

BEFORE THE
SURFACE TRANSPORTATION BOARD

STB EX PARTE NO. 646
RAIL RATE CHALLENGES IN SMALL CASES

COMMENTS OF THE
U.S. DEPARTMENT OF AGRICULTURE



211630

ENTERED
Office of Proceedings

JUL 22 2004

Part of
Public Record

Bill Hawks
Under Secretary
Marketing and Regulatory Programs
U.S. Department of Agriculture
Washington, D.C. 20250

Date: July 21, 2004

AUTHORITY AND INTEREST

The Secretary of Agriculture is charged with the responsibility under the Agricultural Adjustment Act of 1938 and the Agricultural Marketing Act of 1946 to represent the interests of agricultural producers and shippers in improving transportation services and facilities by, among other things, initiating and participating in Surface Transportation Board (Board) proceedings involving rates, charges, tariffs, practices, and services.

BACKGROUND

The purpose of this public hearing is to provide a forum for the continued discussion of proposals regarding the Board's processing of railroad rate challenges in small cases that are not suitable for handling under constrained market pricing (CMP) procedures. The Board has noted that even though it has provided simplified guidelines for seeking rate relief in those cases where its standard rate guidelines would be too costly or infeasible, it continues to hear from smaller rail customers that its procedures are still impractical for the limited amounts of traffic that they ship.

The Board held an initial public hearing on April 22, 2003, to hear suggestions from interested parties. At the request of Chairman Nober, 17 of the commenting shipper organizations identified their common recommendations and submitted a joint proposal to the Board on July 11, 2003.

The Department of Agriculture (USDA) thanks the Board for initiating these public hearings and supports productive dialogue on this issue that is of great significance to agricultural shippers. USDA commends the combined comments of the 17 shipper organizations

on July 11, 2003, and the testimonies of agricultural representatives and the other shippers on April 22, 2003. These comments have been thoughtfully prepared and provide excellent information as to why the Board's current simplified rate appeal procedures are not perceived as cost-effective. USDA urges the Board to develop a process for handling rate appeals for small cases that is cost-effective, well-defined and fair, and transparent.

SHIPPERS NEED COST-EFFECTIVE APPEALS PROCEDURES

The ability of agricultural shippers to appeal excessive rail rates is particularly important for agricultural producers because of the characteristics of the market in which they operate. Due to their numbers (many), size (small), and the nature of their products (homogeneous with many substitutes) individual agricultural producers of grain and oilseed crops are considered "price-takers." That is, they have little or no ability to influence the price they receive for their products, and therefore, are unable to pass increases in costs forward to buyers of their products. Instead, these individual agricultural producers tend to absorb any cost increases because of their lack of market power. Consequently, increases in transportation costs typically result in decreased producer incomes as individual producers absorb the increased transportation cost. In turn, lower producer incomes can adversely affect the ability of individual producers to borrow funds, potentially reducing economic prosperity in rural areas. Higher transportation costs may also hinder the competitive position of U.S. agricultural products in highly competitive export markets.

Transportation costs for agricultural products are large relative to crop value, often exceeding 40 percent of the final delivered price of the grain. Tariff rates on approximately 30

percent of farm product shipments exceed the jurisdictional threshold, which is a revenue-to-variable cost (R/VC) ratio of 180 percent. In regions of the country that are highly dependent upon rail service, many agricultural shippers consider their rail rates to be excessive because the R/VC ratio is much higher—sometimes exceeding 300 percent—than the 180 percent jurisdictional threshold.

Despite extremely high rail rates, agricultural producers in captive regions perceive that they have no cost-effective access to regulatory relief. The Board currently provides two methods for shippers to challenge rail rates: the Constrained Market Pricing (CMP) guidelines or the simplified rate appeal procedures.

CMP involves the creation of a hypothetical railroad to haul the product on which the rate is being contested. The CMP process is cumbersome, expensive, and time consuming. A rail customer filing a rate complaint at the Board can expect to spend over \$2 million and wait several years for a final decision, according to grain shipper associations. In its February 1999 study, *Railroad Regulation: Current Issues with the Rate Relief Process*, the General Accounting Office (GAO) found that the 41 rate complaints reviewed by the GAO cost shippers from about \$500,000 to \$3 million and required a few months to about 16 years to resolve through the rate complaint process. Consequently, CMP has been most successful when used by energy companies to appeal rates on large-quantity coal movements between one origin and one destination.

