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**BEFORE THE
SURFACE TRANSPORTATION BOARD**

Ex Parte No. 646

Rail Rate Challenges in Small Cases

WRITTEN TESTIMONY

SUBMITTED BY

THE NATIONAL INDUSTRIAL TRANSPORTATION LEAGUE

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**BEFORE THE
SURFACE TRANSPORTATION BOARD**

Ex Parte No. 586

Rail Rate Challenges in Small Cases

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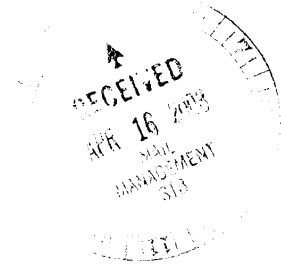
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In a Notice and Amended Notice of Public Hearing issued by the Board on March 26 and April 1, the Board announced that it would hold a public hearing to provide a forum for the expression of views by rail shippers, railroads, and other interested persons regarding rail rate challenges in small cases to be considered by the Board. The hearing is intended to provide a forum for discussing proposals for handling small cases involving a challenge to the reasonableness of rates charged by a rail carrier, as well as views on how small rate cases should be defined or identified. This Written Testimony is submitted by the National Industrial Transportation League ("League") in response to the Board's Notice.

The League is very pleased that the Board is holding this hearing. Regulatory oversight of rail rates and charges in situations where there is a lack of effective competition from other rail carriers or modes of transportation is one of the primary duties and functions of the Board. In light of these statutory responsibilities, the Board has issued "evidentiary guidelines" in its decision in Ex Parte No. 347 (Sub-No. 2), *Rate Guidelines – Non-Coal Proceedings*, 1 S.T.B. 1004 (1996) [*"Small Case Guidelines"*]. However, as the Board has noted, there has not been a

single case filed under these guidelines since they were promulgated. The League believes that these guidelines are deeply flawed, and the League highly commends the Board for attempting to take a fresh look at its procedures for processing so-called “small” cases. The League believes that the Board has recently made commendable changes in its procedures for processing large rate cases under its stand-alone cost methodology,¹ and the League welcomes a similar – indeed, even a more far-reaching – review of its small case procedures. Finally, the League very much commends the Board for the process that it is utilizing in this proceeding, that is, an initial informal hearing without formal proposed rule changes, so that the Board can obtain a sense of the problems with its current procedures, as well as possible areas of solution to investigate further.

I. IDENTITY AND INTEREST OF THE NATIONAL INDUSTRIAL TRANSPORTATION LEAGUE

The League is one of the oldest and largest national associations representing companies engaged in the transportation of goods in both domestic and international commerce. The League was founded in 1907, and currently has over 700 company members. These company members range from some of the largest users of the nation’s and the world’s transportation system, to smaller companies engaged in the shipment and receipt of goods. The League’s members includes shippers and receivers of goods as well as carriers, third party intermediaries, logistics companies, and similar entities. Members of the League are engaged in all forms of transportation, including rail, motor, ocean and air carriage. Members of the League ship large quantities of goods by rail, and therefore have a keen interest in the regulatory rules that govern rail transportation.

¹ See, Ex Parte 638, *Procedures to Expedite Resolution of Rail Rate Challenges to be Considered Under the Stand-Alone Cost Methodology*, decision served April 3, 2003 [*Expediting Resolution of SAC Cases*].

II. THE BOARD'S CURRENT SMALL CASE GUIDELINES DO NOT PERMIT SHIPPERS TO PRACTICABLY ACCESS THE PROTECTIONS AFFORDED BY THE STATUTE AND DISCOURAGE THE PURSUIT OF RELIEF

As noted above, in its decision in Ex Parte 347 (Sub-No. 2) *Small Case Guidelines*, the Board issued “evidentiary guidelines” to be used in proceedings to determine the reasonableness of challenged rail rates charged on captive traffic where the Board’s “Constrained Market Pricing” (“CMP”) guidelines could not practicably be applied. Despite the fact that these “small case” guidelines have been in effect for more than six years, they have not been invoked in a single case. It would be fatuous to conclude that, in this period of time, there has not been a single dispute over rail rates of a magnitude that would lead even one complainant to file for relief under the *Small Case Guidelines*. Rather, the League submits that the Board’s guidelines do not permit shippers to practicably access the protections afforded them by the statute, and in fact discourage the pursuit of relief.

