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Common Carrier Obligation Hearing: July 22, 2008

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On April 25, 2008, in Ex Parte No. 677, the Surface Transportation Board held a hearing to examine the scope and application of the common carrier obligation in a variety of contexts. In the ASLRRA's written comments for that hearing, the Association identified the transportation of hazardous materials as a particularly troublesome issue insofar as the scope of the common carrier obligation is concerned. At that time, the ASLRRA urged all stakeholders (i.e., carriers, manufacturers, shippers and the government) in the movement of hazardous materials that are toxic/poisonous by inhalation (TIH) to seek creative solutions to address the risks and liabilities associated with handling those commodities.

The ASLRRA is pleased to have the opportunity to participate in this proceeding to specifically address the application of the common carrier obligation to hazardous materials. Our comments focus on the transportation of TIH, and propose a framework under which the stakeholders in TIH transportation share in the liability risks presented by TIH.

Background

TIH is unique in terms of its potential to cause harm. The claims in the Graniteville incident (the breach of a single chlorine car, at night, in a rural area), estimated to be in excess of \$500 million, are approximately 100 times the annual revenue of the typical Class III railroad. The Graniteville claims, while devastating, would be dwarfed by those arising in a multiple-car incident during rush hour in an urban area. There is no other commodity handled by railroads that has the potential to cause even a fraction of the losses that would result from even a minor TIH release.

Although small railroads generally are well-equipped to handle the risks related to common carrier freight operations, these railroads simply cannot manage the extraordinary risk presented by TIH. Small railroads do not have the financial resources, and cannot reliably obtain insurance coverage, to address claims in the hundreds of millions of dollars, let alone claims in the billions of dollars. A TIH incident on a Class III or Class II railroad likely would bankrupt the carrier and leave vast numbers of people without a remedy for losses resulting from injury, death or destruction of property.

In light of the disproportionate risks to the public presented by TIH, and the limited financial resources of small railroads, an unconditional requirement that small railroads carry those commodities does not serve the public interest. On the other hand,

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ASLRRA recognizes it is in the public interest that rail transportation be available for TIH. Therefore, a balance must be reached between the obligation of small railroads to handle traffic tendered by TIH shippers and the inherent limitations on those carriers to manage TIH risks.

Fortunately, the common carrier obligation is not *unconditional*. Section 11101 of the ICC Termination Act requires that a railroad provide service upon *reasonable* request. The ASLRRA believes that it is *not reasonable* to force a small railroad to bear 100 percent of the risk associated with TIH movements, when it is beyond dispute that a small railroad does not have the financial resources to manage such risk.

Both court and agency decisions indicate that the Board has the discretion to determine the scope of the common carrier obligation¹. The ASLRRA respectfully urges the Board to use its discretion to determine that it is reasonable for a small railroad to condition its willingness to handle a TIH shipment on the existence of a liability-sharing arrangement, as described below, that protects the public from TIH risks. In crafting a proposal for such an arrangement, the ASLRRA has attempted to create a framework that balances several factors: a participant's financial resources; the financial benefits the participant derives from the TIH movement; and the responsibility of the participant to protect the public.

The ASLRRA Liability-Sharing Proposal For TIH Movements

ASLRRA hereby proposes that, if the small railroads satisfy certain minimum insurance requirements, they be permitted to publish a tariff that conditions their obligation to carry TIH on the other stakeholders similarly assuming certain insurance and liability obligations. In other words, if the other stakeholders in a TIH move agree to the conditions in the tariff, the request for service is reasonable, and the small railroad is bound by its common carrier obligation. However, if the other stakeholders choose not to comply with the conditions, then the small railroad is not *required* to serve the TIH shipper. In order to implement this proposal, the ASLRRA urges the STB promptly to issue a policy statement that interprets the term "reasonable request," as applied to TIH shipments, in a manner consistent with this proposal.

