railroad is the only hope the shipper has of getting reasonable rates and/or a reasonable level of service quality from the railroad they currently use.”¹¹ Many commenters are explicit regarding their dissatisfaction with pursuing reduced rates through the statutory rate reasonableness provisions. Thus, Cargill supports an expansion of forced switching because “[t]he idea that existing regulations constrain rates on captive traffic is unrealistic.”¹² And another shipper commenter asserts that “the absence of a viable competitive-switching remedy is exacerbated by what is essentially a lack of effective alternative methods of challenging unduly high rates.”¹³

In many instances, the shippers’ preoccupation with the use of switching as a vehicle to obtain reduced rates is reflected in their contention that compensation for forced switching must be cost-based or shippers would lose the benefit of forced switching. In their Verified Statement in support of the Shipper Coalition, Messrs. Crowley and Fapp argue for a cost-based compensation standard for forced switching. They contend that a methodology, such as efficient component pricing (“ECP”), that included a measure of lost contribution in the switching fee, would deprive the shipper of the benefit of the reduced rail rate it would expect to receive as a result of forced switching: “[A]pplication of ECP would prevent shippers from benefitting from

¹¹ ARC Op., at 4. While the shippers sometimes couple their pleas for reduced rates with pleas for improved service by a second carrier, the shippers fail to acknowledge that the existing competitive access rules would permit a switching remedy to address a failure of service. See *Midtec Paper Corp. v. United States*, 857 F.2d 1487, 1511-13 (D.C. Cir. 1988).

¹² Comments of Cargill, Inc., *Reciprocal Switching*, STB Ex Parte No. 711 (Sub-No. 1), at 3 (filed Oct. 26, 2016) (“Cargill Op.”).

¹³ Initial Comments of INEOS USA LLC, *Reciprocal Switching*, STB Ex Parte No. 711 (Sub-No. 1), at 2 (filed Oct. 26, 2016) (“INEOS Op.”). See also Initial Comments of Sandy Creek Energy Associates, Brazos Sandy Creek Elec. Coop., and Lower Colorado River Auth., *Reciprocal Switching*, STB Ex Parte No. 711 (Sub-No. 1), at 3 (filed Oct. 26, 2016) (same) (“Sandy Creek Op.”).

the competition provided by reciprocal switching.”¹⁴ In the same vein, Cargill asserts that “[i]f the Board were to adopt ECP, it would completely undermine the very objective of reciprocal switching by setting an access fee that effectively ensures the shipper will pay the same price for the full origin to destination movement regardless of which carrier it uses.”¹⁵ Many other shipper commenters make similar claims that switching fees need to be held to cost-based levels to assure that rate reductions result from forced switching.¹⁶

As discussed below, the shippers’ view of the proposed reciprocal switching rules as a back-door means of obtaining rate reductions is based on a fundamental misreading of the statutory scheme and is further evidence that adoption of the Board’s proposed rules would be unlawful.

B. Section 11102(c)(1) Does Not Provide a Remedy for Shipper Rate Complaints

The Board’s authority to determine in certain limited circumstances that a rail rate is unreasonably high is central to its carefully circumscribed role in the economic regulation of

¹⁴ Shipper Coalition Op., Verified Statement of Thomas D. Crowley and Daniel L. Fapp, at 29.

¹⁵ Cargill Op., at 7.

¹⁶ Dow Op., at 11 (“Absent a reasonable switch fee, reciprocal switching is a meaningless regulatory remedy”); Initial Comments of G3 Enterprises, Inc., *Reciprocal Switching*, STB Ex Parte No. 711 (Sub-No. 1), at 5 (filed Oct. 26, 2016) (“[T]he STB appears to propose a reciprocal switching fee structure that could eliminate the usefulness of the remedy of reciprocal switching”) (“G3 Op.”); INEOS Op., at 1 (access fee should be “no higher than the fully allocated costs of the incumbent railroad”); Opening Comments of National Grain and Feed Association, *Reciprocal Switching*, STB Ex Parte No. 711 (Sub-No. 1), at 16 (filed Oct. 26, 2016) (“[T]he Board should summarily reject the suggestion by Union Pacific Railroad that the incumbent railroad should be paid for lost contribution or opportunity costs if reciprocal switching is ordered”) (“NGFA Op.”); Opening Comments of Northern Indiana Public Service Co., *Reciprocal Switching*, STB Ex Parte No. 711 (Sub-No. 1), at 6-7 (filed Oct. 26, 2016) (access pricing should exclude opportunity cost and lost contribution) (“NIPSCO Op.”); Sandy Creek Op., at 13 (access fee should be limited to, at most, fully allocated cost); Joint Comments of Western Coal Traffic League and Minnesota Power, *Reciprocal Switching*, STB Ex Parte No. 711 (Sub-No. 1), at 23 (filed Oct. 26, 2016) (“[R]eciprocal switching fees . . . must be set at competitive levels for reciprocal switching to provide an effective competitive alternative”) (“WCTL/MP Op.”).

freight railroads. The contours of that authority are clearly delineated in the statute and have been carefully adhered to by the Board for the thirty-six years since Staggers was enacted. None of the Board's rate reasonableness authority resides in or derives from the reciprocal switching provision of the statute, 49 U.S.C. § 11102(c)(1).

The switching provision itself says nothing about the reasonableness of rates or the level of rates. The subject of rates, including the reasonableness of rates, the limitations on Board authority over rates, and the standards that govern rate regulation, is addressed exclusively in Title 49 U.S.C., Subtitle IV, Part A, Chapter 107.

Railroads have the discretion to establish the rates they charge in the first instance, and the authority of the Board to determine the reasonableness of a railroad-established rate cannot be invoked unless a complaining shipper makes a threshold showing of market dominance. The statute states:

(c) Except as provided in subsection (d) of this section and unless a rate is prohibited by a provision of this part, a rail carrier providing transportation subject to the jurisdiction of the Board under this part may establish any rate for transportation or other service provided by the rail carrier.

(d)(1) If the Board determines, under section 10707 of this title that a rail carrier has market dominance over the transportation to which a particular rate applies, the rate established by such carrier for such transportation must be reasonable.

49 U.S.C. §§ 10701(c), (d).

A finding of market dominance under section 10707 is a threshold determination that triggers Board jurisdiction to determine rate reasonableness but provides no indication whether or not a challenged rate is reasonable:

When the Board finds in any proceeding that a rail carrier proposing or defending a rate for transportation has market dominance over the transportation to which the rate applies, it may then determine that rate to be unreasonable if it exceeds a

reasonable maximum for that transportation. However, a finding of market dominance does not establish a presumption that the proposed rate exceeds a reasonable maximum.

49 U.S.C. § 10707(c). Thus, there are two showings that a shipper must make to establish that it is entitled to a rate reduction: (1) a threshold showing of quantitative and qualitative market dominance, and (2) a second showing that the level of the challenged rate exceeds a reasonable maximum.

The statute sets out, in 49 U.S.C. § 10701(d)(2), substantive standards bearing on the determination of rate reasonableness. The statutory standards for determining rate reasonableness have been further developed through extensive guidelines on rate reasonableness methodologies and decisions in individual rate cases issued by the agency.¹⁷ In addition to these extensive substantive standards and guidelines regarding rate reasonableness, the statute contains multiple provisions addressed to the procedures to be applied by the Board in adjudicating rate reasonableness cases.¹⁸

In short, the statute establishes standards and limitations that must be applied for a shipper to obtain reduced rail rates via a Board determination that a rate is unreasonably high. Accordingly, the court in *Midtec Paper Corp. v. United States*, 857 F.2d 1487, 1505 (D.C. Cir. 1988), rejected Midtec's argument that § 11102(c)(1) can be used as "an alternative means of obtaining rate relief." The Board has reached the same conclusion. See *Entergy Arkansas, Inc. & Entergy Services, Inc. v. Union Pac. R.R. Co.*, STB NOR Docket No. 42104, at 15 (served

¹⁷ See, e.g., *Coal Rate Guidelines, Nationwide*, 1 I.C.C.2d 520 (1985), *aff'd sub nom. Consol. Rail Corp. v. United States*, 812 F.2d 1444 (3d Cir. 1987); *Major Issues in Rail Rate Cases*, STB Ex Parte No. 657 (Sub-No. 1) (served Oct. 30, 2006), *aff'd sub nom. BNSF Ry. v. STB*, 526 F.3d 770 (D.C. Cir. 2008); *Simplified Standards for Rail Rate Cases*, STB Ex Parte No. 646 (Sub-No. 1) (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); *Total Petrochemicals & Refining USA, Inc. v. CSX Transp., Inc.*, STB NOR Docket No. 42121 (served Sept. 14, 2016).

¹⁸ See 49 U.S.C. §§ 10701, 10704, 10707.

Mar. 15, 2011) (“[T]he competitive access rules were promulgated not to provide shippers with an alternative form of rate relief, but to offer a competitive remedy where a bottleneck carrier has exploited its market power.”) (internal quotation marks omitted). And Congress has repeatedly rejected requests to transform forced switching into an alternative pathway to lower rates.¹⁹ It is not remotely plausible to contend that having established a detailed statutory rate reasonableness regime, Congress then intended to allow that regime to be circumvented by permitting shippers to pursue rate reductions through the backdoor regulatory mechanism of forced switching.