There are at least four major flaws with the Board’s *Small Case Guidelines*. First, the Board’s process for qualifying for small case treatment is needlessly expensive and extremely vague. Second, the *Guidelines* describe a process that takes far, far too long. Third, the maximum rate “standards” proposed by the *Guidelines* are extremely vague, and therefore it is virtually impossible for a shipper to make any rational judgment as to whether its case is meritorious or not. Fourth, the combination of the uncertain qualifying process, the length of time to process a case, and the vagueness of the substantive standards appears to permit a defendant rail carrier to drive up the cost of a case so as to outweigh any possible monetary relief.

Even one or two of these flaws would discourage all but the most determined shipper, and the existence of all of them has caused virtually the entire universe of shippers of

commodities other than coal – even shippers of relatively large volumes of goods transported at high rail revenue-to-cost ratios – to simply dismiss the possibility of relief from the Board. Thus, aside from its responsibilities in rail mergers and in some other rail matters such as abandonments, the Board’s existence is practicably useful for probably well less than seventy-five rail shippers (almost exclusively utility unit-train coal shippers) out of the thousands of rail customers.

1. The Transportation Situation of Non-Coal Shippers

Before discussing the specific flaws with the Board’s existing rules, it may be useful to set the stage by describing the transportation and market situation facing the large majority of rail shippers. As the Board well knows, there have been a number of complaints against unreasonably high rail rates under the Board’s *Coal Rate Guidelines*,² but none under the Board’s *Small Case Guidelines*. Unit-train coal shippers typically transport huge volumes of a single commodity between one or a few origins to a single destination, year after year after year – often for twenty years or more. Thus, if a case takes two or three years, it may still be financially feasible to bring a complaint for the prescription of a maximum reasonable rate, because the shipper will see the benefit of even a large litigation cost since the maximum rate prescription will apply to the transportation of large volumes of goods far into the future.

None of this is usually true for a non-coal shipper. Although a non-coal shipper may have an initial rail movement of a fairly substantial volume of some commodity year after year over the track of a single carrier from one or a few origins to a rail yard or interchange, once beyond the “bottleneck” the non-coal shipper’s goods are often widely dispersed to many

² *Coal Rate Guidelines – Nationwide*, 1 I.C.C.2d 520 (1985), *aff’d*, *Consolidated Rail Corporation v. United States*, 812 F.2d 1444 (3d Cir. 1987).

(sometimes hundreds) of destinations. But under the Board's "bottleneck" rules, a shipper generally cannot file a complaint against the bottleneck carrier alone (even though the rate charged by the bottleneck carrier is virtually always the *situs* of the monopoly pricing). Thus, the non-coal shipper is faced with the need to bring numerous separate origin-to-destination complaints, none of which individually may be financially viable, and all of which collectively would be extremely expensive to pursue.

Making the situation even more problematic is the fact that demand for the transportation of non-coal commodities to a specific destination point changes much more rapidly compared to the consistent movement of coal for twenty-years or more. In other words, even though a chemical plant, for example, might produce a fairly substantial volume of chemicals year after year, and that volume might be transported fairly consistently from the plant over the line of a monopoly bottleneck carrier that charges high rates to an interchange, the identity of dispersed destination points often changes after a few years, or even less in some cases. Thus, a case process that on its face takes a year, or (much more likely) substantially more time, will likely chew up a substantial amount of the maximum period for relief useful to the shipper.

Compounding the problem is the fact that complaints against unreasonably high rail rates can be brought only after a contract ends, at which point the rail carrier will immediately and substantially increase the rate. While such an increase itself would discourage a complaint, the even larger problem is that the shipper, as discussed below, cannot rationally calculate his exposure in view of the uncertain period of time under the *Small Case Guidelines* for the agency to arrive at a decision, and the uncertain substantive standards articulated in that decision.