¹ See *Granite State Concrete Co., Inc. v. Surface Transportation Board*, 417 F.3d 85, 92 (1st Cir. 2005) ("Granite State") (noting that the Board "has been given broad discretion to conduct case-by-case fact-specific inquiries to give meaning to [the phrase "adequate service on reasonable request"]"); *Terminal Warehouse Inc. v. CSX Transportation Inc.*, 175 Fed. Appx. 715, 718-19 (6th Cir. 2006) (noting "[t]he STB has discretion in determining whether an entity has made a reasonable request for service") (citing *Granite State*); *Classification of Ratings of Chemicals, Comail*, April 30, 1986, 3 ICC 2d 331, Dec. 19, 1986 (stating the ICC "has discretion to determine if there may be limitations on a carrier's tariff publication/common carrier obligation"). See also *WFL Rail Corporation Petition for Declaratory Order and Interim Relief, WFL Rail Corporation Petition for Partial Revocation or Exemption*, STB Docket Nos. 42092 and 230(Sub-No. 9), served February 17, 2006 (stating, in the analogous context of an unreasonable practice, that "[t]he statute does not specifically define what constitutes an unreasonable practice," and that "Congress has committed such determinations to the Board")

Insurance Requirement for Small Railroads

In order for a small railroad to be able to publish a tariff that conditions its handling of TIH on the criteria below, (A) a Class III railroad must have liability insurance coverage with a minimum limit that equals or exceeds the lesser of (i) 200% of its freight revenue,² and (ii) \$25 million, and (B) a Class II railroad must have liability insurance coverage with a minimum limit of \$25 million.

Criteria for interline TIII moves with a Class I railroad:

1. The Class I railroad must have liability insurance coverage in an amount the Board determines.³ The policy must name the Class III or Class II railroad as an additional insured for interline moves of TIH. In the event of a loss-producing incident on or caused by the Class III or Class II railroad, the insurance of the Class III or Class II railroad would be the primary coverage.
2. To the extent that the Class I railroad's insurance policy has an attachment point that is greater than the limit on the Class III or Class II railroad's insurance policy, the Class I railroad would indemnify the Class III or Class II railroad for TIH-related losses that fall within the coverage gap.
3. The TIH shipper must have excess insurance in an amount the Board determines,⁴ which coverage attaches at the limit of the Class I railroad's insurance policy. The excess policy must name the Class III or Class II railroad as an additional insured unless the Board determines that it is commercially unreasonable to do so based on insurance industry capacity limitations for TIH hazards.
4. The TIII shipper must indemnify the Class III or Class II railroad for TIH-related losses above the limit of the shipper's excess insurance policy.

Criteria for TIH moves that do not involve a Class I railroad⁵

² This requirement should be based on the carrier's average freight revenue over the preceding three, full calendar years

³ ASLRRRA understands that, based on *current* market conditions, liability insurance should be available for Class I railroads in the \$500 million to the \$1 billion range

⁴ ASLRRRA understands that, based on *current* market conditions, excess liability insurance should be available for TIH shippers in the \$500 million to the \$1 billion range

⁵ ASLRRRA does not believe there are many small railroads that carry TIH in moves that do not involve a Class I railroad

1. The TIH shipper must have liability insurance coverage in an amount the Board determines will protect the railroad and the public and is commercially available in the insurance marketplace.⁶ In the event of a loss-producing incident on or caused by the Class III or Class II railroad, the Class III or Class II railroad's insurance policy would be the primary coverage, and the TIH shipper's coverage would attach at the limit of the small railroad's insurance policy.
2. The TIH shipper would indemnify the Class III or Class II railroad for TIH-related losses that fall into the coverage gap, if any, between the Class III or Class II railroad's policy limit and the attachment point of the shipper's policy.
3. The TIH shipper must indemnify the Class III or Class II railroad for TIH-related losses above the limit of the shipper's insurance policy.

