

DOB # 010216900, 207613
ORIGINAL

BEFORE THE
SURFACE TRANSPORTATION BOARD

DOCKET NO. 42054

PPL MONTANA, LLC

v.

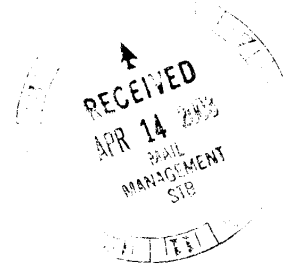
THE BURLINGTON NORTHERN AND SANTA FE RAILWAY COMPANY

PETITION OF PPL MONTANA, LLC FOR RECONSIDERATION
OF DECISION SERVED MARCH 24, 2003

John M. Cutler, Jr.
McCarthy, Sweeney & Harkaway, P.C.
2175 K Street, N.W., Suite 600
Washington, DC 20037
(202) 775-5560

Attorney for PPL Montana, LLC

Dated: April 14, 2003



**PETITION OF PPL MONTANA, LLC FOR RECONSIDERATION
OF DECISION SERVED MARCH 24, 2003**

I. INTRODUCTION

Complainant PPL Montana, LLC ("PPL") hereby petitions the Board for reconsideration of its Decision served March 24, 2003 (hereafter "2003 Decision") in this proceeding. In the 2003 Decision, the Board granted in part and denied in part the petition for reconsideration PPL filed on September 30, 2002 as to the original Decision served August 20, 2002 in this proceeding ("2002 Decision").

In its 2003 Decision, the Board reopened the proceeding for new evidence as to a narrow issue: the manner in which the Board calculated operating expenses attributable to the traffic using the western portion of PPL's stand-alone railroad.¹ PPL is developing its evidence as to this issue and intends to file its opening evidence and argument on May 23 and its rebuttal evidence and argument on August 6, 2003, as provided for in the 2003 Decision.

II. PREFACE AND SUMMARY OF ARGUMENT

PPL's decision to seek reconsideration of the 2003 Decision in this proceeding was not taken lightly. The Board has clearly indicated that it is determined to apply, in future stand-alone cost ("SAC") cases, a prohibition against reliance on a stand-alone railroad ("SARR") that includes any segment over which traffic moves that does not generate revenues sufficient to cover the segment costs. In addition, revenues from non-issue traffic in the stand-alone group will be available to fund the SARR only to the extent that such revenues are needed to cover the costs of portions of the SARR over which such traffic moves.

¹ PPL's use of the Board's "western portion" terminology cannot be read as indicating that the SARR here was designed with discrete segments. PPL designed the SARR as a single line of railroad.

PPL regards this position not just as unprecedented but also as bad law and bad policy. PPL nevertheless believes such arguments are preserved for possible appeal. However, to the extent that the March 24, 2003 Decision asserts new reasons for denying relief to PPL, it is arguably a new decision, and PPL must seek reconsideration of such new rationales by the Board or risk being foreclosed from challenging such rationales on judicial review.

In its 2002 Decision, the Board cited two earlier decisions in support of the proposition that its segment cross-subsidy test was not new. One was a decision served November 27, 2001 in this proceeding, and the other was the decision served December 31, 2001 in STB Docket No. 42058, Arizona Electric Power Coop v. BNSF.

In its petition for reconsideration of the 2002 Decision filed September 30, 2002, PPL pointed out that reliance on these decisions is misplaced, because they were not issued until after the close of the record in this case. PPL argued if the Board were determined to adopt its segment cross-subsidy test, it would be unfair to deny PPL an opportunity to show the absence of a cross-subsidy in this proceeding. In its 2003 Decision, the Board granted reconsideration to the extent of allowing PPL to introduce new evidence on the allocation of operating expenses attributable to traffic using the western part of PPL's SARR, but it rejected PPL's request to introduce new evidence on traffic levels and on levels of investment on the western portion.

In apparent recognition that PPL cannot be charged with knowledge of the Board's new test based on decisions issued in November and December 2001, long after the record closed in this proceeding on May 7, 2001, the Board's 2003 Decision no longer relies on those decisions. Instead, the 2003 Decision denies PPL's request to introduce new evidence as to traffic levels and investment based on a new rationale: that complainant shippers have always had "every in-

centive" to maximize the former and minimize the latter for the SARR "as a whole." 2003 Decision at 8-9.

As shown below, this rationale is inadequate. Even as applied to the SARR "as a whole," it is not correct, in light of statutory limits on the Board's power to order relief from unlawful rail rates, and other factors. In any event, it is a non sequitur to contend that if a shipper has every incentive to maximize traffic and minimize investment over the whole length of its SARR, it also has every incentive to maximize traffic and minimize investment over every segment of its SARR.