Finally, a discussion of the situation facing a shipper considering a rate complaint against its market-dominant rail carrier cannot be complete without at least a mention of the built-in risk and fear that any shipper (even the largest coal shipper) faces by publicly challenging a rail carrier who controls its ability to transport, and therefore to sell, its product in the market. Particularly during times of high demand, shippers are concerned that even subtle shifts in a rail carrier's service and willingness to transport may put at risk product sales that dwarf the cost of transportation, however high.

In view of the above situation, the Board needs to understand that its process for adjudicating small cases must be very quick, very clear, and inexpensive. Instead, the Board's current guidelines describe a process that takes a substantial period of time, is extremely uncertain, and is unnecessarily expensive.

2. Qualifying for *Small Case Guidelines* Treatment is Vague and Unnecessarily Expensive

Under the Board's *Small Case Guidelines*, in order to invoke the small case procedures outlined by the Board, the shipper not only has to declare its intent, but also "has to present sufficient information to show that CMP is not available." *Small Case Guidelines*, 1 S.T.B. at 1050. The rules indicate that the initial complaint must contain "at minimum" nine separate information items, each with a variety of separate subparts, including the general history of the traffic at issue, the commodity, the shipping characteristics of the commodity, the amount of traffic, the average revenue per carload, and an estimate of "the full relief sought, including all reparations and the level and duration of any rate prescription," etc. Most problematic is the requirement for "an estimate of the feasibility and anticipated cost of preparing a SAC presentation," a requirement that suggests some expenditure of money, including probably a

verified statement from a SAC cost consultant, discussing what has been done to determine the feasibility and cost of a full SAC presentation.

If it were “accepted” by the Board that a SAC presentation costs \$2 million, the showing outlined in the Board’s rules might not be so onerous. But the Board cannot assume that a carrier will agree that a SAC presentation actually costs that much. The Board’s own *Small Case Guidelines* decision states that the “Association of American Railroads claimed in that case that a SAC presentation could be made for as little as \$25,000 to \$85,000.” Given the Board’s recent decision in *Expediting Resolution of SAC Cases*, such a claim might be regarded as ludicrous (indeed, a scaled-down presentation of variable cost evidence, which is far simpler to calculate than SAC, probably would cost substantially more than \$25,000 to \$85,000, depending upon the complexity of the facts). However, in *Small Case Guidelines*, the agency simply noted the AAR’s claim without any disapproving comment, and there is no reason to believe that a rail carrier defendant today would not make the same or similar claim in opposing a shipper’s request for small-case treatment.

Indeed, a reading of the agency’s *Small Case Guidelines* decision would suggest that the guidelines will be available for only very small movements. In its decision, the agency rejected, for example, as “overly sweeping in their reach” various origin-destination pair tonnage tests presented by shippers, and even dismissed a suggestion by the Department of Transportation that any shipper whose freight bill was less than \$1 million per year should presumptively qualify for simplified procedures. 1 S.T.B. at 1047.

Finally, it is extremely important to note that *the very uncertainty* of the process for qualifying for small case treatment discourages the filing of a complaint. A rational attorney

counseling a rational client cannot assure that client, once a potential claim exceeds a nominal amount, that the shipper will receive small-case treatment from the Board. Thus, a shipper does not know what case to prepare, and given the uncertainty, the shipper is faced with the possibility that the money spent to investigate and prepare a “small case” might simply be thrown out the window. And this is only the beginning of the uncertainty and expense.

3. The *Small Case Guidelines* Require An Adjudication That is Far Too Long

Probably the single largest disincentive to a shipper’s use of the Board’s *Small Case Guidelines* is that the process takes far too long, and the time period is highly uncertain.

