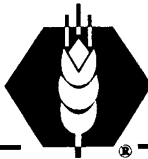


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National Grain and Feed Association

April 16, 2003

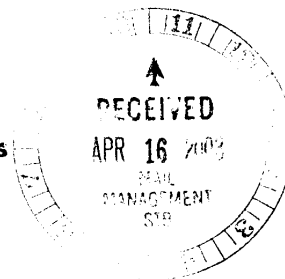
BY HAND-DELIVERY

Surface Transportation Board
Attn: STB Ex Parte No. 646
1925 K Street, NW
Washington, DC 20423-0001

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Re: Ex Parte No. 646 – Rail Rate Challenges in Small Cases

Dear Sir or Madam:

Enclosed for filing please find an original and ten copies of the written testimony of Dr. Kendell W. Keith on behalf of National Grain and Feed Association. Your attention is greatly appreciated.

Very truly yours,

Charles M. Delacruz
Counsel for Public Affairs

CMD/lp
Enclosures

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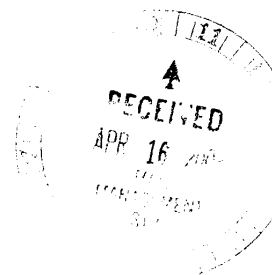


National Grain and Feed Association

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**BEFORE THE
SURFACE TRANSPORTATION BOARD**

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

**TESTIMONY OF
DR. KENDELL W. KEITH ON BEHALF OF
NATIONAL GRAIN AND FEED ASSOCIATION**

Dated: April 16, 2003

My name is Kendell W. Keith. I am President of the National Grain and Feed Association ("NGFA"). I thank you for the opportunity to address you this morning.

I. INTRODUCTION AND DESCRIPTION OF NGFA

NGFA is the U.S.-based trade association for 1,000 grain, feed, processing and grain-related companies operating 5,000 or more facilities that store, handle, merchandise, mill, process and export over two-thirds of all U.S. grains and oilseeds. Approximately 70 percent of NGFA member firms are small businesses -- country elevators and feed mills. Also affiliated with NGFA are 36 state and regional grain and feed associations.

NGFA has been seeking for years to promote the concept of private solutions to differences between railroads and their agricultural customers. Several years ago, NGFA and the railroad industry agreed to a program of compulsory arbitration for certain rail-shipper disputes, excluding those involving rates. The arbitration program, which addresses differences in many areas of transportation, including loss and damage claims, demurrage, and railroad practices, has proven to be extremely successful. Based on information we receive from NGFA members and carriers and from our experience in administering the arbitration program, we find that the availability of even-handed arbitration propels many potential disputes toward voluntary resolution without so much as the commencement of an arbitration proceeding, and often results in the settlement of arbitrations that have been commenced.

One of the driving forces behind the success of the NGFA rail arbitration program is that all participants, rail and shipper alike, recognize that they are at risk if a formal arbitration case is pursued to completion. A party's knowledge that it has at least as much chance of losing a for-

mal case as its opponent provides the most forceful motivation for that party to undertake a voluntary disposition of its differences with another party. That motivation is lacking in disagreements subject to Board jurisdiction between railroads and NGFA members regarding rate levels because the system is so clearly uphill for the shipper.

That is not to say that all agricultural commodity rates are perceived by shippers to be excessive. The agricultural community in fact recognizes that the majority of rail rates for agricultural commodities are not above 180 percent of variable costs and therefore ineligible for any challenge before the Board.

However, measured by railroad revenue, approximately 30 percent of farm product shipments move at rates in excess of 180 percent of variable costs, and in some regions of the country, including those where agriculture is intensely dependent on rail service for a very high percentage of grain output, rail rates are widely recognized to be well above the jurisdictional threshold of 180 percent. Grain interests in those areas perceive themselves to be without an effective rate remedy, especially in the wake of the McCarty Farms case, which was before the ICC for some 18 years before finally ending in dismissal of the complaint.

