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BEFORE THE
SURFACE TRANSPORTATION BOARD



EX PARTE NO. 586

ARBITRATION -- VARIOUS MATTERS RELATING TO ITS USE
AS AN EFFECTIVE MEANS OF RESOLVING DISPUTES THAT
ARE SUBJECT TO THE BOARD'S JURISDICTION

COMMENTS OF
NATIONAL GRAIN AND FEED ASSOCIATION

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Dated: November 21, 2001

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I. INTRODUCTION

National Grain and Feed Association ("NGFA") is commenting in response to the Board's Decision of September 20, 2001 ("Decision"), as modified on October 26, 2001.

NGFA is the U.S.-based trade association for over 1,000 grain, feed, processing and grain-related companies operating 5,000 or more facilities that store, handle, merchandise, mill, process and export over two-thirds of all U.S. grains and oilseeds. Approximately 70 percent of NGFA member firms are small businesses -- country elevators and feed mills. Also affiliated with NGFA are 36 state and regional grain and feed associations.

As modified, the Decision seeks (1) to update the Board's roster of qualified individuals willing to serve as arbitrators under the Board's voluntary arbitration program, (2) to add to the Board's formal complaint rules a requirement that a complaint must include a statement regarding arbitration, (3) to explore issues relating to legislation that would require binding arbitration of "small rail rate disputes," and (4) to entertain comments on the merits of arbitration in general or suggestions for mandatory arbitration of issues other than small rail rate disputes.

NGFA has no names to offer for the Board's roster of arbitrators. Nor does it have any comments regarding the Board's proposal to require that a statement of arbitration progress be included in formal complaints.

II. PROTECTION OF EXISTING ARBITRATION AGREEMENTS

The Board is to be complimented for seeking to explore a broader use of arbitration at the election of a party. NGFA operates and administers one of the nation's longest-standing industry-based arbitration systems that is available to resolve disputes between NGFA members or between NGFA members and third parties. NGFA believes that arbitration has the potential to provide a more commercially feasible manner of dispute resolution than does court or regulatory litigation, although it should be recognized that arbitration may not be suitable for handling certain types of issues such as those involving a multiplicity of interests.

As noted in the Decision, NGFA and all of the Class I railroads (plus many smaller carriers) have in place an arbitration system to address rail transportation issues. It provides for arbitration of certain specifically enumerated types of disputes such as the applicability and reasonableness of a railroad's demurrage rules and practices, mishan-

dling of private rail cars, and loss and damage claims arising under 49 U.S.C. § 11706. Claims involving more than \$200,000 per occurrence, railroad rates, charges and relationships, opening industries to reciprocal switching, credit terms and car allocation/distribution practices are not subject to the arbitration system.

The list of disputes subject to arbitration is reviewed periodically by representatives of the railroad industry who are associate members of NGFA and by NGFA's commercial members. The list has been expanded twice since rail arbitration was instituted three years ago. Arbitration is conducted, generally but not necessarily, through written statements before a committee of three arbitrators selected from NGFA agricultural members and rail industry associate members with a view to forming each committee of prominent people experienced in the type of trade involved in cases to be brought before it. A written decision is issued and an appeal is available to an arbitration appeals committee consisting of five member representatives. The NGFA rail arbitration rules are subject to the Federal Arbitration Act, 9 U.S.C. §1, et seq.

NGFA rail arbitration rules provide that NGFA active members and associate trading members can sign an agreement to arbitrate disputes that arise under the rules. That agreement, from which a participant can withdraw on 90 days' notice, is a binding contract to arbitrate.

Any legislation making small rate case arbitration available at the election of a party should do nothing to interfere with the implementation of contractual arbitration agreements such as the NGFA pre-dispute arbitration consent provisions. Even if congressional legislation were to authorize a party to a dispute unilaterally to designate STB arbitration as the means of dispute resolution, that election must give way to any preexist-

ing contract to arbitrate the same dispute. The Board need not seek to replace all other forms of arbitration with its own system, but instead should offer an arbitration structure that is available where appropriate.

III. ARBITRATION IN SMALL RATE DISPUTES

NGFA offers the following specific comments regarding arbitration.

