

**Before the
SURFACE TRANSPORTATION BOARD
Washington, DC 20423**

MAJOR ISSUES IN RAIL RATE CASES) Ex Parte No. 657 (Sub-No. 1)

**Comments of
ALBEMARLE CORPORATION**

Albemarle Corporation ("Albemarle") respectfully submits its comments concerning the procedures utilized by the Surface Transportation Board ("STB" or "Board") in assessing the reasonableness of railroad rates and charges under the stand-alone cost ("SAC") test. These comments are submitted in response to the Decision issued by the Board February 27, 2006.¹

I. Statement of Interest

Albemarle is a Virginia corporation, with administrative offices located at 451 Florida Street, Baton Rouge, Louisiana, 70801. Albemarle operates chemical production facilities at seven (7) locations throughout the United States, as well as plants elsewhere throughout the world.

Albemarle currently is engaged in litigation before the Board with The Louisiana and North West Railroad ("LNW") in two proceedings, Docket No. 42096, Albemarle Corporation—Petition for Declaratory Order—Certain Rates and Practices of The Louisiana and Northwest Railroad Company, on referral from the United States District Court for the Western District of Arkansas concerning LNW's switching, storage and weighing rates, charges and practices, and Docket No. 42097, Albemarle Corporation v.

¹ 71 Fed. Reg. 11015 (Mar. 3, 2006).

The Louisiana and Northwest Railroad Company, concerning LNW's linehaul rates. In both proceedings (or in a consolidated proceeding) LNW expects to use the SAC methodology. LNW is a Class III carrier.

II. Comments

Albemarle comments on the issues raised by the Board and other issues of interest to Albemarle, as follows:

1. Percent Reduction Methodology

In recent applications of the SAC constraint to determine maximum reasonable rail rates, the Board has used a percent reduction methodology whereby, when the aggregate revenues produced by the incumbent's rates exceed stand-alone costs, *all* rates in the stand-alone shipper group are assumed to be reduced by the same percentage in order that the reduced rates in aggregate are equal to stand-alone costs.

The percent reduction method allows the carrier to manipulate the stand-alone cost system in that it can simply publish a rate on the issue traffic at such a high level that when all rates are reduced to stand-alone costs the issue traffic rate is still at a level which is exceedingly high. This is illustrated by a hypothetical expiring contract rate of \$10 where the carrier desires a \$4 increase but in negotiations the shipper will not agree to any more than a \$2 increase and as a result the parties cannot agree to a new rate. The carrier then publishes a \$20 rate which is contested by the shipper in a formal complaint. When a stand alone traffic group is formed from the carrier's existing traffic group and the group's aggregate revenues exceed the stand-alone cost of service to the traffic group by 25% then the percent reduction methodology would reduce the published rate by 25% to \$15, or a level higher than that offered by the carrier in negotiations. Thus even

though the shipper has demonstrated that the published rate is too high, the shipper has not been provided any relief from the excessive rate level.

The Board proposes to replace the percent reduction methodology with either the Maximum Contribution Methodology (“MCM”) or the Maximum Markup Methodology (“MMM”). The Board states that both approaches would calculate a maximum contribution from each movement in the traffic group such that the total contribution from the traffic group would equal the total SAC cost and with no shipment assigned a contribution higher than the current rate charged for the movement.

A. Maximum Contribution Methodology

Under the MCM method, the Board states that it would assume that the current rates charged for the non-issue traffic reflect profit-maximizing rates. If a movement’s share of the SAC cost is higher than what is actually charged, the MCM approach would reapportion the difference between the current rate and its share of SAC costs to the remaining traffic in the SAC traffic group, which would increase the contribution level from the remaining traffic.

Through this application, the STB proposes to maintain the relationships among the individual rates charged and thereby protect the issue traffic from monopoly pricing practices and guard against any cross subsidy arising from reducing the already low competitive rates below the cost of providing the service. At the same time the Board indicates that the carrier would have the opportunity to earn adequate revenues by permitting demand-based pricing, up to the level of stand-alone costs for the traffic group.