NGFA and its agricultural community members have always supported a financially strong and healthy railroad system in this country and recognized that railroads cannot be all things to all people at all times. Nonetheless, we believe that Congress did intend for there to be practical limits on the contribution which individual railroad shippers should be expected to make to the financial health of a given railroad, and Congress created rate reasonableness remedies for use in those cases where that contribution is excessive in "market dominant" situations. Where there is a statutory rate remedy, it is important that it be fair, functional, and reasonably

accessible. Ideally, such a system should discourage litigation, much as NGFA's arbitration system does.

With those prefatory observations in mind, we offer the following comments on the existing "small rate case" rules established in Ex Parte No. 347 (Sub-No. 2), Rate Guidelines -- Non-Coal Proceedings (served December 31, 1996).

II. WHY THE EXISTING RULES HAVE NOT BEEN USED

As the Board no doubt recognizes, no case has been brought under the "small rate case" guidelines in the more than six years that the guidelines have been in effect. The absence of small rate case complaints does not attest to uniform satisfaction with the level of the railroads' rates. At least in certain regions of the country, rates for various agricultural shipments are claimed to exceed 180 percent of variable costs by margins that would warrant a rate complaint under appropriate circumstances. The present small rate case rules discourage the pursuit of relief even where it is assumed that market dominance can be established without excessive difficulty.

The reason is that, even though the statute directs the STB to establish "simplified and expedited" procedures for "small" rate cases, it is debatable whether the non-coal rate case rules are, indeed, "simplified" or will yield a rate reduction sufficient to justify the time, expense, and potential carrier ill-will generated by a formal complaint.

Let's start with how the "simplified" rules must be invoked by a shipper. Although no rate case can proceed without a jurisdictional demonstration that the rate at issue is subject to market dominance, including the 180 percent revenue/variable cost threshold, I will not dwell on that issue.

The statute requires that the SAC procedures be used unless they are "too costly, given the value of the case." Although the Board's rules at 40 C.F.R. 1111.1(a) contain a list of certain data which a complaining shipper should present for a determination of "simplified" case eligibility, the statutory language and the Board's rules appear to leave the railroad defendant free to argue that the "too costly, given the value of the case" test requires a demonstration of the estimated results of an SAC case; otherwise, it may not be possible to determine the full "value" of the case for purposes of determining if SAC is "too costly." The Board's rules appear to invite just such an analysis, calling for the complainant to explain the "feasibility and anticipated cost of preparing a stand-alone cost presentation." Thus, shippers seeking to use the "simplified" approach may find themselves in the anomalous position of having to undertake some form of estimated SAC analysis in order to establish that they should not be required to make a full-blown SAC presentation.

No matter how the requirements of 49 C.F.R. 1111.1(a) are viewed, a complaining shipper under the "simplified" procedures faces a complicated task which will require the use of cost experts and other professional assistants to meet the Board's eligibility requirements, to satisfy the other threshold elements of a rate case, including market dominance evidence, and to estimate the outcome of the case in order to comply with the rules' requirement that the "full relief sought, including all reparations as well as the level and duration of any rate prescription," be established.¹ A shipper thus begins down the road to a "simplified" case in a very complicated and potentially costly manner.

If a shipper establishes eligibility to use the "simplified" methodology, the path remains far from clear. The Board's guidelines contain three "benchmarks" -- data sets -- to be used in

¹ NGFA and others requested the Board to adopt abbreviated, "bright line" rules in Ex Parte No. 347 (Sub-No. 2) to facilitate "simplified" case eligibility determinations, but the Board declined to do so.

small rate case determinations. Two of the benchmarks (RSAM, designed to measure the uniform markup above variable costs that would be needed from every shipper of potentially captive traffic in order for the defendant to recover all of its fixed costs, and $R/VC > 180$, designed to measure the degree of differential pricing actually being practiced by the defendant) can be derived from data published by the Board. The third benchmark, R/VC comp. (to measure the markup taken by the defendant on existing traffic yielding in excess of 180 percent of variable cost that involves similar commodities moving under similar transportation conditions), is not ascertainable in the absence of discovery. The three benchmarks are described in the Board's decision as a "starting point" that can be augmented by additional evidence of rate unreasonableness, such as proof that the railroad's excessive rates are the result of inefficient operations.

