

Washington, D.C. Update

Southwest Association of Rail Shippers
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Presentation Outline

- A New Administration and New STB
- Inflation, Courts, Border, Crime, Education, Foreign Affairs – But Gasoline Prices Coming Down, Unemployment Rate Is Low, and Administration Has Some Legislative Victories
- Big Picture Washington, DC Issues
- Mid-Term Elections – Setting the Stage for 2024?
- Rail Service Issues at the STB—Demurrage/Fee Decisions, Shipper Petition Governing Private Railcars (EP 768) and Now EP 770, Urgent Issues in Freight Rail Service
- Rail Competition Issues at the STB
- Rail Rate Issues at the STB (including InterVISTAS, TRB)
- Revenue Adequacy at the STB (Including RR Pet'n in EP 766)
- RR Petition re: Cost-Benefit Issues (EP 752)
- Fuel Surcharge Issues at the STB and in the Courts

A New Administration and STB

- Elections (especially Presidential elections) matter
- Conservative (6-3) Supreme Court less deferential to agencies
- A new STB since most policy issues were decided. Members (Fuchs (R) and Oberman (D)) arrived in 2019, Members Primus and Schultz in 2021, and Member Hedlund in 2022
- Martin Oberman (D) Chairman, Michelle Schultz (R) Vice-Chairman
- Policy matters of interest to shippers were delayed
- Hearings held (in 2019) on demurrage/fees, final decisions issued, and, already in 2022, in CSX/Pan Am merger, Amtrak, Reciprocal Switching, Urgent Issues in Freight Rail Service, CP-KCS merger
- Administration pro-regulatory attitude, RRs oppose change
- STB staffing down
- Shipper visits to STB matter!

Inflation, Spending, Border, Crime, Education, Infrastructure, Foreign Affairs, Climate Change Bill

- While inflation may have more than one cause, governmental spending has to have had a major role
- Supply-chain issues are also a factor, with a myriad of causes, but unemployment rate is historically very low
- Fuel prices are also a factor, of course, which should have been a big benefit for the railroads
- Border issues are Administration's, especially after S Ct decision upholding elimination of "Remain in Mexico" policy
- Bipartisan deal on gun issues, infrastructure, CHIPS Act, climate change treaty, possibly permitting reform, spending, offer hope for Parties and Administration working together in the next Congress
- Chaotic withdrawal from Afghanistan, Ukraine, China are troubling for Administration, although the President has led an improvement in NATO cooperation, defense funding, aid to Ukraine

Big Picture Washington, DC Issues

- Perception that Congress isn't getting much done.
- Reality is that Congress has enacted a lot of bills with spending increasing debt by \$4.8 trillion by 2030.
- “Whenever the legislature is in session, every man's life and property are in danger.”
- Interest on debt has been low, around \$200 billion annually or less, but soon will be over \$500 billion, and heading higher. Will be greater than defense or Medicaid budgets soon.
- Annual interest estimated to be \$1.2 trillion by 2032, as debt grows and grows (now over \$30 trillion).
- That ever-increasing level of indebtedness will cause taxes to rise, spending to fall, or both.

Big Picture Issues – Continued

- By law, Social Security must have a surplus in its Trust Fund, or payments must be reduced.
- Trust Fund will be in deficit by 2034 or 2035, so, by law, payments may be only 75% of what otherwise would be the case, unless taxes are raised or retirement age increased.
- Year-end “extenders” may add another \$1.2 trillion over 10 years.
- All of these issues will make it harder and harder for Congress to agree on spending bills.
- Increasing regulation at virtually every agency.

Big Picture Issues -- Continued

- All of this sets the stage for 2024 Presidential elections.
- As for the mid-term elections, it seems likely that the Republicans will take the House, but the Senate outcome is less clear. History would suggest Republicans will do well, but have hurt themselves with some of their nominees. Trump is obviously a factor.
- Polls have been off since 2016, so predictions are difficult, but a 50-50 Senate today may be as much as 54-46 either way, with a higher likelihood that it will be closer. Now, not a “wave election,” but could change.
- AK, AZ, CO, FL, NC, NH, NV, OH, PA, WA, WI Senate races may go either way, as of now. 33 days to go.