C. The Proposed Rules Are Inconsistent with Existing Rate Reasonableness Standards

Forced switching cannot be a remedy for unreasonable rates. If adopted, the Board’s proposed switching rules would undermine the existing statutory rate reasonableness regime as they would allow shippers to pursue regulatory intervention to seek reduced rates through the reciprocal switching provision of the statute without complying with the statutory standards that must be satisfied to obtain a rate reduction. Prong 1 of the Board’s proposed rules sets out no substantive standards that a shipper would have to comply with to obtain an order of forced switching. Accordingly, a shipper could qualify for a forced switching order under Prong 1 that it would use to obtain reduced rates from the incumbent or a competitor without showing that the incumbent possessed market dominance over the transportation at issue and without showing that the rate the shipper has been paying for line-haul service is unreasonably high. Under Prong 2, the shipper would have to make the threshold showing of market dominance to obtain a forced

¹⁹ See Opening Comments of Norfolk Southern Railway Co., at 43-44, *Reciprocal Switching*, STB Ex Parte No. 711 (Sub-No. 1) (filed Oct. 26, 2016) (“NS Op.”).

switching order, but it would not have to make any showing that the existing line-haul rate is unreasonably high.²⁰

Shippers do not need forced switching to obtain reduced rail rates if such relief is warranted. The statute unambiguously specifies the showings that a shipper must make to obtain a Board-ordered rate reduction. The adoption of rules that provide an alternative pathway to obtaining reduced rates that is different from and less rigorous than the pathway specified by Congress is unlawful. Fabrication of an alternative way to obtain reduced rates amounts to an end-run around the statute. The Board is not free to disregard or rewrite the statute.

D. The Proposed Rules Would Undermine Differential Pricing by Artificially Manipulating Demand for Rail Service

The use of forced switching rules as an alternative pathway to reduced rail rates would not only bypass mandatory statutory rate reasonableness standards, it would undermine the core congressional policy of differential pricing that underlies the Board's rate reasonableness standards and that makes it feasible for railroads to recover the full economic costs incurred in serving shippers. According to the statutory Rail Transportation Policy, the Board is required "to allow, to the maximum extent possible, competition and *the demand for services* to establish reasonable rates for transportation by rail." 49 U.S.C. § 10101(1) (emphasis added). When it enacted the Surface Transportation Board Reauthorization Act of 2015, Congress acknowledged that demand-based differential pricing is a central feature of the Staggers Act regulatory regime, permitting "railroads to charge lower rates to their customers who operate in a competitive

²⁰ The statute makes clear that the existence of market dominance alone is not sufficient to establish that a rate is unreasonably high. Moreover, as AAR explained in its opening comments, a finding of market dominance under the Board's standards, which exclude consideration of product and geographic competition, does not mean that there is an absence of effective competition for the traffic at issue. AAR Op., at 17.

environment and higher rates to customers who are ‘captive’ to one railroad carrier for transportation service (i.e., demand-based differential pricing).”²¹

Forced switching would achieve rate reductions by regulatory manipulation of the “demand for services” through the artificial introduction of a new rail carrier that had not made an economic decision to invest in the infrastructure necessary to serve a particular shipper facility. Congress instructed the Board to give effect “to the maximum extent possible” to market mechanisms to ensure reasonable rates, not to engineer the market so as to create artificial competitive outcomes.

It has long been recognized that the existence of shipper facilities served solely by a single rail carrier is a prominent feature of the U.S. railroad landscape and that demand for rail transportation to and from those facilities is frequently relatively inelastic. The principles of Constrained Market Pricing (“CMP”) set out in the ICC’s 1985 decision in *Coal Rate Guidelines* are premised on the agency’s understanding that all users of the rail network are better off if railroads are allowed to recover a relatively higher portion of unattributable costs from shippers with relatively inelastic demand.²² The Board’s proposed switching rules would change the conditions of demand elasticity that exist naturally in the markets served by railroads. Where market conditions have led multiple carriers or transportation modes to serve the same facility, one would expect more elastic demand for any one carrier’s service. Artificially creating multiple carrier service where market forces have dictated that only one carrier serves the facility, as the Board proposes, would force lower rates and undermine the incumbent railroad’s ability to cover its unattributable costs. As AAR explains in its discussion of differential pricing

²¹ S. Rep. No. 114-52, 114th Cong., 1st Sess., at 2 (2015).

²² The ICC explained that CMP is “a practical and economically sound method of applying competitive pricing principles to a regulatory framework.” *Coal Rate Guidelines*, 1 I.C.C.2d at 523.

in the context of compensation for switching services (pages 35-40, *infra*), the recovery of network-wide unattributable costs is essential to the creation and preservation of a financially healthy rail network.

The ICC's formulation of CMP makes clear that the freedom of carriers to engage in demand-based differential pricing is not a license to charge unreasonably high rates. CMP is intended to cap rates at maximum reasonable levels. But CMP recognizes that rail rates charged for movements to or from a sole-served facility can provide substantial recovery of unattributable costs without being unreasonably high.²³ Thus, CMP both allows and encourages differential pricing on relatively demand-inelastic traffic up to the maximum level calculated in accordance with a Board-sanctioned rate reasonableness methodology.

Shippers' preference for obtaining reduced rates through forced switching orders is based not only on their desire to avoid compliance with the standards and requirements governing rate reasonableness claims; that preference is also based on the expectation that the magnitude of a rate reduction achieved through forced switching could well be greater than that obtained through a Board-prescribed maximum reasonable rate. The shippers' argument that compensation for switching should be cost-based and should include no element of lost contribution is a prime illustration of their desire to use switching as a means to erode differential pricing, including the element of differential pricing that is economically appropriate and legally permissible under rates capped by the Board at maximum reasonable levels.²⁴ The Board's adoption of rules that would restrict differential pricing through government manipulation of market demand is

²³ The D.C. Circuit observed in *Midtec* that rate regulation under the Staggers Act "obviously does not ensure that captive shippers will pay only those rates that would obtain under 'perfect competition.'" 857 F.2d at 1507.

²⁴ See shipper comments cited in footnotes 14-16, *infra*.

contrary to the statutory requirement to allow railroads to price in accordance with market demand and the Board's long-standing commitment to differential pricing.

In its decision announcing the proposed switching rules, the Board did not address the prospect that many shippers would view forced switching as a preferable alternative means of obtaining reduced rates and one that the shippers would expect to result in a larger revenue transfer from railroads to shippers than a successful rate reasonableness claim. In light of the shippers' opening comments, that preference is now obvious.²⁵ The shipper preference provides a clear indication that the Board has veered badly off course in formulating its new proposed switching rules.

* * * * *

AAR's opening comments in this proceeding emphasized that switching that is needed to address a market failure or market abuse is switching that is "necessary to provide competitive rail service," as required by 49 U.S.C. § 11102(c)(1).²⁶ Switching that is "necessary" is a remedy, not a hand-out from a regulator. The Board stated in its July 27, 2016 decision that "[t]he purpose of ordering reciprocal switching under [Prong 2] is to encourage competition between two carriers." *Reciprocal Switching*, STB Ex Parte Docket No. 711 (Sub-No. 1), at 27 (served July 27, 2016) ("Decision"). However, an order of forced switching that is granted solely "to encourage competition between two carriers," and that is intended to yield lower rail rates is not "necessary to provide competitive rail service."

The Board's Decision setting out its proposed forced switching rules is at odds with itself regarding the purpose of a forced switching "remedy." The Board's proposal states that the shipper is required to demonstrate a "need" for forced switching. However, the objective of

²⁵ See shipper comments cited in footnote 10, *infra*.

²⁶ AAR Op., at 8-12.

“encourag[ing] competition between two carriers” through regulatory fiat is divorced from the showing of need that the Board said shippers would be required to make. *See* Decision at 19 (Under the proposed rules “shippers would be required . . . to . . . bear the burden of showing that reciprocal switching is needed. There would be no presumption of need.”). A desire to be served by a second rail carrier is not a need.²⁷ Nor is a desire to obtain reduced rates, in particular given the existence of a statutory rate reasonableness remedy.

III. IN SEEKING LOWER RATES, SHIPPERS IGNORE THE HARM TO NETWORK EFFICIENCY, SERVICE, INVESTMENT AND REVENUE ADEQUACY.

When the Board launched the original Ex Parte No. 711 proceeding, it acknowledged the importance of assessing the impact of a change in switching rules on railroads, shippers and the rail network.²⁸ But, as AAR explained in its opening comments in this proceeding, when the Board issued its Decision here it ignored the extensive evidence gathered in Ex Parte No. 711 and failed to make any independent assessment of the scope or impact of the proposed rules on the railroads it regulates or on other industry stakeholders.²⁹ The Board recognized in its Decision here that forced switching could have significant impacts on network operations and service, noting “the potential for operational challenges in gateways and terminals that are vital to the fluidity of the rail network.” Decision at 17. The Board did not, however, make any effort to assess the service degradation that would result from forced switching. Nor did the Board consider the impact of the proposed rules on the willingness and ability of railroads to invest in their networks, including the effect of the proposed rules on the ability of railroads to earn

²⁷ *See Midtec Paper Corp. v. Chicago & Northwestern Transp. Co.*, 3 I.C.C.2d 171, 174 (1986) (“*Midtec I*”), *aff’d*, *Midtec Paper Corp. v. United States*, 857 F.2d 1487 (D.C. Cir. 1988).

²⁸ *Petition for Rulemaking to Adopt Revised Competitive Switching Rules*, STB Ex Parte No. 711, at 2 (served July 25, 2012).