The Board's 2003 Decision, like its 2002 Decision, is flawed, and the relief granted was too limited.

III. NEW RULINGS IN THE BOARD'S 2003 DECISION **PROMPT THIS NEW PETITION**

The 2002 Decision denied relief on the ground that a stand-alone railroad is fatally flawed if there is any segment of the hypothetical railroad whose costs are not covered by the traffic transported over that segment. This rule was held to apply even if members of the stand-alone group as a whole, paying the rates actually charged by the defendant railroad, generate more than enough revenue to cover the costs of the SARR, considered as a whole.

The arguments in PPL's September 30, 2002 petition for reconsideration fell into four general categories. First, PPL argued that this holding represented a new approach to stand-alone cost cases that is not warranted by the statute, the case law or economic theory, and should not be adopted by the Board for legal and policy reasons. Second, PPL argued that if this new approach were to be adopted as to future rate cases (and it should not be), it nevertheless could not be applied to deny relief in this proceeding because PPL had no notice of the new approach. Third, PPL argued that if it had known that its SARR would be judged by a standard not applied

to any other SARR in any other decided rate case, it could and would have designed its SARR to satisfy the test, and PPL provided examples of changes it would have made.² Fourth, PPL argued that the Board's finding of a cross-subsidy by non-issue traffic was erroneous, because of the Board's misreading of the record.

To the extent that the Board's 2003 decision rejects PPL's arguments based on the rationales cited in the 2002 Decision, PPL does not seek further reconsideration.³ To the extent that the 2003 Decision denies relief on the basis of new contentions not asserted in the 2002 Decision, PPL must seek reconsideration, in order to preserve its arguments on appeal.

It is well-established that a party cannot raise arguments on judicial review of an administrative agency decision if those arguments were not first raised in the proceedings before the agency. See generally United Transportation Union v. STB, 114 F.3d 1242, 1244-5 (D.C. Cir. 1997). There is also case law indicating that if PPL does not seek reconsideration of the 2003 Decision, the Board or Defendant The Burlington Northern and Santa Fe Railway Company ("BNSF") might argue, or a reviewing court might find, that PPL waived its right to challenge new rationales in the 2003 Decision. See Town of Norwood v. FERC, 906 F.2d 772, 775 (D.C. Cir. 1990), and Kelley v. FERC, 96 F.3d 1482, 1488 (D.C. Cir. 1996). PPL is not prepared to take that risk.

In addition, this case is clearly controversial and groundbreaking. The Board's discussion of the issues in its 2002 Decision was abbreviated and erroneous. For example, it cited as authority for denying relief two decisions that were not issued until after the close of the record in this proceeding. 2002 Decision at 9. PPL notes that the Board's 2003 Decision no longer relies

² PPL was criticized for not giving more examples of changes it would have made, but the Board must recall that it denied PPL's request for relief from the 20 page limit of 49 CFR § 1115.3(d).

³ PPL does not accept the Board's arguments that its cross-subsidy threshold test is lawful or supported by prior precedent or is sound as a policy matter, or that it is proper to apply that test in this case. However, PPL does not believe those arguments must be reasserted here to be preserved for appeal.

on those decisions as supporting the outcome, but supports its result with new contentions that have their own defects. Those defects should be addressed by the Board in the first instance.

Finally, the reopening of this proceeding provides time for reconsideration of the 2003 Decision. A final decision is unlikely for several months, and reconsideration will delay this proceeding only if the Board concludes that aspects of its 2003 Decision are untenable, in which case the ultimate decision in the case is likely to be less objectionable.

IV. ARGUMENT

The 2003 Decision states that the Board is "not persuaded by PPL's claim of surprise" in light of Coal Rate Guidelines,⁴ and in light of the testimony of PPL Witness George Borts.⁵ However, the Decision goes on to argue that even if the facts of record would have supported a SARR designed with higher traffic volumes over the western portion, PPL is to blame for failing to design the SARR this way. According to the 2003 Decision "PPL had every incentive from the outset of the case to maximize revenues for the WMCRR as a whole," and one way of maximizing revenues for the SARR as a whole was to maximize utilization of the western portion. 2003 Decision at 8.

The Decision goes on to state that it is "the shipper's responsibility to design the least costly, most efficient SARR." Decision at 9. For this reason, the Board rejects PPL's argument that, had it known the Board would consider the revenues and costs of the western portion in isolation, the western portion could and would have been designed to provide the necessary service levels at lower cost.

⁴ Coal Rate Guidelines -- Nationwide, 1 I.C.C. 520 (1985), aff'd sub nom Consolidated Rail Corp. v. United States, 812 F.2d 1444 (3d Cir. 1985). Notably, the 2003 Decision cites no prior SAC decision in which Coal Rate Guidelines was interpreted in the way it was interpreted in the 2002 Decision.