Discussion of ASLRRRA's Proposal

In order for a Class III or Class II railroad to qualify to issue a tariff that requires interline Class I carriers and TIH shippers to share in the liability for a TIH move, the Class III or Class II carrier first would be required to obtain a sizeable amount of insurance. This requirement would increase the insurance coverage currently maintained by many small railroads, which is in the public interest. In addition, the small railroad's insurance under this proposal is primary. The Class I interline carrier and/or the TIH shipper would become responsible for a portion of the small railroad's liability *only if* the TIH incident produces liability in excess of the small railroad's required insurance limit. The amount of primary insurance this proposal requires a small railroad to maintain is intended to reflect the small railroad's responsibility and commitment to protect the public interest, but also to recognize the inherent financial limitations of a small business and the minimal benefits many small railroads derive from the carriage of TIH.⁷

Under the ASLRRRA's proposal, the next level of risk-sharing for a TIH incident occurring on or caused by a small railroad would be allocated to the Class I interline carrier for the TIH movement, if applicable. The risk-sharing mechanism would focus primarily on insurance coverage. Unlike small railroads, the Class I carriers have the financial resources to obtain insurance coverage that would be adequate for the types of TIH releases that have occurred in the past (*i.e.*, single car ruptures in rural areas). Many Class I carriers likely already have insurance policies that cover this level of liability. The ASLRRRA believes, based on preliminary research, that the cost of adding a small

⁶ ASLRRRA understands that, based on *current* market conditions, liability insurance should be available for TIH shippers in the \$500 million to the \$1 billion range

⁷ Many small railroads do not have pricing authority to establish rates for TIH movements, and their revenue is limited to a fixed per carload allowance that does not compensate the carrier for the risk involved in handling TIH

railroad as an additional insured on Class I insurance policies for TIH movements would be negligible.

To the extent there is a gap between the insurance requirement for the small railroad and the attachment point of the insurance of the Class I interline railroad, the ASLRRRA proposes that the Class I carrier be responsible for the gap amount. This allocation of liability can be justified on several fronts: (1) the insurance costs for a small railroad will be a vastly higher percentage of its annual revenue than those for a Class I railroad;⁸ (2) the Class I railroad typically has pricing authority over the TIH move, and receives a substantially larger amount of the revenue generated by an interline TIH movement than does the small railroad, (3) the Class I railroad has the necessary financial resources to manage the risk of TIH; and (4) if not covered by another stakeholder, a liability claim that falls within the gap amount would be sufficiently high to bankrupt many small railroads and leave the injured public without adequate compensation.

The final component of the risk-sharing arrangement would allocate any excess liability to the TIH shipper involved in the movement. If the TIH movement includes a Class I interline carrier, the liability of the TIH shipper would be triggered only in the event of a truly catastrophic TIH incident. In situations where there is no Class I interline connection, the liability of the TIH industry necessarily would be triggered at a much lower threshold, given the limited financial resources of the small railroad. However, it is reasonable for the TIH shipper to share in the responsibility to protect the public from the inherent risks of its products, especially in light of the fact that the TIH shipper is the stakeholder that derives the most financial benefit from the TIH movement, and is the sole stakeholder in the TIH move that freely chooses to handle TIH (i.e., without any type of legal obligation to do so).

Conclusion

The ASLRRRA has attempted to craft a liability-sharing framework that is workable and equitable, given the financial limitations of small railroads and the immense liability risks that arise from the handling of TIH. The ASLRRRA acknowledges that, although its proposal will provide adequate coverage for the vast majority of TIH incidents, it likely would not be sufficient to address all losses arising from a significant TIH spill in a metropolitan area. In order to address that situation, the ASLRRRA urges the Board to support a legislative solution similar to the Price-Anderson approach. The Association looks forward to hearing and discussing any other proposals that address the difficult and unique issues small railroads face when they are forced to carry TIH.

⁸ In addition, small railroads cannot afford (and often are contractually prohibited from) having any significant amount of self-insurance. This limitation makes it much more expensive to increase the insurance limit on a small railroad's policy.