Small Rate Disputes

The Decision seeks to "explore whether binding arbitration should be legislatively prescribed for small rate disputes." The Decision adopts the tentative position that arbitration of this category of disputes should be limited to those shippers whose traffic "would meet [the] market dominance test (i.e., traffic yielding more than 180 percent of variable costs and lacking feasible intermodal or intramodal alternatives) and who neither originate nor receive more than a defined number of cars per year via the railroad involved." For "purposes of promoting discussion on this issue," the Board suggests that a "proper figure might be in the 200-to-500 carload-per-year range."

NGFA does not object to the premise that arbitration of "small rate disputes" should be available only where the market dominance test is met, so long as that test remains applicable to all other maximum rate disputes.

However, NGFA does not believe that it would be appropriate or constructive to measure eligibility for small rate case arbitration by carloads shipped annually via the defendant railroad's system.

NGFA suggests that the best approach to determine eligibility for mandatory rate arbitration is one that utilizes monetary benefits derived from the arbitration. Monetary benefits are what shippers in fact analyze in determining whether to undertake rate litiga-

tion. A shipper contemplating such a step invariably does so by estimating net litigation benefits; estimated rate reduction minus estimated litigation costs. Indeed, a cost-benefit analysis was employed by Congress as the measure of those instances when "a simplified and expedited method" for determining maximum rate complaints should be made available. See 49 U.S.C. § 10701(d)(3).

The Board appears to have arrived at carloads as a measure of eligibility by virtue of having eliminated freight revenues as the standard,¹ apparently regarding freight revenues as inappropriate because of the disparate revenue levels that attach to different commodities. Thus, it appears that the Board reasoned that there must be a uniform standard for use in all small rate case arbitrations and that, if it should not be freight revenues, it should be carloads shipped.

Whether or not a single uniform standard is the correct approach, the standard should not be based on carloads shipped or extend beyond the origin-destination pairs to which the complaining shipper applies the challenged rate.

In the first place, setting the threshold at anywhere between 200 and 500 carloads per year shipped via a defendant railroad would make arbitration unavailable to the vast majority of grain shippers, since there are few who ship quantities below those thresholds and who also have enough at stake to enter into the dispute resolution process.

Second, carloads by themselves say nothing meaningful about the need to access arbitration in lieu of other more time-consuming and expensive means of dispute resolution. Depending on the extent to which any given rate that is challenged exceeds a

¹ The Decision states that if "special treatment was limited to a particular commodity group (such as agricultural commodities), then freight revenues could be a useful measure as well."

maximum reasonable level, a rate complaint involving far more than 500 cars a year could end up having a smaller economic impact than one involving 200 cars per year.

Third, it is inappropriate to apply any test to the totality of shipments made by a complaining party via the defendant railroad. The Board's jurisdiction to entertain rate cases turns on "transportation to which a particular rate applies," 49 U.S.C. § 10701(d)(1). The jurisdictional market dominance threshold, 180 percent of variable costs, applies only to the transportation to which the challenged rate applies. It is inconsistent with that statutory approach to use system-wide carloads to delineate an applicable remedy.

For similar reasons, NGFA disagrees with the Board's view that access to rail rate arbitration should depend on total traffic volume shipped via the defendant carrier. This approach means that not only would all points at which the complaining party ships or receives be considered, but also all commodities. As a result, traffic having absolutely nothing to do with the potential rate complaint itself would determine the shipper's right to access arbitration. NGFA regards that as an illogical approach that unnecessarily will narrow access to arbitration.

The Board reasons that a system-wide analysis of the shipper's traffic via the defendant railroad is appropriate because it measures the "leverage that a shipper ... can exercise." That assumption is weak factually and structurally. For example, shipments of wheat for export depend on almost totally different commercial and market conditions than do shipments of corn syrup or soybean meal, even though all three commodities may be shipped by the same company via the same railroad. Large railroads sometimes assign marketing responsibilities for these commodities to different individuals. Further, the

commingling of all commodities and origins to determine "leverage" is inconsistent with the approach which the Board has taken in market dominance determinations, which are commodity-specific and geographic-specific. See Ex Parte No. 627, Market Dominance Determinations -- Product and Geographic Competition, ___ S.T.B. ___ (April 6, 2001). It seems inconsistent to conclude that the ability to maintain a maximum rate complaint is determined strictly by a market analysis of the commodity at issue in the geographic context of the points between which it is shipped on the defendant railroad, while the right to access arbitration to resolve the dispute is determined by a test that has nothing to do with either the commodity or its movement.