Big Picture Issues -- Continued

- Supreme Court not quite as active on “hot button” issues, but affirmative action, and some Trump-related legal issues may get there, too.
- After *West Virginia v. EPA*, Congress must speak clearly for agencies to regulate on “major issues.”
- The *Chevron* doctrine may also be under reconsideration, meaning agencies may get less deference in interpreting their statutory authority.
- Senate controls judicial confirmations

STB Background Information

- Staggers Rail Act of 1980: deregulation, competition instead of regulation “to the maximum extent possible”
- Abandonments, mergers, deregulatory and pro-RR policies → reduced competition (UP’s economic witness in CP-KCS now admits that “end-to-end” mergers foreclosed competition)
 - 80% of traffic served by one RR
 - Non-jurisdictional contracts for most movements
- “Stand-alone costs” (“SAC”), adopted in 1985, was the only relevant rate standard until recently
- “Revenue-adequacy” constraint, also adopted in 1985, may change that, and could be workable

STB Reauthorization Act of 2015 (S. 808)

Procedural History

- Senator Thune introduced reauthorization bill
- Stripped out pro-shipper substantive provisions of S. 2777
- Shipper associations, RRs supported bill, Senate passed by voice vote
- House passed same bill, President signed

STB Reauthorization Act of 2015 (S. 808)

Summary of Contents

- Makes STB independent (formerly part of DOT)
- Adds 2 new STB board member seats (for total of 5)
- STB Board members may discuss matters w/o public
- Deadlines for rate challenges (which may be unrealistic)
- Encourages STB to resolve pending matters quickly
- More investigatory authority, rates still require complaints
- STB arbitration (for rates) voluntary, damages limited (\$25 million rates, \$2 million service, over five years)
- Instructs STB to consider RRs' investment needs – a sleeper provision (but which Sen. Thune said by letter to the STB was not intended to change law)

STB Reauthorization Act of 2015 (S. 808)

Implications for Shippers

- Bill is largely process-oriented, reflecting Senator Thune's preferences; no real substance in favor of shippers
- Senator Thune, as Chairman, was getting regular reports from STB, STB pushed to implement bill, urged to speed proceedings (except now policy proceedings) – but no evidence that Chairman Cantwell doing same
- STB's increased investigation authority perhaps will be useful for service problems, but what more can the STB do? (Its informal inquiries apparently were quite helpful.)
- There is a great need for shippers to educate Members of Congress about problems with STB processes

Rail Service Issues at the STB

- At CSX, Hunter Harrison implemented the same “precision scheduled railroading” (“PSR”) system he implemented at the IC, CN, and CP. Successor Foote following same approach
- PSR -- serious impacts on service, which Covid worsened
- IC, CN, and CP are straight-line RRs
- BNSF, CSX, UP, NS -- “spaghetti bowls” – different RRs than IC, CN, CP – and the “Big 4” RRs have had serious service issues?
- STB is monitoring service on the Class Is, in response to letters from the auto and farm industries and other shipper groups:
https://www.stb.gov/stb/elibrary/NDP_Correspondence.html.
- STB rulings on demurrage/storage fees – practical meaning?
- EP 770, Urgent Issues in Freight Rail Service – STB gets it; the STB has ordered all Class Is to submit service-related information every two weeks

Demurrage/Accessorial Charges

- STB issued policy decision in EP 757. Also issued decisions in EP 759, EP 760.
- Board's statements critical of RRs, sympathetic to shippers, BUT no hard-and-fast rules. Shippers advocate more specificity.
- Board's over-arching point – demurrage is intended to promote efficient utilization of railcars.
- If “free time” too short, Board disapproves. Seems at least 24 hours to load, unload, maybe even 48 hours to unload, might be intended.
- “Bunching” or other RR-caused events -- no demurrage or storage charges.
- Railroads must provide more detail with invoices, and generally be fair in dispute resolution, especially in providing information.
- Shippers have proposed rules governing use of private railcars (EP 768) -- “demurrage-like” penalties that would be due after 72 hours

Rail Competition Issues at the STB

Procedural History

- Abandonments, mergers, lack of competitive switching as in Canada → rail-to-rail competition is often totally lacking, or at best ineffective
- EP 711: NITL petition for rulemaking
- STB required NITL to do study, hearing held in March 2014
- STB proposed rules July 2016 (in EP 711 (Sub-No. 1))
- Opening comments Oct. 2016; reply comments Jan. 2017
- Under new statute, Board Members may meet ex parte with public. Some meetings have occurred
- Our client INEOS was the first to attend, in early Feb.; meeting summaries on STB website. Based on INEOS meetings and others, discussion of particular circumstances matters greatly
- Shippers supportive, rail labor not; railroads have met with Board Members, and are vehemently opposed
- Board has not said when rulemaking will conclude, but record is closed; Chairman Oberman, Member Primus support, perhaps Member Hedlund, too; Members Fuchs and Schultz may be opposed