In contrast, using the percent reduction methodology an across-the-board

reduction could cause the competitive rates in the traffic group to fall below the carriers' cost of providing service, thus creating a cross-subsidy which is in violation of CMP's Management Efficiency Constraint. This Management Efficiency Constraint states that the carrier cannot force captive traffic to cross-subsidize competitive traffic that moves at rates that are less than marginal costs. Moreover, the Board contends the MCM approach requires the carrier to recover as much of its costs as possible from each shipper before charging higher rates to its captive shippers.

In theory, the MCM method appears to make sense and to provide the complaining shipper some protection from a carrier who is attempting to manipulate the system. However, depending on the characteristics of the other shipments that are available for the shipper to include in its traffic group, it is possible that the MCM method will cause the issue traffic to bear an unreasonable burden. For example, if the carrier is charging far less than stand-alone cost to others in the traffic group and no other traffic is available for inclusion in the traffic group, then the issue traffic can be made to not only bear the burden of the cost of providing its service, but also that of the other traffic comprising the traffic group. Albemarle believes that it is not appropriate to uniformly mandate a specific methodology and thereby eliminate other methodologies that in a specific proceeding produce a more appropriate result.

B. Maximum Markup Methodology

Alternatively, the Board proposes the MMM approach for those instances where the traffic group is diverse and comprised of various disparate volumes and handling characteristics. In this instance under the MMM approach, the parties would determine the variable cost of each shipment in the traffic group using URCS and then express the

maximum contribution towards SAC cost as a markup above variable cost. The Board states that in no instance would the rate be set above the existing rate, even though the current rate may be less than the average markup above variable cost. The MMM approach proposed by the Board is not appropriate for Albemarle as there is no URCS available for a Class III carrier.

Finally, from the Board's February Decision it is not clear how the Board intends to actually determine the rates under either the MCM or MMM methodology. For this reason and because the specific characteristics of the stand-alone traffic group will vary from proceeding to proceeding, the appropriate methodology for determining a maximum reasonable rate should be determined on a case-by-case basis.

2. Cost-based methodology for Allocating Divisions of Revenue to Cross-over traffic

The cross over division allocation does not pertain to Albemarle as the rates apply only to LNW's rates on Albemarle's traffic between the interchange point and Ethyl, Arkansas, or LNW's actual division of revenue on other traffic in the stand-alone traffic group. There is no interchange of traffic on the LNW line except at its interchanges with the Class I carriers at the limits of LNW's service.

3. Productivity as measured by the Rail Cost Adjustment Factor ("RCAF")

The STB has proposed to phase productivity in throughout the life of the Discounted Cash Flow ("DCF") analysis by using 100% of the RCAF unadjusted by productivity ("RCAF-U") and 0% of the RCAF adjusted for productivity ("RCAF-A") in the first year of the model, then in each subsequent year using 5% less of the RCAF-U and 5% more of the RCAF-A. For example in year 2 of the model operating expenses would be increased by 95% of the RCAF-U and 5% of the RCAF-A.

This approach used for all proceedings has no recognition of the specific productivity that may or may not be available in a particular stand-alone cost proceeding and as such is arbitrary and capricious. A stand-alone carrier must be able to capture the same amount of productivity that is available to the railroad industry as long as the productivity is not already built into the SARR system. For example, if new techniques are available in railcar design and shippers are providing the railcars, to the extent that the industry gains from this productivity so should the SARR. The same is true with regard to gains in productivity made through traffic growth, increase capacity of railcars, the ability to sell or lease existing locomotives to others in order to take advantage of newer more efficient locomotives, etc.

It is inappropriate to pre-judge all proceedings by stating the specific amount of productivity that can or cannot be achieved by a stand-alone carrier.