Under the current rules, 45 days is consumed in just determining whether a case deserves “small case” treatment. At that point, cost discovery and review of the Board’s Waybill Sample is needed, with opening, reply and rebuttal evidence then filed by the parties. Since the Board’s discovery rules provide for at least twenty days for reply, discovery cannot be completed in less than a month. It is more likely that discovery will consume at least twice that time, and probably much more, depending upon the carrier’s responsiveness to discovery propounded by the shipper. Even assuming a very brief period for the filing of evidence (e.g., 30 days for opening, 30 for reply and 15 for rebuttal), the “qualification,” discovery and evidentiary phases under the Board’s current rules will likely consume 6 months, under extremely favorable assumptions. In SAC cases, the Board has always required the filing of a post-evidence brief, usually two months or more after the rebuttal evidence has been submitted, and there is no reason to believe that the Board would not order a brief in a small case. At that point, the Board is permitted a six month period for rendering a decision.

Thus, under extremely favorable assumptions, a “small case” will take at least a year, and probably more. As noted above, few shippers have the type of ongoing, year-after-year, repetitive origin-to-destination movements such as exist in large coal cases, and challenges to rates over “bottlenecks” (which often do have ongoing, repetitive movements over them) are basically not allowed.

Compounding the disincentives presented by a complaint process that on its face will take more than a year is the uncertainty. The Board’s rules make no promises, set out no maximum time limits for discovery, indeed do not address discovery at all. History in SAC cases suggests that a single motion to compel filed by the carrier over some aspect of cost or market-dominance evidence would require a substantial period of time to resolve. Thus, while a shipper can “guess” that the *minimum* time period for resolving a case under the *Small Case Guidelines* is probably fourteen months, the actual time period is simply not knowable.

4. The Vagueness of the Board’s Guidelines Discourage Potential Complaints

The Board’s *Small Case Guidelines* do not present a standard for decision, as with cases under CMP, but rather three kinds of evidence that must be submitted. Two of the benchmarks (RSAM³ and R/VC>180⁴) require the shipper to calculate and present a calculation of the variable cost of its own traffic, and compare that evidence with data published by the agency. The third benchmark, R/VC_{comp}, requires the shipper to calculate and present evidence of the variable cost of its own traffic, and to compare its markup with the markup on “similar commodities moving under similar transportation conditions.” 1 S.T.B. at 1034. That

³ RSAM measures the uniform markup above variable costs that would be needed from every shipper in order for the defendant to recover all of its fixed costs.

⁴ R/VC>180 is designed to measure the degree of differential pricing actually being practiced by the defendant.

information cannot be ascertained until after the filing of a complaint, since the Board has ruled that the shipper cannot have access to the confidential waybill sample prior to filing of the complaint. *Id.* at 1054.

The Board's *Small Case Guidelines* decision gives no indication, however, as to the relative weight to be given to these three pieces of evidence, and even rules that this evidence is not exclusive. The Board stated: in presenting a case, "each of the benchmarks will be introduced and can be subjected to scrutiny. Moreover, . . . the benchmarks serve merely as the starting point of an analysis that should be further developed and tailored to the individual case." *Id.* at 1045.

Given the lack of definition in the *Small Case Guidelines* and the unavailability of data necessary to apply the benchmark standards, it is impossible for a shipper to make a reasonable judgment about the probable outcome or range of outcomes of a case prior to filing a complaint. This factor militates strongly against filing a complaint, since a rational shipper cannot assess its cost and risk against the likelihood of success. Moreover, what little evidence can be gleaned from the Board's *Small Case Guidelines* decision suggests that the rate prescribed in a small case is likely to be a far higher rate than a Stand-Alone Cost proceeding. A review of all SAC cases since 1985 in which the shipper has obtained prescription of a maximum reasonable rate indicates that the 180% jurisdictional threshold has usually determined the rate. Even in cases in which this was not true – such as the recent *TMPA* decision – the prescribed rate exceeded the jurisdictional threshold by a relatively small percentage amount.⁵ But the evidence available from the RSAM and the R/VC>180 data published by the Board suggests that a shipper bringing

⁵ See, *Texas Municipal Power Agency v. The Burlington Northern & Santa Fe Railway Company*, decision served March 24, 2003. The prescribed rate to variable cost percentage in that decision was about 190%.

a small rate case will have a rate prescribed that is substantially in excess of the jurisdictional threshold.