CMP is not considered feasible for rate appeals by agricultural shippers because, in contrast with coal movements, agricultural production is geographically disperse. That

is to say, agricultural firms typically ship much smaller quantities (compared to coal shippers) of varied crops to many destinations. Rate appeals using CMP procedures become extremely complex and expensive as multiple hypothetical origin-destination pairs and commodities are added to the rate appeal.

Due to the excessive costs and duration of CMP rate proceedings, the Board developed simplified rate appeal procedures for non-coal shippers. The simplified rate appeal procedures, however, have not been used for many reasons, as previous shipper testimony in this hearing has indicated. One key factor inhibiting the use of the simplified procedures is that shippers are uncertain how the Board will apply these appeal procedures. The Board may evaluate the rate challenge under the simplified procedures based on the three revenue-cost measures, but shippers do not know in advance which method the Board will use. Another reason inhibiting the use of these procedures is that to be able to use the simplified rate appeal procedures, shippers must first persuade the Board that CMP would not be cost-effective. Thus, shippers must incur costs of developing a modified CMP challenge to be granted the use of the simplified appeals procedure. As a result, the Board's simplified rate appeal procedures are impractical for those shipping limited amounts.

USDA RECOMMENDATIONS

USDA agrees that the Board should continue to use the following principles articulated by the Department of Transportation to guide their efforts in developing effective procedures for handling small rate appeal cases:

“The Board has had several fundamental goals when considering how best to handle cases involving small shippers. The first is to identify a more simple analysis than CMP in order to provide meaningful regulatory access. The second is to enable railroads to differentially price their services according to the demand characteristics of the traffic. The third is to protect captive shippers from bearing an undue share of railroad revenue requirements.”¹

For the Board to achieve these goals, USDA believes that the rate appeals process for small cases must be cost-effective, well-defined, and transparent to all parties.

Cost effective. The costs of appealing apparently excessive rail rates should be commensurate with the stakes involved. At the present time, the procedures for a simplified rail rate appeal are heavily weighted in favor of the rail carrier because the potential cost of the appeal appears to be much higher than the potential benefits to any single shipper.

Consequently, shippers conclude that they have little or no practical access to regulatory relief.

As discussed in previous shipper testimonies, the Board has the authority to adopt some simplified procedures that could reduce the shipper cost of pursuing regulatory relief. In other cases, the Board may need to request appropriate legislation from Congress. USDA urges the Board to greatly reduce the shipper cost of pursuing a small rate appeal by:

- Adopting simplified procedures that reduce the cost of appealing rail rates;

¹ *STB Ex Parte No. 646, Rate Challenges in Small Cases*, U.S. Department of Transportation comments, April 16, 2003.

- Adopting procedures that minimize the amount of legal representation a shipper appealing rail rates requires;
- Providing a shipper contemplating a small rate case relevant information from the confidential waybill so the shipper could assess the merits of its case; and
- Encouraging the consolidation of rate challenges for multiple origin-destination pairs or commodities.

USDA recommends that the Board adopt simplified rate appeal procedures that reduce the cost of appealing rail rates. One way to accomplish this could involve requiring the railroad to prove that the CMP appeals process is economically feasible for the small rate case. For small rate cases, it seems intuitive that the potential shipper benefit (including the consideration of risk and the probability of winning the appeal) would be less than the \$2-plus million required for the CMP process. As previous shipper testimonies have indicated, placing the burden of proof on the shipper has denied shippers practical access to regulatory relief. It would appear that if insurmountable barriers are erected to obtain regulatory relief, the rail rates in question are more susceptible to perceptions of being unjustifiably excessive.

Similarly, the Board could require rail carriers to prove the lack of market dominance (at least in the very smallest cases) rather than requiring shippers to prove the presence of market dominance. If 70 percent of farm product shipments have R/VC ratios less than 180 percent (thus removing those rates from challenge and review by the Board), conceivably the remaining 30 percent of farm shipments may be subject to considerable market power by the railroads. In contrast to CMP procedures that often result in rail rates at or slightly above the jurisdictional R/VC threshold of 180 percent, shippers that use the simplified rate appeal procedures are apt to

end up with rates substantially above the 180 percent threshold. Consequently, shippers using the Board's simplified rate appeal procedures are not likely to appeal rail rates unless the revenue-to-variable cost ratio is well above 180 percent.²

USDA recommends that the Board simplify the small case rate appeal procedures to minimize the amount of legal representation that a shipper appealing rail rates requires. As discussed in previous shipper testimony, this could be accomplished by limiting the amount of discovery allowed, expediting the rate appeals process, and making use of administrative law judges. The cost of a small rate appeal is perceived to greatly exceed its benefit because of the complexity of the current procedures.