Rail Competition Issues at the STB

Summary

- STB proposed two standards, tracking statute:
 - (1) practicable and in the public interest, or
 - (2) necessary to promote rail-to-rail competition
- Much complexity to first prong, but second may be workable for shippers who can show “market dominance”
- This second approach could work for more shippers, provided rates are over 180%, they are otherwise market-dominant, and there is a safe, efficient, non-congested interchange with which to interchange traffic on the competitor RR within a reasonable distance of shipper’s plant

Rail Competition Issues at the STB

Implications for Shippers

- Could help some shippers, but lots of complexity
- Shippers should advocate:
 - (1) simple, *prima facie* affirmative case, based on publicly available information, for competitive switching; if made,
 - (2) burden shifts to RR to show (if it can) that remedy not safe, or practical, or adversely impact other shippers, or other reasons
- Then limited discovery, only on matters RR puts at issue
- Shipper can then rebut RR showing
- Approach does not work for small shippers (due to cost), and short-lines exempt; need to find ways to expedite
- STB apparently regards 2% of RR revenues as significant, so apparently it does not intend this approach to apply to too much traffic; need to change STB's mindset on that
- AAR filed 612 pages of comments in opposition, and each Class I and ASLRRRA filed comments also opposed

Rail Rate Issues at the STB

Status Update

- Challenges to “stand-alone cost” methodology
- EP 665
 - Sub. 1: Considers new rate-challenge process for grain shippers
 - Sub. 2: ANPRM re: rate reasonableness methodology for very small disputes (STB rejected proposals by shipper groups)
- Coal-rate challenge – *Consumers Energy v. CSX* (NOR 42142) – raised “revenue adequacy constraint” issue; decided in Jan. 2018; with CSX “revenue-inadequate” according to STB (but other proof allowed), STB determined “constraint” did not apply; dismissed due to settlement
- Recently, WCTL filed a petition in EP 722 seeking action on “revenue-adequacy constraint”
- Past Board Member decisions indicated deep unhappiness with SAC; STB Staff Rate Reform Task Force Report delivered in 2Q’19; in 2019, STB proposed “final offer” rate determinations for small shipments (up to \$4 million damages) in EP 755
- RRs proposed STB arbitration, RR which opts in would not be subject to FORR
- “Bundling issue” discourages rate challenges
- Recently, OPPD filed complaint against UP over coal rate

Rail Rate Issues at STB: InterVISTAS and TRB Studies on Stand-Alone Cost Methodology

- Commissioned under S. 808, submitted in 2016
- Independent assessment of STB's SAC rate methodology and identify possible alternatives
- Conclusions (favor RRs by recommending status quo):
 - Full SAC remains preferred approach in many cases
 - Simplified SAC and three-benchmark test are upheld as well
 - Definition of “most efficient network” could be simplified
 - Suggests reducing the contribution of cross-over traffic
- TRB Authored Its Own Report – Very Critical of STB

Transportation Research Board Report – June 2015

- Report commissioned by Congress; issued in 2015
- STB processes dysfunctional, urges replacement with “baseball arbitration,” quick resolution
- Fails to address Constitutional issues, appeals to STB, judicial review, discovery, standards (except a competitive benchmark approach, undefined)
- Would require replacement of Uniform Rail Costing System methodology, and there would be winners and losers; STB recently issued procurement docs to seek experts’ assistance to revise URCS
- Report was useful to convince STB to propose “final offer” determinations up to \$4 million in damages

Rail Rate Issues at the STB

Implications for Shippers

- SAC challenges – not workable for chemical shippers with single-car or multi-car shipments
 - (*M & G* settled; *Dupont v. NS*, *Sunchlor Belt Alkali v. NS*, and *Total v. CSX* all adverse to shippers)
- Ex Parte No. 665 (Sub. No. 1) proposal: challenges more difficult and more costly for all shippers, not just grain
- Ex Parte No. 665 (Sub. No. 2):
 - Acknowledges that “three-benchmark” methodology may not work because transaction costs may exceed amounts at stake
 - Proposal would only apply to Class I RRs – but what if “the last mile” is spun off to Class II or III?
 - Vice Chairman Miller: adjusting “3-B” methodology would do nothing to solve problems with the SAC methodology, because it would apply only to small shipments (and 3-B may not work, anyway)