²⁹ *See AAR Op.*, at 29-41.

adequate revenues.³⁰ Further, the Board wholly failed to consider the cumulative impact of the proposed rules in connection with the other proposals that would expand the Board's regulatory reach beyond the path laid out by Congress for the agency in the Staggers Act, ICCTA, and the Surface Transportation Board Reauthorization Act of 2015.

As AAR explained in its opening comments, the Board is required to consider the potential adverse effects of new forced switching rules, and its failure to do so here was a fatal flaw in its decision-making process.³¹ The Rail Transportation Policy directs the Board "to promote a safe and efficient rail transportation system" and "to ensure the development and continuation of a sound rail transportation system." 49 U.S.C. §§ 10101(3), (4). Congress amended the statute in 2015 to ensure that rail carriers should be permitted to earn revenues adequate "for the infrastructure and investment needed to meet the present and future demand for rail services." 49 U.S.C. § 10704(a)(2). The Board cannot comply with these statutory mandates without examining the potential impact of expanded forced switching on railroads and the rail network.

Moreover, the case law requires that an agency consider the potential costs of new regulations. The Supreme Court recently stated that "reasonable regulation ordinarily requires paying attention to the advantages *and* disadvantages of agency decisions." *Michigan v. EPA*, 135 S. Ct. 2699, 2707 (2015) (emphasis in original). The Board failed here to consider either

³⁰ Railroads explained in their comments submitted in Ex Parte No. 711 that forced switching would undermine railroads' ability and incentive to invest in infrastructure needed to support the rail network. *See, e.g.*, Reply Comments of the AAR, Verified Statement of William J. Rennie, *Petition for Rulemaking to Adopt Revised Competitive Switching Rules*, STB Docket No. 711, at 17-33 (filed May 30, 2013); Comments of Norfolk Southern Railway Co., *Petition for Rulemaking to Adopt Revised Competitive Switching Rules*, STB Docket No. 711, at 79-80 (filed Mar. 1, 2013); Opening Comments and Evidence of Union Pacific Railroad Co., *Petition for Rulemaking to Adopt Revised Competitive Switching Rules*, STB Docket No. 711, at 67-72 (filed Mar. 1, 2013).

³¹ *See* AAR Op., at 32-33.

side of the cost-benefit analysis. It failed to consider whether any public benefits would be produced by the new rules, since a mere transfer of revenues from railroads to shippers does not confer any benefit to the public.³² In fact, a forced transfer of revenues that does not remedy a competitive harm would be contrary to the public interest since the transfer of revenues would impose substantial costs on the public from a degradation of rail service and erosion of railroads' ability and incentive to continue investing in rail infrastructure. The Board failed to consider these costs.

Shipper comments in this proceeding did nothing to rectify the complete absence of any impact evidence in this record that would support a major reversal of existing switching policy. As discussed below, the only shippers that considered the potential impact of the proposed rules—intermodal service partners who depend on a high quality rail service product—oppose the Board's rules. No other shippers made any reasoned effort to address or assess the potential impact of the proposed rules. One shipper, G3 Enterprises, argued that the revenue impact on railroads should be irrelevant.³³ Other shippers took it for granted that there would be a revenue transfer from railroads to shippers. Indeed, as noted above, the shippers appear entirely pre-occupied with the potential to use forced switching as an end-run around the statutory limitations on rate regulation and differential pricing to obtain lower rail rates. None of these shippers considered the potential impact of the resulting revenue reductions on the quality and efficiency of the rail network or the likelihood that service would be degraded for all shippers as a result of forced switching.

In contrast, the railroad filings in this proceeding contain substantial evidence about the risks and likely adverse impacts of the proposed forced switching regime. This evidence

³² See AAR Op., Verified Statement of Mark Fagan, at 1.

³³ G3 Op., at 9.

includes serious service impacts that would result from regulatory interference with carefully balanced network operations and frustration of Board approved railroad efforts to streamline their networks for efficient, single-line service.³⁴ Railroad filings also addressed deferred as well as stranded investment resulting from enhanced regulatory risk and the prospect that a railroad would be required to share facilities in which it invested with a competitor.³⁵ The Board must not give weight to this evidence, particularly in light of the complete absence of any contrary evidence by interests favoring the Board's proposed rules.

The railroads were not the only parties that expressed concern over the impact of the proposed rules on the strength and efficiency of the rail network and the Board's failure to consider the potential adverse effects of the proposed rules. Transportation companies that depend on efficient rail operations to facilitate intermodal service, like UPS and Hub Group, expressed concern that intrusive regulation of switching could lead to "decreased network velocity, diminished capital investments into the freight rail network, and deteriorating rail intermodal service levels."³⁶ Public officials at both the state and federal level expressed

³⁴ Opening Comments of CSX Transportation, Inc., Verified Statement of Michael J. Ward, at 7-8 and Verified Statement of Cindy M. Sanborn, at 2-18, *Reciprocal Switching*, STB Ex Parte No. 711 (Sub-No. 1) (filed Oct. 26, 2016) ("CSX Op."); Opening Comments and Evidence of the Kansas City Southern Railway Co., Verified Statement of Gregory Walling, at 57-61 and Verified Statement of Jeffrey M. Songer, at 6-8, *Reciprocal Switching*, STB Ex Parte No. 711 (Sub-No. 1) (filed Oct. 26, 2016) ("KCS Op."); NS Op., Verified Statement of Jeffrey H. Sliger; Opening Comments and Evidence of Union Pacific Railroad Co., Verified Statement of Thomas C. Haley, at 4-9, *Reciprocal Switching*, STB Ex Parte No. 711 (Sub-No. 1) (filed Oct. 26, 2016) ("UP Op.").

³⁵ CSX Op., Ward VS, at 8-15; KCS Op., Songer VS, at 3-6; NS Op., Verified Statement of David R. Goode, at 11-19, Verified Statement of John H. Friedman, at 2-10, and Verified Statement of Michal Grajek, at 4-6, 8-9; UP Op., Haley VS, at 10-12 and Verified Statement of Jon T. Panzer, at 7-11.

³⁶ Letter from Kenneth Buenker, and Thomas F. Jensen, UPS, *Reciprocal Switching*, STB Ex Parte No. 711 (Sub-No. 1) (filed Oct. 26, 2016); Letter from David P. Yeager, Hub Group, *Reciprocal Switching*, STB Ex Parte No. 711 (Sub-No. 1) (filed Oct. 26, 2016).

concern that forced switching could interfere with railroads' ability to meet the growing demand for transportation services and changing market conditions.³⁷ Amtrak noted its "concern that the new reciprocal switching policy may adversely impact the performance of our national network trains."³⁸ Ports, municipalities and chambers of commerce urged the Board to consider the potentially disruptive effects of forced switching on the rail network and on the many local economic interests that depend on efficient rail transportation for their own business success.³⁹ The Board cannot ignore the concerns of parties that rely on efficient rail service.

The Board appears to wrongly believe that pursuing a case-by-case approach to the impact on service of individual forced switching requests will be sufficient to avoid the worst potential harms of a forced switching regime, but this is far from the truth. As AAR pointed out in its opening comments, case-by-case analysis is wholly inadequate for assessing potential network service impacts or cumulative impacts of serial forced switching orders.⁴⁰ Nor is it

³⁷ See Appendix A listing letters from more than 32 state and federal public officials, including officials in the states of Alabama, Florida, Illinois, Kentucky, Maryland, Michigan, New York, North Carolina, Ohio, Pennsylvania, Tennessee, Virginia, and West Virginia.

³⁸ Letter from C.W. Moorman, President and Chief Executive Officer, National Railroad Passenger Corp. (Amtrak), *Reciprocal Switching*, STB Ex Parte No. 711 (Sub-No. 1) (filed Dec. 2, 2016).

³⁹ See Letter from Port of Tampa Bay, *Reciprocal Switching*, STB Ex Parte No. 711 (Sub-No. 1) (filed Oct. 31, 2016); Letter from Port of Greater Cincinnati, *Reciprocal Switching*, STB Ex Parte No. 711 (Sub-No. 1) (filed Nov. 10, 2016); Letter from the Honorable Steve Williams, Mayor, City of Huntington, *Reciprocal Switching*, STB Ex Parte No. 711 (Sub-No. 1) (filed Nov. 2, 2016); Letter from Franklin County Area Development Corp., *Reciprocal Switching*, STB Ex Parte No. 711 (Sub-No. 1) (filed Nov. 8, 2016); Letter from Harrisburg Regional Chamber & Capital Region Economic Development Corp., *Reciprocal Switching*, STB Ex Parte No. 711 (Sub-No. 1) (filed Nov. 8, 2016); Letter from Ohio Chamber of Commerce, *Reciprocal Switching*, STB Ex Parte No. 711 (Sub-No. 1) (filed Oct. 13, 2016); Letter from Hampton Roads Chamber of Commerce, *Reciprocal Switching*, STB Ex Parte No. 711 (Sub-No. 1) (filed Nov. 2, 2016); Letter from Indiana Chamber of Commerce, *Reciprocal Switching*, STB Ex Parte No. 711 (Sub-No. 1) (filed Nov. 2, 2016); Letter from Montgomery Area Chamber of Commerce, *Reciprocal Switching*, STB Ex Parte No. 711 (Sub-No. 1) (filed Nov. 8, 2016).