⁵ Dr. Borts' testimony is quoted in the 2003 Decision at 9, but his testimony filed with PPL's September 30, 2002 petition for reconsideration is ignored. As he there explained, he relied (as did PPL and BNSF) on prior case law in which the ICC and STB consistently treated SARRs as unitary rail systems, without considering line segments in isolation.

These arguments, which appear nowhere in the 2002 Decision, reflect a misunderstanding of the limits of Board jurisdiction and of the practical realities of rate cases.

A. The "Every Incentive" Rationale Ignores the Board's Segmentation Approach

It is astonishing that that STB would say, in defense of its segmented approach, that PPL had every incentive to maximize revenues for the SARR as a whole, when the 2002 Decision has just adopted an analytical approach that ignores the adequacy of revenues for the SARR as a whole. Considered as a whole, PPL's SARR has revenues exceeding its costs, but the Board dismissed the complaint without analyzing the reasonableness of BNSF's rates.

The Board evidently adopted its "every incentive" rationale in recognition that it cannot apply its cross-subsidy test in this proceeding, or deny PPL's request to show the absence of a cross-subsidy due to increased traffic or reduced investment on the western portion, in reliance on decisions issued after all the evidence in this case was submitted. However, the fallback "every incentive" argument is also flawed. Even if it were true that PPL had every incentive to maximize traffic and minimize investment over the SARR as a whole (and this contention is not true), it simply would not follow that PPL had every incentive to maximize traffic and minimize investment over every portion of the SARR.

The Board contends that PPL should have foreseen that the western portion of its SARR might be considered in isolation because "PPL was put on notice, with BNSF's reply evidence, that cross subsidization of the western part would be an issue in this case." 2003 Decision at 9, n. 28. This statement would not support the contention that a shipper complainant has every incentive to maximize revenues for the SARR as a whole. As this case illustrates, PPL could have designed its SARR to generate more revenues on the north-south part, thus maximizing revenues on the SARR as a whole, but the result would not have been any different.

Moreover, the Board mischaracterizes BNSF's position. BNSF's argument for a cross-subsidy was based on its contention that its own rates for north-south traffic exceeded SAC for that traffic. The Board rejected that argument in the 2002 Decision at 9-10 and notes 19-20. To condemn PPL for failing to anticipate the Board's development of a different theory based on BNSF's discredited cross-subsidy arguments ignores due process and the Board's own recent decision in Ex Parte No. 347 (Sub-No. 3), General Procedures for Presenting Evidence in Stand-Alone Cost Cases, decision served March 12, 2001, at 6. The Board there cautioned litigants that it "would adhere to precedent established in prior cases."

When BNSF did call on the Board to adopt the cross-subsidy rule it adopted in its 2002 Decision, BNSF recognized that such a rule would be a departure from precedent established in prior cases. See PPL's September 30, 2002 petition for reconsideration at 3-4, discussing arguments BNSF first made after the close of the record in this case. PPL is not alone in seeing the Board's cross-subsidy test as new.

B. The "Every Incentive" Rationale Ignores the Board's Limited Jurisdiction

In contending that PPL had every incentive to maximize revenues or to minimize SAC, the Board also ignores the fact that the Board's ability to grant relief from unlawful rates is limited by its lack of jurisdiction over rates below the threshold of Board jurisdiction. As the Board has recognized many times, rate relief in a SAC case will be granted based on the higher of the stand-alone cost or 180% of variable cost. See, e.g., West Texas Utilities Co. v. Burlington Northern R. Co., 1 STB 638, 677 (1996), aff'd., BNSF v. Burlington Northern R. Co. v. STB, 114 F.3d 206 (D.C. Cir. 1997).

As a result, once a shipper develops a SARR producing a stand-alone cost below the jurisdictional threshold (as PPL did here with respect to most routings), it has already justified

more relief than it will receive. Even the railroads' economists acknowledge that rates above SAC are excessive, but Congress has immunized significant amounts of differential pricing from regulatory scrutiny.⁶

Once a shipper has developed a SARR that produces a stand-alone cost equivalent to a revenue/variable cost percentage of 175%, it could modify its design to reflect greater revenues or lower costs, producing a stand-alone cost equivalent to 165% of variable costs. However, such efforts would increase litigation costs for no benefit. Whether the SAC is at 175% or 165% of variable costs, rates will not be prescribed below 180% of variable cost.

Moreover, such efforts may be counterproductive as well as futile. The more a SARR deviates from the practices of the defendant railroad, the more likely it is to be attacked as infeasible. Accordingly, PPL and other complainant shippers have long sought to balance costs and benefits in bringing SAC cases. Where the case is relatively small, like PPL's, the incentive not to engage in rate case overkill is even more compelling.