Revenue Adequacy Status Update

- “Revenue adequacy” standards are not realistic; STB hearings in EP 761, 722 Dec. 2019 to hear proposals; shippers proposed competitive benchmark standard for revenue-adequate RRs
- “Revenue adequacy” rate constraint must be defined; STB considering improvements to Cost of Capital methodology (EP 664); no deadline (“TBD”) but new RR-instituted CoC proceeding underway (EP 766)
- Replacement costs used in SAC because hypothetical RR. Not used for actual RRs’ costs, or for revenue adequacy
- Matt Rose: CoC was 7% in 2018. Had 7% been STB-determined CoC, all 7 Class Is would have been revenue-adequate. All but NS rev-ad in 2020, NS close

Revenue Adequacy

Implications for Shippers

- Shippers advocate alternatives to SAC, argue not only economically justifiable measure for determining rate reasonableness; STB Rate Reform Task Force agreed, Board Members Begeman and Miller seemed to agree. New Board Members?
- Railroads have defended ICC/STB determinations that SAC is the only economically rational methodology for setting rail rates
- Task Force proposed incumbent RR cost-based methodology as alternative to SAC
- Also proposed to revise “3-Benchmark” methodology; Board has now proposed “final offer” (“FORR”) in EP 755, 665 (Sub-No. 2)
- Board has not yet proposed changes to SAC, but did also propose to “streamline” market dominance determinations (through limiting length of some pleadings) in EP 756
- “Revenue adequacy constraint” may offer real rate relief for many shippers

Cost-Benefit Analysis Applied to All STB Notice-and-Comment Rulemaking Proceedings?

- On March 14, 2019, AAR filed Petition for Rulemaking (EP 752) seeking rule requiring cost-benefit analyses in STB notice-and-comment rulemaking proceedings.
- Various shipper groups filed replies opposing – in part -- the AAR Petition, but expressing some support for the concept.
- STB postponed decision to institute a rulemaking proceeding.
- Petition intended to delay action in proceedings that could benefit shippers, create record allowing railroads to challenge the Board's actions, whatever STB found, on the ground that the cost-benefit analysis was erroneous, so grounds for appeal and delay.
- Petition seems particularly directed at EP 711 (Sub-No. 1), Reciprocal Switching, where cost study of proposed rule was submitted years ago, but railroads argue needs updating.
- Any such rule would create additional grounds for appellate challenge of STB actions.

Fuel Surcharge Issues

Status Update and Shipper Implications

- Cargill proved BNSF over-recovered but no relief
- “Safe harbor” concept intended to benefit shippers
- STB was not bound to deny relief to Cargill
- STB: alter policy to avoid over-compensating RRs
- Record completed in 2014, but no action (“TBD”), so in 2019, WCTL filed in DC Circuit (No. 19-1080) for mandamus
- Court set matter down for oral argument
- STB then terminated the proceeding because the three Board Members could not agree; Chairman Begeman: get rid of “safe harbor” rule. DC Circuit affirmed
- Fuel surcharge antitrust case (includes contracts and exempt traffic) -- class-certification was denied by DC Circuit in 2019
- Many shippers were able to file individual complaints

Conclusions

Importance of Shipper Involvement (1)

- Board Members meet with public in EP 704, Exemptions, EP 711 (Sub-No. 1), Reciprocal Switching, and about rail service concerns, among other things
- Competitive switching – competition was presumed in Staggers Rail Act of 1980, but not the result
- RR finances improved dramatically, STB seemingly concedes in recent CoC decision
- Chairman Oberman would like to improve competition
- TRB Report supports need for change on rates
- RRs' arguments for change to CoC, revenue adequacy are not appropriate

Conclusions

Importance of Shipper Involvement (2)

- Rate reasonableness – needs to be an effective alternative to “stand-alone costs” for large disputes – will STB respond? (It has proposed FORR for smaller disputes.)
- Common carrier obligation issues, especially on service
- Pressures that shippers are under have increased because of higher rates, fees, charges
- Until recently, RRs did not have to work to compete or become more efficient to raise revenues; RRs only needed to raise rates, fees, charges, did so inexorably
- Several RRs having achieved revenue adequacy (or close), but non-SAC rate challenges don't work; FORR might, STB arbitration is less clearly useful (what standard?)
- Shippers will need to comment, suggest alternative approaches, participate in upcoming STB proceedings

Q&A

Questions or Comments?

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