NGFA believes that the appropriate measure for a "small rate case" is one which reflects the case's economic yield. To evaluate that approach, the Board must recognize that any form of rate arbitration -- whether it be final offer or more conventional arbitration -- entails a commitment by the complaining party of considerable economic and human resource expenditures. In the first instance, market dominance must be proven, which necessitates revenue/variable cost studies often preceded by discovery. Second, it should be expected that railroads resisting maximum rate prescriptions will utilize their version of an established methodology for calculating maximum reasonable rate levels. A stand-alone cost presentation (SAC) is the only such tried and proven methodology. There also are "simplified" procedures which have been prescribed but never utilized. See Ex Parte No. 347 (Sub-No. 2), Rail Guidelines--Non-Coal Proceedings, ___ S.T.B. ___ (December 31, 1996). It is a virtual certainty that a railroad defendant in a rate arbitration proceeding will utilize one or the other of these methodologies to sustain its position, thereby necessitating a similar presentation by the complaining shipper. SAC is an

extremely fact-intensive approach, one that relies on detailed discovery and the use of expert witnesses. Even the so-called simplified methodology in Ex Parte No. 347 (Sub-No. 2) requires implementing discovery and expert witnesses.

Because arbitration of rate disputes is highly technical, it does not appear susceptible of being carried forward without the assistance of counsel. Nor can it be assumed that a successful complainant necessarily will escape arbitration costs, such as the fees and expenses of one or more arbitrators. All things considered, if a defendant railroad were to rely on any form of SAC presentation, "simplified" or full-blown, to further its position, there is no reason to believe that arbitration can be conducted at bargain costs, even though it has the potential to be more expedited than ordinary regulatory litigation. A "small rate case" could easily entail hundreds of thousands of dollars in fees and expenses, even if confined to a single origin-destination pair. If the case is expanded, costs likewise will expand.

A shipper would have a difficult time justifying arbitration expenditures of that magnitude in return for a potential recovery that was not well above the level of the expenditures. Limiting arbitration access to only those shippers who tender less than a few hundred cars per year spread over the defendant railroad's entire system -- when any maximum rate award would not even apply to the entirety of this already small group of cars -- would almost certainly foreclose the use of arbitration in rate cases.

The alternative is to cap the amount of recovery available to an arbitration complainant. This process entails establishing a maximum life for an arbitration award from the day it is issued. The Board's present bilateral arbitration rules provide for a three year

monetary damage award life. See 49 C.F.R. §1108.4(a)(2). NGFA sees nothing wrong with that limitation.

To allow for recovery of all arbitration costs and a cushion to make the arbitration worthwhile if successful, NGFA proposes that small rate case arbitration be limited to recovery of \$250,000 per origin-destination pair for each year the arbitration award would be effective.

Entitlement to use the small rate case procedures would not have to be proven at the outset of a case, as under the Board's present "simplified" procedures, where each case must commence with resolution of a dispute regarding case costs and benefits to see if it qualifies for "simplified" treatment. See 49 C.F.R. §1111.9. Instead, the relief granted (if any) would simply be capped by the small case award limit. Once the complaining party exhausts its damage award maximum for the case or the award expires chronologically, the arbitration award would cease to be of further application. More so than the Board's proposal of tying small rate case arbitration to carloads shipped without regard to case benefits, this approach will realistically reflect the cost-benefit type of analysis that drives any decision to invoke formal dispute resolution procedures, yet will be simple enough to apply without the necessity of a pre-dispute argument regarding arbitration access.

Arbitration Standard

The Decision poses the question of whether small rate case arbitration should follow traditional paths, leaving to the arbitrator(s) the discretion to find for one side, for the other side, or to fashion a middle-ground remedy; or whether to utilize final offer arbitration ("FOA"). Final offer arbitration, sometimes known as baseball-style arbitration, re-

quires the arbitrator(s) to do nothing more than select the final offer of one side or the other. No compromise decision is permitted.

Final offer arbitration does not appear well-suited for all aspects of small rate case arbitration but may well be appropriate for selection of a final rate level. In many respects, virtually every issue that arises in arbitration requires the arbitrator(s) to make a black-and-white choice: yes, there is effective intra-modal competition or no, there is not; yes, the challenged rate exceeds 180 percent of variable cost, or no, it does not. Yet, these types of decisions, and especially the latter issue, are not always reached through a mere election between the position of one party or another. There are many instances in which the facts are restated by the decider. Whether a rate exceeds 180 percent of variable costs should not be determined because one side got a little closer to the truth than the other side. Either the rate is over 180 percent of variable cost, or it is not.