5. The Combination of the Vague Qualifying Standards, the Uncertain Time Period for Processing a Case and the Lack of Clear Substantive Standards Drives Up the Cost of Bringing a Small Case

While the uncertainty in various aspects of the process is a key discouraging factor in the non-use of the Board's *Small Case Guidelines*, the uncertainty leads to a well-justified fear that the cost of bringing a small case will soon exceed any potential gains. A rail carrier defendant will have a clear incentive to oppose a complaint at every turn, both to drive up the cost of a case for the complainant, and to discourage potential future complainants. The Board's *Small Case Guidelines* do not blunt that incentive: indeed, their vagueness and uncertainty encourage it. In such an environment, a rational shipper will soon conclude that all of the potential costs -- the cost of investigating whether a case is justifiable, the cost of qualifying for small case treatment, the cost of presenting variable cost and other evidence, etc. -- will not outweigh the potential relief. Even worse, the uncertainty of the process and therefore the uncertainty of the cost will make the risk of bringing even a "large" small case too great.

III. THE BOARD SHOULD CONSIDER A VARIETY OF CHANGES TO IMPROVE ITS PROCESSING OF RATE CHALLENGES IN SMALL CASES

The League acknowledges the difficulty of solving the severe problems with the Board's small case guidelines, particularly in light of judicial decisions that have approved the use of CMP as the only test recognized thus far as complying with the statute's directives. The Board initiated the proceeding to develop small case rules in 1986, and it took a Congressional directive to force the Board to complete it. *Small Case Guidelines*, 1 S.T.B. at 1006, 1010. The League recognizes that the only solution for some of these problems may be statutory amendment. In

addition, the League would note that it believes that a pro-competitive solution, such as fixing the Board's terminal access rules, is far better than "fixes" to the Board's procedural or substantive rules for processing small rate cases. A competitive rail market will *automatically* provide efficient solutions to high rail rates, without the need for expensive and slow direct regulatory intervention in the prices that rail carriers charge. Another option for the Board would be to re-examine its "bottleneck" decision, to permit pro-competitive bottleneck rates. Nevertheless, if the Board believes that it is unable under the statute or is unwilling to consider changes to its policies regarding rail-to-rail competition, there are some things that the Board might investigate to improve its processing of small rate cases.

A. The Board Might Investigate Whether a Radically Simplified SAC Is Possible, Using Standardized Data

There appears to be a huge regulatory "gap" between cases suitable for SAC and cases that would appear to qualify for "small case" treatment under the Board's *Small Case Guidelines*. The cost of bringing a SAC case by a complaining shipper requires an expenditure of approximately \$2 million. A SAC case involving multiple origins or destinations costs more than that, since a SAC system with multiple origins and destinations is substantially more complicated than a system designed for a rate complaint against a single origin and single destination. Thus, under the current SAC standard, a shipper must have an annual rail "bill" that is several times greater than \$2 million between a single origin and destination in order to even consider bringing a case under the CMP/SAC standard, since the potential rail rate reduction must, in order to justify the risk and expense of litigation, be well in excess of that amount. As the agency pointed out, "a SAC presentation would not be cost-effective unless the value of the expected remedy exceeds the expected cost of obtaining the remedy by a sufficient margin to make it worthwhile to pursue the complaint. [Footnote omitted] If the cost of pursuing a

complaint would consume most or all of the expected recovery, then the remedy would be a hollow one indeed.” 1 S.T.B. at 1049. Aside from utility coal shippers, there are almost no other shippers with origin to destination movements whose rail bills are of a sufficient magnitude to realistically consider a SAC case under current procedures.

On the other hand, there are statements in *Small Case Guidelines* that suggest that the Board believes that those small case processes should be used by only the smallest rail shippers. As noted above, the Board did not even see fit to adopt a DOT suggestion that shippers with a total rail bill of \$1 million automatically qualify for small case treatment. See, 1 S.T.B. 1045-1049.