⁴⁰ AAR Op., at 37.

possible to evaluate the impact of an expansion of forced switching on investment decisions, service quality and infrastructure needs across the rail network in the context of individual cases, as discussed by railroads in their opening comments.⁴¹ Case-by-case litigation over the potential impact of a forced switch in a particular terminal also cannot adequately address the impact of operational uncertainty caused by a forced switching order on rail planning across a railroad's network.⁴² The problems of a case-by-case approach are only enhanced by the Board's stated intention to severely limit broader impact evidence in individual cases. *See* Decision at 18.

IV. THE SHIPPERS' PROPOSALS FOR EXPANDING THE SCOPE OF FORCED RECIPROCAL SWITCHING ARE INAPPROPRIATE AND UNLAWFUL

Notwithstanding the clear legal defects in the Board's proposed rules, most shipper commenters support the Board's proposal and argue that the Board has not gone far enough. The shippers' proposals for expanding the scope of the Board's proposed rules are obviously intended to increase the number of shippers who could obtain rate reductions through forced switching orders. Their proposals are inappropriate and unlawful.

A. Definition of "Reasonable Distance"

Under both prongs of the Board's proposed rules, a shipper seeking forced switching must show that "there is or can be a working interchange between the Class I carrier serving the party seeking switching and another Class I rail carrier within a reasonable distance of the facilities of the party seeking switching." The term "reasonable distance" was included in the National Industrial Transportation League's ("NITL") original forced switching proposal but was not defined. The Board rejected the approach proposed by NITL to use presumptions to define its "reasonable distance" proposal, noting that "bright-line cut-offs would make this [forced

⁴¹ *See, e.g.,* NS Op., at 57-58; UP Op., at 43-51.

⁴² *See* AAR Op., Rennie VS, at 12-14.

switching] remedy both over inclusive and under inclusive.” Decision at 13-14. While adopting NITL’s “reasonable distance” concept but leaving it to be determined in individual cases, the Board did not describe the factors it would consider to determine what constitutes a “reasonable distance” for a forced switch. Instead, the Board asked for comments on the “reasonable distance” requirement in the proposed rules so that the Board could consider providing “guidelines to parties that may seek switching under the proposed regulations.” *Id.* at 21.

Several shippers commented on the proposed “reasonable distance” requirement. While these commenters generally paid lip service to the Board’s proposal for a case-by-case determination of a “reasonable distance,” they urged the Board to adopt an expansive approach to defining “reasonable distance” to ensure the availability of forced switching for as large a group of shippers as possible. In furtherance of their result-oriented proposals, these shippers urged the Board to reconsider the use of presumptions and suggested several “reasonable distance” presumptions that the Board should use.

Grain shippers asked the Board to set a presumptive outer limit on forced switching at 100 miles, apparently hoping that such an outer limit would result in a presumption that forced switching distances below 100 miles would be considered reasonable. The grain shippers’ rationale for a 100-mile presumption was simply that grain shippers “need responsive alternatives” and in some areas of the country the nearest interchange point with another railroad could be 100 miles from the grain origins.⁴³ A similar result-oriented approach was advocated

⁴³ See NGFA Op., at 6-7.

by the National Mining Association, which proposed that a “reasonable distance” should be based on the distance to the nearest interchange with another railroad.⁴⁴

Coal shippers expressed concern over the possibility that the Board would interpret “reasonable distance” as a “very short distance,” which would exclude too many shippers (particularly coal shippers).⁴⁵ To avoid this result, they asked the Board to establish a presumption that 10% of the distance of a line-haul unit coal train movement would be a “reasonable distance.”⁴⁶ The proposed 10% presumption is completely arbitrary and intended only to expand the scope of new reciprocal switching rules.

The Shipper Coalition asked the Board effectively to eliminate the “reasonable distance” requirement by assuming that a forced switching order would be permitted if a shipper’s traffic that originates (or terminates) outside a terminal is currently handled by the incumbent railroad through a rail yard or terminal area where the traffic could be switched to another carrier, regardless of how far away the traffic originated.⁴⁷ The Shipper Coalition’s witnesses Messrs. Crowley and Fapp took a somewhat different approach and proposed that 100 miles should be considered to be a “reasonable distance” based on the supposedly typical operations of railroad “local” trains.⁴⁸

There is a fundamental flaw in all of these shipper proposals, which is the same flaw that invalidates the Board’s proposal to define the scope of reciprocal switching by reference to the

⁴⁴ See Comments of National Mining Association, at 2, *Reciprocal Switching*, STB Ex Parte No. 711 (Sub-No. 1) (filed Oct. 26, 2016) (e.g., a reasonable distance in Kentucky for association members would be 145 miles based on distance to nearest interchange for some mines).

⁴⁵ See WCTL/MP Op., at 16-17.

⁴⁶ *Id.*; see also NIPSCO Op., at 4-5.

⁴⁷ See Shipper Coalition Op., at 38-40.

⁴⁸ Shipper Coalition Op., Crowley/Fapp VS, at 31-32.

distance between the shipper facility and the point of the forced interchange. The statute does not authorize forced switching by reference to a “reasonable distance” between the origin or destination of the movement and an interchange point with another railroad. As the Shipper Coalition acknowledges, a *different* statutory provision governing terminal trackage rights, section 11102(a), authorizes the Board, under appropriate circumstances, to require an incumbent railroad to make available its tracks to another railroad for a “reasonable distance” outside of a terminal.⁴⁹ But the statutory provision authorizing reciprocal switching contains no such language relating to “reasonable distance.” The Shipper Coalition asserts that the Board can borrow the “reasonable distance” requirement of the terminal access statute for use in reciprocal switching cases. But the Shipper Coalition points to no authority or rationale that would justify writing into the statute a term that was not put there by Congress.

The statute permits the Board to order *reciprocal switching* under certain circumstances, so the question is what constitutes *reciprocal switching*. As AAR and its member railroads explained in their opening comments, when the precursor to section 11102(c) was adopted in 1980, the term “reciprocal switching” had a commonly understood meaning – namely, it referred to switching of traffic originating or terminating within a terminal area among railroads operating within the terminal area. Reciprocal switching was not defined by reference to the length of the movement but by reference to whether the movement occurred in a terminal area. The case law is abundantly clear on this point:

- *Railroad and Warehouse Commission of Minnesota v. Chicago Great Western Railway*, 262 I.C.C. 437, 437-38 (1945) (“It is a common custom for carriers to publish switching charges for *intraterminal* movements between industries located upon private side-tracks on their lines and the point of interchange with other carriers The switching of cars in such service is called *reciprocal switching*.”) (emphasis added)

⁴⁹ See Shipper Coalition Op., at 36.

- *Switching Charges and Absorption Thereof at Shreveport, LA*, 339 I.C.C. 65, 70 (1971) (“It has long been a common practice among the railroads to participate at *commonly served terminal areas* in what is called *reciprocal switching*.”) (emphasis added)
- *Increased Switching Charges at Kansas City, Missouri-Kansas*, 344 I.C.C. 62, 63 (1972) (“It is the practice for the railroads serving Kansas City to engage in *reciprocal switching*. This means that a carrier on whose lines an industry is located will switch cars to or from that industry as an incident to the road-haul movement of those cars by another carrier whose tracks *in the terminal area* do not extend to the industry in question.”) (emphasis added).
- *Investigation of Adequacy of Railroad Freight Car Ownership, Car Utilization, Distribution Rules and Practices*, 1 I.C.C.2d 700, 702 (1985) (“*Reciprocal switching* involves services performed by two road-haul railroads, rather than service performed by a single road-haul carrier in conjunction with a short-line or terminal railroad. The two railroads agree to participate at *commonly served terminal areas* in an arrangement under which one of the carriers acts as the switching carrier. . . .”) (emphasis added).
- *Central States Enterprises, Inc. v. ICC*, 780 F.2d 664, 675 (7th Cir. 1985) (“*Reciprocal switching* occurs at stations or terminals served by more than one carrier. A *common station or terminal area* is, therefore, a prerequisite for such switching.”) (emphasis added).

The statute authorizes the Board to order “reciprocal switching,” a term that had an established meaning when the statute was adopted. When Congress uses such a term in a statute, courts presume that Congress intended the term to have its established meaning.⁵⁰ The Board is not free now to ignore the circumstances that defined reciprocal switching when the term was first incorporated into the statute.⁵¹

⁵⁰ See *McDermott Int'l v. Wilander*, 498 U.S. 337, 342 (1991) (noting that “seaman” is a “maritime term of art” and stating “[i]n the absence of contrary indication, we assume that when a statute uses such a term, Congress intended it to have its established meaning”).

⁵¹ Proponents of forced switching have previously pointed to Canadian “interswitching” as a model that the Board could follow in the United States. See, e.g., Opening Submission of the NITL, at 25-35, *Petition for Rulemaking to Adopt Revised Competitive Switching Rules*, STB Ex Parte Docket No. 71, (filed March 1, 2013). In Canada, the scope of “interswitching” is defined by reference to distance. But interswitching rules in Canada are the product of a different statute, designed to address different historical and geographic conditions, and used in a rail market that is fundamentally different from the U.S. rail market. See generally Reply Comments of the

Restricting forced switching to movements occurring entirely within terminal areas is necessary not only to give effect to Congress's intent when the statute was adopted, but it is also necessary to distinguish forced switching orders from prescribed through routes, which are governed by different statutory provisions. Reciprocal switching orders are authorized under section 11102(c); prescription of through routes is authorized under section 10705. Section 10705(a)(2) sets limits on the prescription of a through route, including the protection of the origin carrier's right to the long haul and a respect for the origin carrier's routing preferences. Shippers seeking a prescribed through route must also comply with the existing competitive access standard set out in 49 C.F.R. § 1144.2.