The presence of a feasible and cost-effective small case rate appeal procedure would also encourage the use of mediation, which the Association of American Railroads recommended in its testimony. While USDA is highly supportive of alternative dispute resolution measures such as mediation, USDA opposes mandatory mediation unless shippers have access to cost-effective small case rate appeal procedures.

USDA further recommends that the Board provide a shipper, who is contemplating filing a small rate case, relevant information from the confidential waybill sample. USDA recommends that the Board explore current technology to allow access to this data by creating a query program that is web-accessible by shippers. The query program should be designed to assist a shipper in assessing the merits of its potential rate case. An alternative method might

² The Board publishes on a quarterly basis the R/VC_{RSAM} for each major railroad. This is one of the three R/VC measures used in the simplified appeals process and has a lower value and a higher value. The lower value typically exceeds 220 while the higher value often exceeds 260.

include the Board performing a shipper-requested analysis of the data. The advantage of these methods is that essential data confidentiality would be preserved.

USDA recommends that the Board adopt procedures, where possible, that encourage shippers to appeal rail rates for several commodities and numerous routes in the same small case. Small case rail rate appeals procedures should fit the characteristics of small shippers, who typically ship numerous commodities over many origin-destination pairs. With current procedures, many apparently excessive rates cannot be appealed because few origin-destination pairs for a commodity have enough traffic for an appeal to be cost-effective. Rate appeal procedures that require separate appeals for each commodity and origin-destination pair are not cost-effective for the small shipper and limit the shipper's access to regulatory relief.

Well-defined and Transparent. Previous testimony provided by shippers urges the development and use of a "bright-line standard" to determine a shipper's eligibility for a small case rate appeal as well as objective, straightforward procedures that provide greater predictability regarding the outcome of the appeal.

USDA recommends that the Board develop such a standard of eligibility for filing a small rate case based upon the potential dollar amount of benefits if the shipper prevails in a case. The dollar amount chosen for this standard, adjusted annually to reflect inflation, should be set high enough to allow the realization of actual or positive net benefits relative to the cost of pursuing the appeal if the shipper were to prevail. Eligibility for a small rate case should not be based on the size of the shipper, but rather the value that is being contested.

USDA recommends that the Board establish transparent and straightforward procedures that provide greater predictability regarding the outcome of the appeal. Previous shipper testimony in the hearing indicates general confusion as to how the Board will apply and weigh the three revenue-to-variable cost ratios used in the simplified rate appeals procedure. This uncertainty creates an unacceptable level of risk and discourages shippers from appealing apparently excessive rail rates.

CONCLUSION

USDA thanks the Board for initiating these public hearings on an issue that is important to agricultural shippers. Previous shipper comments in this hearing have been thoughtfully prepared to articulate why the Board's current simplified rate appeals procedures are not perceived as cost-effective for agricultural shippers. USDA urges the Board to develop a process for handling rate appeals for small cases that is cost-effective, well-defined, and transparent.

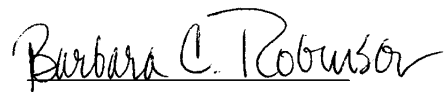
Respectively submitted,



Bill Hawks
Under Secretary
Marketing and Regulatory Programs
U.S. Department of Agriculture
Washington, D.C. 20250

CERTIFICATE OF SERVICE

I, Barbara C. Robinson, certify that on this 21st day of July, 2004, I caused a copy of the foregoing document to be served by first-class mail, postage prepaid, on all parties of record in STB Ex Parte No. 646.

A handwritten signature in cursive script that reads "Barbara C. Robinson". The signature is written in black ink and is positioned above the printed name and title.

Barbara C. Robinson
Deputy Administrator
Transportation and Marketing Programs
U.S. Department of Agriculture
Washington, D.C. 20250