But the large majority of shippers live *precisely* in this “gap” between massive coal rate cases involving tens of millions of dollars of rail costs between a single origin and destination, on the one hand, and small shippers with rail bills of \$1 million or less. If the Board is not willing to clearly indicate that substantially-reformed small case procedures can be used by shippers with, for example, rail bills of \$8 million between a single origin and destination or more,⁶ or if the Board believes that it would not be possible to judicially defend its small case standards in such instances, then the Board must find a middle way between its current SAC procedures and any reformed small case guidelines. One possibility might be for the Board to investigate whether it might be possible to radically simplify and standardize its SAC evidentiary showing by utilizing, for example, data on the cost of constructing a stand-alone railroad and the cost of operating the hypothetical SAC carrier by deriving “standard” figures for construction per

⁶ Even an \$8 million annual rail bill between a single origin and destination may not be enough to justify a \$2 million SAC case. If a shipper with a \$8 million rail bill between a single origin and destination estimates that its rail rate is 25% too high, then a successful complaint would reduce that shipper’s rail bill by \$2 million per year. Assuming that a shipper needs a multiplier of three as the necessary margin between the expected costs and expected recovery to justify the risk, see 1 S.T.B. at 1049, then the shipper would need to be assured that movement would continue for three years at the same level or more in order to justify the cost and risk of a SAC case.

mile and operating costs. The evidence could then focus on the traffic group chosen and the reasonableness of assumptions about traffic and revenue growth, with tight timeframes for the presentation of evidence and a decision.

B. The Board Might Investigate a Number of Changes to Improve Its Processing of Small Rate Cases

The Board might investigate a number of changes to its current *Small Case Guidelines* to improve its processing of small rate cases.

1. The Board should establish some type of “bright line” test for determining when a case is to be adjudicated under its “small case” standards. The current rules require the shipper to submit evidence to demonstrate that the use of CMP is not feasible – an uncertain, unnecessary, and potentially expensive exercise. The League believes that a tonnage test per origin-destination pair should be used. If there is some dispute as to the tonnage at issue, then the railroad (which already has tonnage data for the movement), should have the burden of showing that the test is not met.

2. The Board needs to examine very carefully how it can reduce the time it takes to adjudicate small cases. The League believes that the Board should aim for a four-month processing time, from the filing of a complaint to a decision. In its recent decision in *Expediting SAC Cases*, the Board has asked about the feasibility of standard discovery requests. It should do the same here. For example, a complainant might be required to file, with its complaint, certain discovery on use of alternative transportation modes between the origin and destination, and the railroad might be required to file standard cost information within 10 days of the filing of a complaint. Access to the confidential waybill sample should be provided before the filing of a complaint, upon certification that the request is for a complaint under Section 10701. Motions to

compel could be expedited as the Board has recently done in its decision in *Expediting Resolution of SAC Cases*. Legal argument could be filed with the evidence, to avoid post-evidence briefs. The Board might investigate whether the use of ALJ's to manage and decide a case would result in faster processing. If so, the Board might assign such cases to ALJs, with a high standard of review by the Board to avoid the expense of *de novo* review. The Board needs to commit itself to rendering a decision very promptly after the submission of evidence.

3. If the Board is committed to its current decision standards set forth in *Non-Coal Guidelines*, it needs to give the shipping public some better sense of how they will be applied. The Board should also investigate whether simpler and more realistic standards, rather than complex and expensive rail costing that can only be presented by an expert, might be better. For example, the Board might rely on rate comparisons more directly, rather than the R/VC_{comp} "benchmark."

4. In its Comments in Ex Parte 586, the League strongly supported the use of mandatory, expedited arbitration to simplify and speed rail rate and service disputes. The League continues to believe that the use of mandatory, expedited arbitration is the best way to simplify and shorten rate disputes, leaving the Board to set policy and procedures for arbitrators to follow in resolving such disputes. The League suggests that the Board take the lead in recommending to Congress legislative change that would permit mandatory, expedited arbitration.

IV. CONCLUSION

The League commends the Board for initiating this inquiry, and offers its future cooperation in developing more effective rules for small and medium-sized rate challenges.

Respectfully submitted

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