On the other hand, use of FOA in determining the final rate level to be set has the benefit of discouraging parties from adopting extreme positions. Consequently, its use may well lead to voluntary resolution of disputes once the parties are required to focus on their alternatives within the framework of the arbitration process. For that reason, NGFA believes that FOA is worthy of use in selecting a maximum reasonable rate, even though it may not be imprudent for the Board to have the authority to replace FOA with more conventional arbitration if FOA does not appear to be doing the job.

Discovery

As indicated above, discovery is likely to be necessary in arbitration proceedings involving challenges to rail rate levels. However, discovery must either be closely supervised by the arbitrator(s) or conducted pursuant to rules that deter clear abuses of discov-

ery. Unless extraordinary circumstances are present, depositions should not be allowed and under no circumstances should be allowed as of right, without leave of the arbitrator(s).

Reviewability

In general, NGFA favors review under the Federal Arbitration Act for small rate case arbitration. Allowing such arbitration decisions to be reviewed for jurisdiction will provide assurance that no rate is set that is under 180 percent of the defendant railroad's variable costs or mandated in the absence of market dominance, as both matters are jurisdictional in rate reasonableness proceedings.

Reservations Regarding Small Rate Case Arbitration

As much as NGFA favors arbitration as a means of dispute resolution, it is far from clear -- and in fact is doubtful -- that the extension of arbitration to small rate disputes will do much to improve the ability of shippers to obtain relief from unreasonably high rail rates in those cases where a full-blown SAC presentation is impractical. Although the dispute resolution process clearly warrants improvement, without changes in the Board's substantive outlook toward rate reasonableness proceedings, an improved process may simply bring about a conclusion more quickly and inexpensively than otherwise would be true.

The "simplified" procedures adopted by the Board in Ex Parte No. 347 (Sub-No. 2) have not been utilized in any decided rate reasonableness case. The principal reason why that is so, in the opinion of NGFA, is because the "simplified" guidelines are regarded as offering only a half measure of rate reduction potential, while embroiling the complainant in a complex and costly case.

The Ex Parte No. 347 (Sub-No. 2) procedures involve the use of three "benchmarks," two of which are statistics readily derived from periodically published data of the Board. Those two benchmarks strongly suggest that it would be unlikely for a rate prescribed through that methodology to be set below 240 percent of variable costs, more or less. Whereas a complainant whose traffic is susceptible of a full SAC presentation realistically can anticipate a prescribed maximum rate as low as 180 percent of variable costs, having to use the "simplified" methodology stands virtually no chance of obtaining a similar reduction. Thus, while it might make sense for a rate at 250 percent of variable costs to be assailed by a complainant able to bring a full SAC case, it makes no sense for a like rate to be assailed under the "simplified" methodology because the result is not worth the effort. Rates would have to be well above 250 percent of variable costs before a "simplified" rate case would be justified. If the Board determines to advise Congress that improved access to rate reasonableness recourse is advisable for shipments that do not realistically fit within the SAC methodology, the Board should apprise Congress that an alternative to the Ex Parte No. 347 (Sub-No. 2) methodology appears to be necessary or that not even the availability of arbitration will provide an adequate remedy.

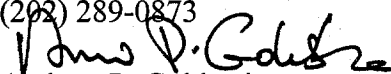
IV. EXTENDING ARBITRATION BEYOND SMALL RATE CASES

NGFA sees no reason why mandatory arbitration at the election of a party should be confined to those cases where the maximum level of a rail rate is at issue. Other types of disputes subject to the Board's jurisdiction also are susceptible of resolution through arbitration and can be arbitrated, probably at less cost and in less time, than they can be litigated through administrative proceedings followed by unlimited judicial review.

While NGFA broadly favors arbitration, arbitration should be available to resolve disputes and not as a regulatory tool. Thus, for example, a claim for monetary damages arising from an alleged failure of a railroad to furnish an adequate number of cars for loading after a request to do so can be regarded as an arbitable matter, while an arbitrator should not be empowered to direct a railroad to alter its method of car distribution in the future.

The Board should review the types of disputes that the Board is capable of resolving through arbitration in addition to rate cases and frame an appropriate recommendation to Congress for the extension of arbitration in those instances.

Respectfully submitted,

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McD/NGFA Comments