4. Elimination of movement specific adjustments to the Uniform Railroad Costing System when calculating the 180% jurisdictional threshold for rail shipments

The Board proposes to do away with movement-specific adjustments to the system-average unit costs in rate reasonableness cases. This would be a departure from the practice recognized throughout SAC adjudication proceedings by both the Interstate Commerce Commission ("ICC") and the Surface Transportation Board ("STB") wherein movement-specific variable costs have been a cornerstone of rate reasonableness proceedings since adoption of the Uniform Rail Costing System in 1989.²

The basis for the proposal is a graph placed into evidence by the defendant

² *Adoption of the Uniform Rail Costing System as a General Purpose Costing System For All Regulatory Costing Purposes*, 5 I.C.C.2d 894 (1989) ("URCS Proceeding").

railroad in the Xcel rate proceeding³ that purported to show the variability relationship between Total (Road Property Return and Depreciation) Cost and Total GT (i.e., Gross Tons of traffic density). It is Albemarle's understanding that the variability example cited in reliance on for this proposal not only is at odds with the ICC's *URCS Proceeding* but moreover was a litigation position that has not been validated as a proposition of general applicability. Albemarle understands that other parties will address the deficiencies in the proposal in detail. Albemarle urges the Board to refrain from adoption of this aspect of its proposal until sound reason has been presented to depart from the decisions made in the *URCS Proceeding*.

5. Stand-Alone Cost Analysis Period

The STB and its predecessor agency, the Interstate Commerce Commission, have used a multi-year analysis rather than a single year analysis when determining stand-alone costs. The Board has used a multi-year analysis in order deal with the effect of taxes and to accommodate the impact of business cycles. The Board uses a DCF analysis to compare the revenue requirements of the SARR against the total revenues generated by the traffic group over the full SAC analysis period.

Historically, the Board has used a 20-year analysis period; however, the Board now believes that the analysis period should be shorter than the 20 years and proposes to use a 10-year analysis period, for five reasons. First, the Board believes that as a practical matter the benefits of a 20-year analysis and potential rate prescriptions do not last longer than 10 years because of changes in circumstances surrounding the issue traffic and the stand-alone traffic group.

³ *Public Serv. of Colorado d/b/a Xcel Energy v. Burlington N. & S.F. Ry.*, STB Docket. No. 42057 (served June 7, 2004).

Second, the Board has determined that the average business cycle is much shorter than 20 years and can be captured within a 10-year analysis period. Third, the Board believes that the shorter period would reduce the expense and complexity of the SAC analysis by limiting disputes over forecasted trends in traffic volumes, revenues, and operating expenses. Fourth, a shorter period for the SAC analysis and resulting rate prescription period would conform its regulatory process to the trend in the rail industry towards shorter contract terms. Finally, the Board believes that its proposal would remove the need for shippers to hypothesize a stand-alone carrier with sufficient infrastructure to handle traffic forecasts that might be realized decades into the future.

While Albemarle appreciates the reasons underlying the Board's proposal to shorten the SAC analysis from 20 years to 10 years, it believes it is incorrect to mandate the use of a 10 year period for all proceedings. There are instances where a proceeding may have long standing and a 10 year SAC analysis may cover only the period that the proceeding has been pending. If this is the case, it would not provide any prospective relief to the complainant.⁴ For these reasons, Albemarle believes that the duration of the SAC analysis should be determined on a case-by-case basis and not limit the analysis to a 10-year period when doing so does not square with the needs of the proceeding at hand.

6. Reopening and Vacating Prior Board Decisions

This issue does not pertain to Albemarle's cases.