If reciprocal switching under section 11102(c) were defined only by reference to an unspecified "reasonable distance" between the shipper facility and an interchange point between the incumbent and a second carrier, shippers could seek prescription of through routes under the guise of "reciprocal switching," hoping they could convince the Board to accept their version of a "reasonable distance" in any given case. Indeed, the shippers' requests that the Board adopt some version of reasonable distance that would allow forced switching well beyond the boundaries of terminals show that their true goal is to achieve the prescription of through routes.

But through route prescriptions are subject to the conditions set out in section 10705(a)(2) regardless of the distance between the facility at issue and the prescribed interchange. Through route prescriptions of a relatively short distance must comply with the long-haul and origin-carrier protections under section 10705(a)(2) the same as through route

AAR, Reply Verified Statement of Phil C. Ireland and Rodney E. Case, at 11-26, *Petition for Rulemaking to Adopt Revised Competitive Switching Rules*, STB Ex Parte Docket No. 711 (filed May 30, 2013). Canadian law and experience are irrelevant in defining a term – reciprocal switching – that had a specific meaning in the United States when the term was adopted into the governing statute.

prescriptions of a long distance. Section 10705(a)(2)(A) sets out an exception to the long-haul and origin-carrier protections for switching orders under section 11102(c). But this limited carve-out for forced switching reflects Congress's recognition of an operational and geographic difference between forced switching under section 11102(c) and through route prescription under section 10705(a)(2). And as discussed above, the case law unambiguously shows that reciprocal switching, the subject of section 11102(c), is a distinct type of rail operation – reciprocal switching refers to switch movements for industries located within commonly served terminal areas. While determining what constitutes a terminal area is fact specific, once a terminal area is identified in a particular case, its boundaries define the scope of activity that is understood to be reciprocal switching, not the distance of the forced switch movement.

Therefore, reciprocal switching can be required only within commonly served terminal areas for movements originating or terminating within the terminal area (and only if other requirements, such as “need,” are satisfied) without specifically addressing the statutory and regulatory limitations applicable to prescription of through routes. But for other interchange movements, regardless of the distance between the shipper facility and an interchange point, the requirements of section 10705(a)(2) and 49 C.F.R. § 1144.2 must be met before an interchange can be prescribed. Further, as discussed below, the Board's *Bottleneck* Decisions set out rules limiting shippers' rights to demand segment rates on a rail carrier's bottleneck segments. Those rules cannot be evaded for movements over bottleneck segments that extend beyond the boundaries of terminal areas.

B. Existence of a Working Interchange

The Board's proposed rules also require that there “is or can be a working interchange” between the incumbent and another Class I rail carrier. The Board explains that this requirement will be satisfied if the incumbent and the other Class I rail carrier currently engage in switching

operations at the proposed interchange point. If there are no current switching operations at the proposed interchange point, the Board would still determine that there “can be” a working interchange if “the infrastructure currently exists to support switching.” Decision at 21. The Board would not impose a forced switch in the absence of infrastructure that would be needed to support the switching activity.

Several shipper commenters took issue with the Board’s proposed requirement that the infrastructure necessary to support switching operations must currently exist. WCTL/MP argued that railroads can and should be required to make infrastructure investments necessary to support forced switching if such investments are “in the public interest.”⁵² They point to no statutes, regulations or case law to support such authority, nor acknowledge the negative effects of diverting capital from market-driven investments to government-mandated construction projects. Indeed, the Shipper Coalition took the opposite position from WCTL/MP, acknowledging that railroads could not be forced to fund infrastructure investments to facilitate switching operations.⁵³ But the Shipper Coalition argued, without any statutory, regulatory or case law support, that an incumbent railroad could be forced to make the infrastructure investments (or allow them to be made on the incumbent’s property) if a shipper or alternative railroad paid for them.⁵⁴ Several other commenting shippers similarly argued that the Board should allow forced switching if the shipper or alternative railroad agrees to pay for facilities necessary to support the switching operation.⁵⁵

⁵² WCTL/MP Op., at 14.

⁵³ Shipper Coalition Op., at 40-41.

⁵⁴ *Id.*

⁵⁵ *See, e.g.*, NGFA Op., at 8; NIPSCO Op., at 6; Shell Op., at 2; Cargill Op., at 10.

The shippers' suggestion that the Board could order a *physical* restructuring of a railroad's property to accommodate a forced switching order is clear evidence of the shippers' improper view of access as a tool to restructure the rail industry. As AAR explained in its opening comments, the ICC and the courts have already determined that Congress did not intend for the statutory access provisions to be used to restructure the rail industry, but rather as a remedy for specific competitive or service problems.⁵⁶ Not only do the shippers want to override market forces and create artificial competition through forced switching, they want the Board to dictate how an incumbent railroad must reconfigure its facilities to accommodate the creation of artificial competition. The shippers' proposal would constitute a massive regulatory intrusion, contrary to the statutory directive to minimize regulation, and it would result in extensive, complex litigation in each and every case.

The issue is not merely who pays the costs of new facility construction, although WCTL/MP's argument that incumbent railroads can be forced to pay for facilities that will be used by competitors to take business away from the incumbent is preposterous on its face. Regardless of who pays, nothing in the statute authorizes the Board to order a railroad to physically restructure its property, or to allow other parties to use the railroad's property to support the other party's operations. The statute authorizes the Board under certain conditions to order a railroad to perform reciprocal switching. The statute *does not* authorize the Board under any conditions to take a railroad's property, even with compensation, to support a forced restructuring of rail operations.

⁵⁶ See AAR Op., at 10-12.

NGFA claims that “competitive access” has been ordered by the Board in crossing cases where an incumbent railroad is forced to allow a crossing of its property.⁵⁷ But the narrow and specific focus of 49 U.S.C. § 10901(d) on *crossings* shows the limits on the Board’s authority to forcibly take a railroad’s property to support other railroads’ operations. Unlike crossings, there is no statutory provision that empowers the Board to order construction to support a forced switch. Moreover, what the shippers seek here goes far beyond a crossing of the incumbent’s existing line. The shippers want to forcibly restructure a railroad’s property to allow access by another carrier to the railroad’s traffic. Not only could the forced restructuring result in the loss of the business that is subject to the forced switching order, it could keep the incumbent railroad from using its property to advance other business opportunities. For example, the construction of new facilities in an incumbent railroad’s yard by the shipper or competitor railroad would take the incumbent’s property and impede the incumbent from using its own property for other purposes, including expanding its own operations.⁵⁸ Particularly in crowded urban areas, a rail landowner’s loss of the opportunity to use its property for its own business purposes could impose enormous economic costs. By having its property diverted for use by others, the railroad would forfeit substantial revenues that could have been generated by using the property to advance its own business. For strong policy and fairness reasons, Congress has not authorized the Board to take a railroad’s property to support forced switching.

⁵⁷ See NGFA Op., at 16 (referring to *Omaha Public Power District—Petition Under 49 U.S.C. 10901(d)*, 1996 WL 428901 (served August 1, 1996)).

⁵⁸ The courts have recognized that such a taking of railroad property could interfere with a railroad’s current and future operations. See *Union Pac. R.R. Co. v. Chicago Transit Auth.*, 647 F.3d 675, 681 (7th Cir. 2011).

C. Market Dominance

Prong 2 of the Board's proposed rules is intended to implement the statutory language authorizing a reciprocal switching order if "necessary to provide competitive rail service." The basic requirement under the Board's Prong 2 proposal is that the proponent of a forced switching order must demonstrate that it is served by a single rail carrier and that "intermodal and intramodal competition is not effective with respect to the movements of the shipper(s) and/or receivers(s) for whom switching is sought." See proposed rule 1145.2(a)(2)(i) and (ii). The Board explains that it would perform a market dominance analysis under existing standards used in rate reasonableness cases to determine whether effective competition exists for the movement at issue. Decision at 22.

AAR explained in its Opening Comments that a forced switching order cannot lawfully be based on the conditions specified in the Board's Prong 2, namely the mere showing that the shipper whose traffic would be subject to the order is served by a single carrier with market dominance over the movement. Access remedies were not established by Congress as a remedy for the *condition* of being a shipper served by a single rail carrier, which was a common condition at the time of the Staggers Act. Access was intended to be a remedy for abuses of market power by railroads. Moreover, a threshold showing of market dominance may be indicative of the existence of market power in some cases, but it is not determinative on this question because the Board excludes consideration of product and geographic competition in determining market dominance. A showing of market dominance also says nothing about whether a railroad has abused any market power it may have.⁵⁹

⁵⁹ See AAR Op., at 16-17.

A number of shipper commenters ask the Board to eliminate altogether the requirement that the proponent of a forced switching order show market dominance and require only that a shipper be served by a single railroad.⁶⁰ These shippers make no effort to hide their improper objective to use forced switching to restructure the rail industry to artificially create multi-carrier competition wherever there is only one railroad serving a shipper, and thereby seek lower rates. As the Board itself noted in the Decision, “[t]here is no indication that Congress intended the agency to prescribe reciprocal switching whenever it would enhance competition.” Decision at 15 (citing *Midtec*, 857 F.2d at 1507).