C. The "Every Incentive" Argument Ignores the Burdens Rate Cases Place on the Parties and the STB Staff

Because complainant shippers have little incentive to develop the lowest possible stand-alone cost, they frequently accept railroad evidence that is questionable or wrong. In doing so, shippers save time and money, avoid disputes, and spare the Board Staff the need to resolve factual issues which should have little or no effect on the outcome of the case. The Board itself used a similar "shortcut" approach in its decision served September 13, 2001 in Wisconsin Power & Light Co. v. Union Pacific R. Co., Docket No. 42051. In adopting this approach in this case, PPL was relying on established precedent.

⁶ In the Staggers Act's legislative history, Congress noted that if all traffic moved at rates set at 150% of variable cost, the railroads would be revenue adequate. In setting the jurisdictional threshold at 180% of variable cost, Congress insulated differential pricing from challenge to the extent of the difference between 150% and 180% of variable cost. See 1980 U.S. Code. Cong. & Ad. News 3978, 4065.

It is true that administrative agencies may change the law in the course of adjudications. However, this authority is not unlimited. The Board must adequately explain its departure from past precedent and its new policies must be consistent with the statute and must have a rational basis. PPL has already argued that these requirements have not been met here, and it reserves the right to pursue these arguments on appeal.

In addition, the law requires adequate notice and fair treatment of litigants when the law changes. Retail, Wholesale and Department Store Union v. NLRB, 466 F.2d 380, 390 (D.C. Cir. 1972). When these requirements are violated, an agency creates uncertainty about the way the law is to be applied. The costs and burdens of seeking regulatory relief, which are already extremely high in rail rate cases, become even more onerous because captive shippers must try to guess what obstacles to relief they may face. Because of this uncertainty, many meritorious cases may not be brought.

When the Board defends its decision to apply policies in unprecedented ways by contending that shippers cannot complain because they have every incentive to develop the highest possible revenues and the lowest possible SAC, the problem is compounded. In effect, the Board is telling captive shippers that they cannot adopt sensible efforts to avoid unnecessary litigation costs in reliance on past agency precedent.

The outcome of this approach is not hard to predict. Estimates of litigation budgets will rise, and more shippers will be deprived of a remedy. The small (and declining) number of shippers that seek relief will be forced to seek greater discovery, file more motions to compel, develop evidence in greater detail, and hire more witnesses, and the burdens on both parties and on the Board will increase. These results are inconsistent with the goals espoused by the Board in

Ex Parte No. 638, Procedures to Expedite Resolution of Rail Rate Challenges, in which the Board expressed concern about excessive shipper discovery.

Greater uncertainty benefits the railroad industry, which has always sought to deter rate litigation. As access to regulatory remedies is withdrawn, more captive shippers will pay the rail rates dictated by monopoly railroads. This is what "market-based" solutions amount to, when captive shippers negotiate with railroads for which there is, by definition, no effective competition.⁷ However, driving up litigation costs undermines the statutory guarantee of reasonable rates for captive shippers.

The Board should not promote a regulatory environment in which relief is available only for shippers with the most money, and an unlimited willingness to spend it on attorneys and accountants. On the other hand, PPL recognizes that complainants generally have no right to modify their case presentations after a decision has been rendered. The law harmonizes these considerations through the doctrine of stare decisis. Litigants with notice of the standards they must meet can fairly be held to those standards. However, when an agency "seeks to change a controlling standard of law and have it apply retroactively in an adjudicatory setting, the party before the agency must be given notice and an opportunity to introduce evidence bearing on the new standard." Hatch v. FERC, 654 F.2d 825, 835 (D.C. Cir. 1981).

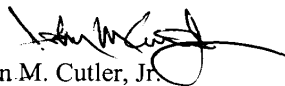
V. CONCLUSION

PPL appreciates the limited reopening of the record that the Board ordered in the 2003 Decision. However, its rationale for refusing to reopen the proceeding in other respects, which would have permitted PPL to use evidence of higher traffic levels and reduced investment over

⁷ The railroads have complained that shippers fail to accept rate reductions offered in pre-complaint negotiations. Those reductions leave in place rates that are far above levels found to be maximum lawful levels in the case law, and the reductions are often transitory, because based on escalation that guarantees increasing profits to the railroad.

the western portion to demonstrate the absence of any cross-subsidy, was arbitrary, capricious,
and contrary to law and sound policy.

Respectfully submitted,



John M. Cutler, Jr.
McCarthy, Sweeney & Harkaway, P.C.
2175 K Street, N.W., Suite 600
Washington, DC 20037
(202) 775-5560

Attorney for PPL Montana, LLC