7. Other Issues

Based on Albemarle's experience with the LNW, Albemarle urges the Board to

⁴ A similar situation was experienced in ICC Docket No. 37809, *McCarty Farms, Inc. et al v. Burlington Northern, Inc.* and ICC Docket No. 37038, *Bituminous Coal – Hiawatha, Utah to Moapa, Nevada*, where the evidentiary record was finally closed considerably more than 10 years after the proceedings were initiated. In these two proceedings the ICC used a 20-year and 25-year stand-alone cost analysis respectively.

consider, in a further proceeding if not appropriate to this rulemaking, issues appropriate to rate adjudication with Class III railroads. The background for these issues is detailed in Albemarle's pleadings in the Docket 42096 and 42097 proceedings. Namely, these issues concern the opportunity for holding Class III carriers which are independently owned and thinly capitalized accountable for rate actions which are extortionate in nature. Illustrative is the LNW's cancellation of track lease arrangements and substitution of a "holding charge" of \$1,000 per car, per day, a charge which could yield a 20,000% increase over the fees previously paid by Albemarle.

First, where solely tariffs are involved,⁵ the customary procedure is for the shipper to pay the disputed charges and seek reparations. Where the Class III railroad is thinly capitalized and the disputed amount may run far in excess of its assets, there exists the potential that the railroad may distribute excess charges to its owners prior to a final adjudication in an effort to avoid accountability.⁶ Albemarle urges the Board to establish policies where there is the potential that a remedial order may be frustrated and reparations which may be ordered may not be available to be paid for a protective order to be issued requiring that the funds in dispute be held in escrow.

Second, as suggested by the \$1,000 per car, per day storage charge, there may be situations where a carrier can impose charges so outrageously high to constitute an effective embargo. While the Board has indicated that it will not use its remedial powers to order substituted service to address rate situations, Albemarle urges the Board to recognize that charges which constitute a *de facto* embargo may be remedied through

⁵ The Docket No. 42096 proceeding arose out of notice of termination of contracts, which were contested in judicial proceedings, and LNW's attempt to substitute the referenced tariff in its place.

⁶ Albemarle is not making an accusation concerning LNW, but rather raises this issue out of prudence in protecting its corporate assets.

substitution of service rather than under the rate case procedures. Relevant factors to consider may include an extraordinarily high rate increase and/or revenue-variable cost ratio of the rate,⁷ and the charges offered by a substitute carrier to handle the transportation service.

Third, Albemarle urges the Board to distinguish between the type of rate case involving Class I carriers which the Board customarily sees and smaller cases involving Class III railroads. Certainly, the cost attributable to handling a coal transportation case involving a 1,000 mile stand-alone railroad hauling multiple unit trains of coal per week for the complaining shipper and hundreds of thousands of cars traveling that same line for other shippers is far in excess of the cost to handle a case involving a sixty-some mile railroad handling 5,000 cars per year total for all shippers on the line.⁸ Since the filing fees should not serve as a barrier to adjudication before the Board, the Board should differentiate in its fees between the typical SAC proceeding and one involving a Class III railroad. The Board further should consider measures it may be able to take to expedite such "small" SAC proceedings.

⁷ The R/VC for the aforementioned \$1000/car/day storage charge is estimated to be 100,000%. The rate increase on the switching charges at issue in Docket No. 42096 is greater than 300%.

⁸ In relative size, the annual ton-miles for a 127 car unit coal train of 100 ton cars traveling 1000 miles is 1,981 million ton miles for the issue traffic alone. The annual ton-miles for a 62 mile railroad handling 5000 cars of 100 tons for all customers on the line, with routings of approximately 20 or 50 miles depending on junction and location, is 17.5 million ton miles. Before taking into account cross-over traffic for the coal SARR, the coal case is more than 100 times greater in scope than the short line case.

WHEREFORE, THE PREMISES CONSIDERED, Albemarle Corporation
requests the Surface Transportation Board to adopt rules and policies in accordance with
the views set forth above.

Respectfully Submitted,

ALBEMARLE CORPORATION

By: 

Martin W. Bercovici

bercovici@khlaw.com

KELLER AND HECKMAN LLP

1001 G Street, N.W.

Suite 500 W

Washington, DC 20001

202-434-4144

202-434-4646 (fax)

Its Attorney

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