A common theme in all shippers’ comments regarding market dominance is that a market dominance showing under existing standards would create evidentiary burdens that could discourage requests for forced switching. While several shippers ask the Board to look for ways to simplify the market dominance showing, none presents a viable simplified approach. Some shippers vaguely suggest that the Board could develop presumptions that can simplify the presentation of market dominance evidence. But the few specific presumptions proposed by these shippers, like those proposed earlier by NITL, are misguided and inappropriate. For example, NGFA proposes that market dominance can be presumed if the rate on the movement at issue produces an R/VC exceeding 180%, directly contrary to section 10707(d)(2) of the statute which prohibits such a presumption.⁶¹ Similarly, WCTL/MP proposes that market dominance can be presumed for coal shipments over 50 miles if the incumbent has handled more than 95% of the traffic for the last five years, ignoring the very real possibility that a shipper’s repeated use of a particular carrier could be the result of satisfaction with that carrier’s service,

⁶⁰ See, e.g., ARC Op., at 10; Diversified CPC Op., at 8; G3 Op., at 5; Comments of Highroad Consulting, Ltd., at 10, *Reciprocal Switching*, STB Ex Parte No. 711 (Sub-No. 1) (filed Oct. 26, 2016); INEOS Op., at 9; NGFA Op., at 11; Sandy Creek Op., at 10; WCTL/MP Op., at 4.

⁶¹ See NGFA Op., at 11.

not the lack of competitive alternatives.⁶² Although the AAR opposes the use of market dominance as a litmus test for a forced switching order under Prong 2, the Board was right to reject the use of simple presumptions to assess market dominance.

The Shipper Coalition and a few other shipper commenters accept the Board's proposed requirement of market dominance under Prong 2, but they argue that the market dominance analysis should be carried out only with respect to the "bottleneck" portion of the movement handled by the incumbent railroad, which may be less than the through movement.⁶³ Once again, the Shipper Coalition's proposal rests on a fundamental misunderstanding of the reciprocal switching statute. The Shipper Coalition asserts that "the very point of reciprocal switching is to create competition for the incumbent carrier's monopoly [i.e., 'bottleneck'] segment."⁶⁴ To the contrary, the courts have made it clear that the objective of forced switching is not to create artificial competition.⁶⁵ The Board, in the *Bottleneck* cases,⁶⁶ expressly rejected shipper claims that the access provisions in the statute could be used to create competitive alternatives to a rail carrier's control of a "bottleneck" over certain rail lines. The Board concluded that statutory provisions, including the statutory protection of an origin carrier's long-

⁶² See WCTL/MP Op., at 20.

⁶³ See Shipper Coalition Op., at 43-45.

⁶⁴ *Id.* at 44.

⁶⁵ See *Midtec*, 857 F.2d at 1507 ("We have not found even the slightest indication that Congress intended the Commission in this way to conform the industry more closely to a model of perfect competition.") (citing *Baltimore Gas & Elec. v. United States*, 817 F.2d 108, 115 (D.C. Cir. 1987)).

⁶⁶ See *Bottleneck* case citations at footnote 4 above.

haul, precludes the artificial creation of competition over a railroad's "bottleneck" segments except under very limited circumstances.⁶⁷

Forced switching cannot be used, as the Shipper Coalition wishes, to circumvent the statutory and policy-based limits in the *Bottleneck* cases on access to a rail carrier's bottleneck segments. As AAR explained on opening, reciprocal switching is intended to be used as a remedy for the abuse of an incumbent rail carrier's market power, including possible abuse of market power over a rail carrier's bottleneck segments, and not as a vehicle for creating artificial competition.

D. Procedural Schedules

The Board's proposed rules do not address the matter of the procedural schedule for reciprocal switching cases and the Board did not request comments on procedural issues.⁶⁸ Nevertheless, some shippers asked the Board to adopt highly detailed procedures to govern reciprocal switching cases, including discovery procedures, the sequence and schedule of evidentiary filings, and rules that would govern parties' respective burdens of proof.⁶⁹

It would be premature to address the procedural issues raised by these shippers. The Board has proposed to rely on case-by-case adjudication of forced switching requests under broad and open-ended standards. The Board rejected NITL's presumption-based approach in favor of standards that would need to be developed over time in individual cases. Given the

⁶⁷ See *Bottleneck I*, at 1067 ("Congress chose not to provide for the open routing that shippers seek here. To the contrary, as discussed above, Congress retained and strengthened the specific statutory provisions allowing carriers to select their routes and to protect their long hauls.").

⁶⁸ In other cases, the Board has specifically requested comments on proposed procedures. See, e.g., *Simplified Standards for Rail Rate Cases*, STB Ex Parte No. 646 (Sub-No. 1), at 16-19 (served July 28, 2006) (Board proposed specific procedures and schedules and requested comments on the procedural issues).

⁶⁹ See, e.g., G3 Op., at 6; Sandy Creek Op., at 12 n. 32; Shipper Coalition Op., at 23-31.

uncertainty in the standards themselves, which the AAR opposes for the reasons stated herein and in its opening comments, it would not be appropriate to impose inflexible procedures before gaining some experience with new rules. Procedures that limit railroads' ability to defend against forced switching claims or that curtail due process would be inappropriate and unlawful. Indeed, the Board appeared to recognize that there are too many open questions about the substantive standards and how they will be addressed in individual cases to propose specific procedures for addressing individual claims.

While it is therefore premature to address the details of the shippers' procedural proposals, AAR comments on two general issues raised by the shippers' discussion of procedures for forced switching cases brought under the Board's proposed rules. First, shippers' concerns regarding procedures are focused on Prong 1 of the Board's proposed rules, which requires a demonstration that the "potential benefits from the proposed switching arrangement outweigh the potential detriments." *See* proposed rule 1145.2(a)(1)(iii). As shippers explain, "the first prong is largely a blank slate," making it difficult to develop and present evidence that would support a forced switching order under Prong 1.⁷⁰

The shippers' "blank slate" concern about Prong 1 of the proposed rules is not a procedural issue. It is a substantive problem that flows from the Board's failure to identify clearly the purpose of the new rules and its failure to show through a cost-benefit analysis that the proposed rules are in the public interest. As AAR explained on opening, an agency is required to assess the costs and benefits of proposed rules *before* adopting them, which requires that the agency first identify the problem to be solved with the new rules. The Board's improper decision to forego any analysis of costs and benefits of its proposed rules is part and parcel of the

⁷⁰ *See Shipper Coalition Op.*, at 24.

Board's failure to engage in rational decision-making in this proceeding. The standard under Prong 1 of the proposed rules is extremely vague and open-ended because the Board failed to articulate what the proposed rule is intended to accomplish. The requirement to carry out a cost-benefit analysis applies to both prongs of the Board's proposed rules, but the shippers' "blank slate" concern about Prong 1 highlights a fundamental problem with the Board's entire rulemaking process.

The shippers improperly seek to address the vagueness problem raised by Prong 1 by shifting the burden of proof onto the railroads, proposing that railroad *defendants* be required to prove in individual cases that forced switching is *not* justified. Under the procedures proposed by the shippers, a shipper seeking forced switching would have to present only the most superficial case (*e.g.*, that a switch is feasible and that the shipper would benefit from it). The railroad defendant would then have to demonstrate why forced switching would not be in the public interest.⁷¹ Such a shifting of the burden of proof would be a clear violation of the Administrative Procedure Act. The Administrative Procedure Act provides that "[e]xcept as otherwise provided by statute, the proponent of a rule or order has the burden of proof." 5 U.S.C. § 556(d). A shipper seeking forced switching under Prong 1 of the proposed rules must bear the burden of proving that the forced switch is in the public interest since a showing that forced switching is in the public interest is an express requirement of the statute. The burden cannot be placed on railroads to show that forced switching is not in the public interest.

E. Shipper Proposals on Compensation for Forced Switching

The AAR has previously cautioned the Board that forced switching cannot be used as a regulatory cudgel to beat down the proper and lawful exercise of differential pricing that is

⁷¹ See G3 Op., at 6; Shipper Coalition Op., at 27-29; Dow Op., at 4-5.

“crucial to the viability of the industry.” *Intramodal Rail Competition – Proportional Rates*, ICC Ex Parte Docket No. 445 (Sub-No. 2), 1990 MCC LEXIS 70 at * 7-8 (Apr. 17, 1990). To remain financially sound, “carriers must be allowed to engage in ‘demand-based differential pricing’—that is, in order to recover the substantial joint and common costs *of its network*, a railroad must be able and permitted to charge different customers different prices based on their different levels of demand for transportation services. If a railroad is unable to recover these joint and common costs, it will not be able to earn adequate revenues.” *Petition for Rulemaking to Adopt Revised Competitive Switching Rules*, STB Ex Parte Docket No. 711, at 7 (STB served July 25, 2012) (emphasis added). The federal courts resoundingly agree.⁷²

The Board’s own compensation proposals in this proceeding were met with tepid and conflicting review by the shipper community. Agricultural parties find more acceptable the multi-factored approach in *Switching Charges & Absorption Thereof at Shreveport, LA*, 339 I.C.C. 65 (1971).⁷³ Yet the Shipper Coalition rejects this first proposal, because it would require “expensive and time-consuming special switching studies.”⁷⁴ In contrast, the second approach, based loosely on the agency’s SSW methodology, was viewed as superior by the Shipper

⁷² See, e.g., *Union Pac. R.R. Co. v. United States*, 637 F.2d 764, 767, n.2 (10th Cir. 1981) (Pursuant to the 4-R Act, “the railroads may propose a rate which includes a price increment over and above fully allocated costs in order to assist them [sic] attain adequate revenue levels. This method of ‘differential pricing’ has been judicially approved as a valid means of achieving the ultimate goal of the 4 R Act which is to financially regenerate the nation’s railroads.”); *Mr. Sprout, Inc. v. United States*, 8 F.3d 118, 124-125 (2d Cir. 1983) (explaining that “Congress in the Staggers Act recognized that railroads must engage in ‘differential pricing’”); *MidAmerican Energy Co. v. STB*, 169 F.3d 1099, 1106 (8th Cir. 1999) (explained that the “Board has recognized that an important part of achieving revenue adequacy is differential pricing.”); *Union Pac. R.R. Co. v. STB*, 628 F.3d 597, 600 (D.C. Cir. 2010) (by “statute, rail carriers are authorized to engage in a certain amount of demand-based differential pricing in order to earn ‘adequate revenues’”).

⁷³ NGFA Op., at 15-16; see also Comments of U.S. Dept. of Agriculture, *Reciprocal Switching*, STB Ex Parte No. 711 (Sub-No. 1), at 7 (filed Oct. 26, 2016) (“USDA Op.”).

⁷⁴ Shipper Coalition Op., at 52.

Coalition, *id.* at 52, but rejected by agricultural parties because of the “costly and complex” process to value track assets. *See* NGFA Op., at 15.

Indeed, the Shipper Coalition’s witnesses, Messrs. Crowley and Fapp, would have the Board set compensation for forced switching based on (1) the incremental fixed and variable costs of providing the forced switch and (2) a rental component based on the system-wide average return on investment per car-mile, calculated from the annual RI reports.⁷⁵ This proposal is defective for three reasons. First, Messrs. Crowley and Fapp are advocating a simplistic fully-allocated cost approach, a concept repeatedly rejected by the ICC, the Board, and renowned economists.⁷⁶ Second, the use of backwards-looking depreciated historic costs rather than forward-looking current costs is inconsistent with Board precedent,⁷⁷ sound economics,⁷⁸ and recent direction from Congress.⁷⁹

⁷⁵ Shipper Coalition Op., Crowley/Fapp VS, at 15-27.

⁷⁶ *See Intramodal Rail Competition*, 1 I.C.C.2d 822 (1985) (rejecting fully allocated cost approach as compensation for forced switching as “arbitrary and economically unsound”), *aff’d sub nom. Baltimore Gas & Elec. v. United States*, 817 F.2d 108 (D.C. Cir. 1987). As the 2014 Nobel Prize winner for Economic Sciences Professor Tirole wrote: “There is no point dwelling on the conceptual drawbacks of fully distributed costs.” Laffont & Tirole, *Access Pricing & Competition*, 38 European Econ. Rev. 1673, 1697 (1994).

⁷⁷ The STB “has consistently stated its preference for using the best valuation of a carrier’s assets in performing its regulation function.” *Western Coal Traffic League—Pet. for Declaratory Order*, STB Finance Docket No. 35506 (served July 25, 2013). And the agency has explained that “carriers cannot attract and retain capital unless they are given the opportunity to be compensated for the real value of property, not just the book value.” *Conrail Acquisition Order*, 3 S.T.B. 196, 265 (1998).

⁷⁸ The weight of economic support for using the current value of rail assets is overwhelming. Over 50 economists, including two Nobel Laureates, have advised the agency that it should use replacement costs. *See* Opening Comments of CSX Transp., Inc., *Railroad Revenue Adequacy*, STB Ex Parte Docket No. 722 (filed Sept. 5, 2014) (“CSX 722 Op.”) and CSX 722 Op., Attachment 1, Verified Statement of William J. Baumol and Robert D. Willig, *Standards for Railroad Revenue Adequacy*, ICC Ex Parte Docket No. 393 (Sub-No. 1) (Aug. 4, 1986), Appendix A, Economists’ Statement in Support of the Staggers Act, at 2 (dated February 25, 1985). And in Ex Parte 722, Professors Kalt, Cornell, and Murphy testified that the economic theory on this issue remains as sound today as it was 30 years ago. Opening Comments of the

But these dual flaws, while grave, are dwarfed by a third and more dangerous flaw: advocacy of compensation that would fail to preserve lawful and necessary differential pricing. In truth, shippers argue that “the very objective of reciprocal switching” is to lower rail rates without having to prove them unreasonable under the Board’s established rate reasonableness standards.⁸⁰ As discussed above, since the “objective” of these shippers is to undermine differential pricing, they can hardly support a compensation methodology that would preserve and protect it. The shippers’ goal is both unlawful and unwise, because “the core regulatory principle in the rail industry is that a railroad must be able to engage in some form of demand-based differential pricing to have the opportunity to earn adequate revenues.” *See Major Issues in Rail Rate Cases*, STB Ex Parte No. 657 (Sub-No. 1), at 20 (served Oct. 30, 2006).

Adopting Shipper Coalition’s proposal would be a recipe for disaster. Professor Willig, in support of CSX’s opening comments in this proceeding, cautioned that “[i]t may be tempting to argue that because revenue from the full O-D move is not permitted to exceed its stand-alone

AAR, Verified Statement of Joseph P. Kalt, at 28-32, *Railroad Revenue Adequacy*, STB Ex Parte Docket No. 722 (filed Sept. 5, 2014); Opening Comments of Union Pacific Railroad Co., Verified Statement of Kevin M. Murphy, at 7-25, *Railroad Revenue Adequacy*, STB Ex Parte Docket No. 722 (filed Sept. 5, 2014); Opening Comments of Norfolk Southern Railway Co., Verified Statement of Bradford Cornell, at 13-19, *Railroad Revenue Adequacy*, STB Ex Parte Docket No. 722 (filed Sept. 5, 2014). See also the report prepared by InterVISTAS Consulting Inc. for the STB, *An Examination of the STB’s Approach to Freight Rail Rate Regulation and Options for Simplification*, at 122 (Sept. 14, 2016).

⁷⁹ See Section 16 of the Surface Transportation Board Reauthorization Act of 2015 (adding new language in italics), amending Section 10704(a)(2) to read: “The Board shall maintain and revise as necessary standards and procedures for establishing revenue levels for rail carriers providing transportation subject to its jurisdiction under this part that are adequate, under honest, economical, and efficient management, *for the infrastructure and investment needed to meet the present and future demand for rail services* and to cover total operating expenses, including depreciation and obsolescence, plus a reasonable and economic profit or return (or both) on capital employed in the business.” The additional statutory language can only be given effect, and its ordinary and natural meaning, if it is interpreted to require the Board to use a forward-looking, current cost approach.

⁸⁰ See, e.g., Cargill Op., at 7; USDA Op., at 7-8.

cost . . . the same stand-alone cost rule should be applied to pricing the components of the move. However, that practice is not economically sound and would lead to financial disaster for the industry.”⁸¹ The Shipper Coalition is undeterred. At the heart of its SSW proposal is an unabashed goal of offering a reasonable return only on the bottleneck segment used to provide forced switching – “a recipe for disaster for railroads and shippers alike.”⁸² Messrs. Crowley and Fapp would ask the STB to ignore the dire financial consequences that would follow a forced switching compensation methodology that fails to protect the industry’s ability to engage in “demand-based differential pricing” to recover the substantial joint and common costs *of its network*, not just the bottleneck segment.

In contrast, individual AAR members provided proposals and general principles on how the Board should set compensation to comport with sound economics and the central role of differential pricing in rail markets. Their testimony is supported by giants in the field of economics, including Professors Mark Armstrong and Bobby Willig (two economists who have published leading articles on access pricing in peer reviewed journals), Professor Kevin Murphy (winner of the John Bates Clark Medal and the George J. Stigler Distinguished Service Professor at the University of Chicago), Professor David Sappington (former chief economist of the FCC and leading expert on the design of regulatory policy), and Professor Joshua Wright (recent Commissioner of the Federal Trade Commission). The lopsided record compels the Board to adopt a compensation proposal that follows the single most important commandment of federal rail policy: to make a continuing and adequate effort to permit the railroad industry to achieve and sustain adequate revenues.

⁸¹ CSX Op., Willig VS, at 11.

⁸² *Id.* at 16.

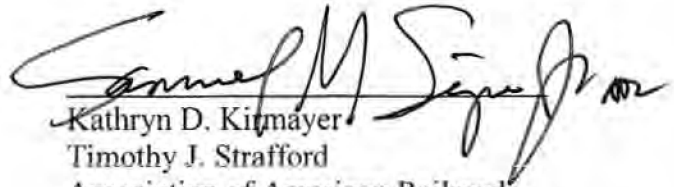
Board policy should not bend to the demands of a limited group of shippers who aspire to eviscerate demand-based differential pricing through forced switching. It cannot cast aside the fundamental economics of the railroad industry that make differential pricing a bedrock of revenue adequacy. It cannot consider a compensation methodology that rests on system-wide depreciated historical costs in conflict with the sage advice of virtually every economist to have addressed this issue before the agency for over 30 years. It cannot compromise and seek to accommodate the polar opposite positions of the shipper and railroad comments. Both the statute and sound economic theory demand otherwise.

Should the Board reach this issue, it must protect the railroads' ability to engage in "demand-based differential pricing" to recover the substantial joint and common costs *of their networks*. Any other objective would place in jeopardy the financial vibrancy of the U.S. freight railroads that drives commerce by safely, efficiently, and affordably connecting businesses, goods, and people with an expansive rail network. That private network is and must remain the backbone of the Nation's economy.

V. CONCLUSION

In sum, the shipper comments underscore the need for the Board to terminate this proceeding. The Board's proposal violates statutes, principles of sound economics, and longstanding policy without any coherent rationale. The Board has failed to make any assessment of the costs of its proposal and has identified no public benefits that would flow from it. The narrow self-interest of certain shippers in a revenue transfer in their favor – based on government intervention that they would never tolerate in their own industries – cannot offset the multiple flaws in the Board's proposal.

Respectfully submitted,

A handwritten signature in black ink, appearing to read "Samuel M. Sipe, Jr.", with a stylized flourish at the end.

Kathryn D. Kirmayer
Timothy J. Strafford
Association of American Railroads
425 Third Street, SW
Washington, DC 20024
(202) 639-2506

Samuel M. Sipe, Jr.
Anthony J. LaRocca
Steptoe & Johnson LLP
1330 Connecticut Avenue, NW
Washington, D.C. 20036
(202) 429-6486

Raymond A. Atkins
Sidley Austin LLP
1501 K Street, N.W.
Washington, DC 20005
(202) 736-8000

*Counsel for the Association of
American Railroads*

January 13, 2017

Appendix A

Letters from State and Federal Public Officials Expressing Concern that Forced Switching Could Interfere with Railroads' Ability to Meet the Growing Demand for Transportation Services and Changing Market Conditions (Referenced in Footnote 37)

Letter from the Honorable Terry Boose, State Representative, Ohio General Assembly, House of Representatives, 57th District, *Reciprocal Switching*, STB Ex Parte No. 711 (Sub-No. 1) (filed Oct. 19, 2016)

Letter from the Honorable Louis Terhar, State Representative, Ohio General Assembly, House of Representatives, 30th District, *Reciprocal Switching*, STB Ex Parte No. 711 (Sub-No. 1) (filed Oct. 27, 2016)

Letter from the Honorable Frank LaRose, State Senator, Ohio State Senate, 27th Ohio Senate District, and Chair, Transportation, Commerce and Labor, *Reciprocal Switching*, STB Ex Parte No. 711 (Sub-No. 1) (filed Oct. 27, 2016)

Letter from the Honorable Robert H. Plymale, State Senator, The Senate of West Virginia, 5th Senatorial District, *Reciprocal Switching*, STB Ex Parte No. 711 (Sub-No. 1) (filed Oct. 31, 2016)

Letter from the Honorable Rocky Adkins, State Representative and House Majority Floor Leader, Commonwealth of Kentucky, House of Representatives, 99th Legislative District, *Reciprocal Switching*, STB Ex Parte No. 711 (Sub-No. 1) (filed Oct. 31, 2016)

Letter from the Honorable Michael Busch, Speaker of the House, House of Delegates, State of Maryland, 30th Legislative District, *Reciprocal Switching*, STB Ex Parte No. 711 (Sub-No. 1) (filed Oct. 31, 2016)

Letter from the Honorable Leslie A. Combs, State Representative, Commonwealth of Kentucky, 94th District, *Reciprocal Switching*, STB Ex Parte No. 711 (Sub-No. 1) (filed Nov. 1, 2016)

Letter from the Honorable Wayne A. Schmidt, State Senator, The Senate, State of Michigan, 37th Legislative District, *Reciprocal Switching*, STB Ex Parte No. 711 (Sub-No. 1) (filed Nov. 1, 2016)

Letter from the Honorable Jim Tracy, Senator, Senate Chamber, State of Tennessee, 14th Senatorial District, and Chairman, Transportation & Safety, *Reciprocal Switching*, STB Ex Parte No. 711 (Sub-No. 1) (filed Nov. 2, 2016)

Letter from the Honorable Robert Stivers, President, Kentucky State Senate, 25th Senate District, *Reciprocal Switching*, STB Ex Parte No. 711 (Sub-No. 1) (filed Nov. 3, 2016)

Letter from the Honorable Robert Cole Sprague, State Representative, Ohio General Assembly, House of Representatives, 83rd District, *Reciprocal Switching*, STB Ex Parte No. 711 (Sub-No. 1) (filed Nov. 3, 2016)

Letter from the Honorable Gayle L. Manning, State Senator, The Ohio Senate, 13th District, and Chair, Transportation, Commerce, & Labor Committee, *Reciprocal Switching*, STB Ex Parte No. 711 (Sub-No. 1) (filed Nov. 8, 2016)

Letter from the Honorable Niraj J. Antani, State Representative, Ohio General Assembly, House of Representatives, 42nd District, *Reciprocal Switching*, STB Ex Parte No. 711 (Sub-No. 1) (filed Nov. 8, 2016)

Letter from the Honorable Damon Thayer, Majority Floor Leader, Kentucky State Senate, 17th Senate District, *Reciprocal Switching*, STB Ex Parte No. 711 (Sub-No. 1) (filed Nov. 8, 2016)

Letter from the Honorable Del Marsh, Senator and President Pro Tem, Alabama State Senate, 12th District, *Reciprocal Switching*, STB Ex Parte No. 711 (Sub-No. 1) (filed Nov. 8, 2016)

Letter from the Honorable Eli Evankovich, State Representative, House of Representatives, Commonwealth of Pennsylvania, 54th Legislative District, and Chairman, Manufacturing Caucus, *Reciprocal Switching*, STB Ex Parte No. 711 (Sub-No. 1) (filed Nov. 8, 2016)

Letter from the Honorable Cliff Hite, State Senator, The Ohio Senate, 1st District, *Reciprocal Switching*, STB Ex Parte No. 711 (Sub-No. 1) (filed Nov. 9, 2016)

Letter from the Honorable L. Brent Boggs, Member, West Virginia House of Delegates, 34th District, *Reciprocal Switching*, STB Ex Parte No. 711 (Sub-No. 1) (filed Nov. 14, 2016)

Letter from the Honorable Dale W. Zorn, State Senator, The Senate, State of Michigan, 17th Legislative District, *Reciprocal Switching*, STB Ex Parte No. 711 (Sub-No. 1) (filed Nov. 23, 2016)

Letter from the Honorable Tonya Schuitmaker, State Senator, The Senate, State of Michigan, 26th Legislative District, *Reciprocal Switching*, STB Ex Parte No. 711 (Sub-No. 1) (filed Nov. 23, 2016)

Letter from the Honorable Joe Hune, State Senator, The Senate, State of Michigan, 22nd District, *Reciprocal Switching*, STB Ex Parte No. 711 (Sub-No. 1) (filed Nov. 23, 2016)

Letter from the Honorable Tom Casperson, State Senator, The Senate, State of Michigan, 38th Legislative District, *Reciprocal Switching*, STB Ex Parte No. 711 (Sub-No. 1) (filed Nov. 23, 2016)

Letter from the Honorable Jim Boxold, Secretary, Florida Department of Transportation, *Reciprocal Switching*, STB Ex Parte No. 711 (Sub-No. 1) (filed Nov. 29, 2016)

Letter from the Honorable Chuck Fleischmann and the Honorable John J. Duncan, United States House of Representatives, Tennessee, *Reciprocal Switching*, STB Ex Parte No. 711 (Sub-No. 1) (filed Nov. 30, 2016)

Letter from the Honorable Martin A. Sandoval, State Senator, Illinois State Senate, 11th Legislative District, and Chairman, Senate Transportation Committee, *Reciprocal Switching*, STB Ex Parte No. 711 (Sub-No. 1) (filed Nov. 30, 2016)

Letter from the Honorable Edward J. Canfield, State Representative, Michigan House of Representatives, 84th District, and Chairman, House Appropriations Subcommittee on Transportation, *Reciprocal Switching*, STB Ex Parte No. 711 (Sub-No. 1) (filed Dec. 7, 2016)

Letter from the Honorable Donna Lupardo, Member, The Assembly, State of New York, 123rd District, and Member, Committees on Transportation and Economic Development, Job Creation, Commerce and Industry, *Reciprocal Switching*, STB Ex Parte No. 711 (Sub-No. 1) (filed Dec. 8, 2016)

Letter from the Honorable Dan Beiser, State Representative, Illinois House of Representatives, 111th District, and Chairman, Transportation Committee: Regulation, Roads & Bridges and Member, Intermodal Infrastructure Committee, *Reciprocal Switching*, STB Ex Parte No. 711 (Sub-No. 1) (filed Dec. 12, 2016)

Letter from the Honorable James L. Seward, State Senator, The Senate, State of New York, 51st District, *Reciprocal Switching*, STB Ex Parte No. 711 (Sub-No. 1) (filed Dec 12, 2016)

Letter from the Honorable Kathy Harrington, the Honorable Bill Rabon, the Honorable Wesley Meredith, the Honorable Warren Daniel, Senators, North Carolina General Assembly, Senate Chamber, 43rd, 8th, 19th, and 46th Legislative Districts, *Reciprocal Switching*, STB Ex Parte No. 711 (Sub-No. 1) (filed Dec. 13, 2016)

Letter from the Honorable Catharine M. Young, State Senator, The Senate, State of New York, 57th District, *Reciprocal Switching*, STB Ex Parte No. 711 (Sub-No. 1) (filed Dec. 13, 2016)

Letter from the Honorable Ralph S. Northam, Lieutenant Governor, Commonwealth of Virginia, *Reciprocal Switching*, STB Ex Parte No. 711 (Sub-No. 1) (filed Dec. 21, 2016)