The Board's decision contains no indication of how the three "benchmarks" or any other evidence will be balanced to arrive at a maximum reasonable rate. A shipper is thus faced with the prospect of filing a complaint under the simplified rules without guidance either in estimating the outcome of the case or in arguing for any particular method of balancing the benchmarks. These conditions make it difficult for a shipper to obtain authority from its Board of Directors or other appropriate governing body to expend the money, time and effort on a highly contentious rate case that is sure to antagonize the serving carrier.

Some people have suggested that the outcome of a "simplified" rate case is not altogether unpredictable because of the fact that two of the "benchmarks" rely on publicly available data published periodically by the Board. That data, I understand, suggests that the RSAM and $R/VC > 180$ numbers for most Class I railroads would be in a range between 220 and 280 percent of variable costs. For purposes of this discussion, let's just say that these two data categories would approximate 250 percent of variable costs and militate toward an outcome of that nature. This

school of analysis suggests that it accordingly would be difficult for the third benchmark, R/VC > comp., to outweigh the first two benchmarks by a measure sufficient to bring about a significant reduction in the 250 percent outcome.

This outlook creates yet another impediment to use of the "simplified" procedures because it means that a shipper's rate must not be just marginally above 180 percent of variable costs in order to justify the expense and other detriments of a rate case, but in practical terms must be well above 250 percent of variable costs. In these circumstances, many "small case" shippers paying rates up to 275 percent or so of variable costs, and who could have viable rate recourse were they able to afford a SAC case, are discouraged as a practical matter from pursuing a simplified case.

III. POSSIBLE IMPROVEMENTS TO REDUCE BARRIERS TO RESOLUTION

We would be the first to acknowledge that there may be no easy solution for what ails the "small rate case" guidelines. We recognize that some earlier efforts by the Interstate Commerce Commission to find rate reasonableness solutions lacking all the complexities and expenses of SAC were met with judicial resistance, and we recognize that the Board may, to some extent, consider its hands tied by court language suggesting that SAC is the only test thus far recognized as fully compliant with differential pricing principles.

While NGFA members do not quarrel with the theory of differential pricing, we believe that there is something askew when adherence to a principle means that only a relative handful of railroad shippers paying rates in excess of the jurisdictional threshold are able as a practical matter to obtain rate relief. It was never our impression that what some have called the "delicate balance" of the Staggers Act was meant to have any such result.

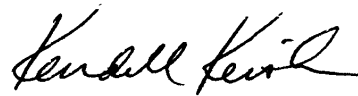
The easiest correction to make in the existing guidelines is with respect to the eligibility test. Under the present rules, complaining shippers must compile and submit data requiring extensive cost and expert preparation. However, there is a very small likelihood, if any at all, that a complaining party would elect to use the "simplified" methodology if there was a realistic option for that party to proceed under the SAC methodology, where the potential rewards at the end of the case are far greater. Accordingly, the Board should adopt a presumption in favor of a shipper's election to rely on the "simplified" methodology.

We suggest that the Board essentially shift the burden to the defending railroad of proving that the SAC methodology would not be "too costly, given the value of the case" if the defendant wishes to challenge the complainant's reliance on the simplified procedures. If a railroad elects to make such a showing, then the shipper should be required to submit the basic data necessary for the carrier to complete its challenge to the extent such data is not already disclosed in the complaint such as the following: origin, destination, route, commodity, movement type (e.g., single car, unit train), equipment type (including car ownership), lading weight per car, and annual volume, as well as its evidence of the costs of a SAC case based on witnesses of its selection. The railroad should be required to establish the outcome of the SAC case and demonstrate that the benefits of the case exceed the costs of bringing it by a sufficient margin to convince the Board that a SAC presentation is not "too costly, given the value of the case." NGFA believes that this approach will greatly simplify and streamline the "eligibility" phase of a small rate case complaint.

With respect to the three "simplified" benchmarks, NGFA urges the Board to solicit proposals under which the satisfaction and application of the benchmarks can be explained more fully. For example, one possibility would be for the Board's staff to assemble the inputs for a

hypothetical "simplified" case and then to demonstrate how those inputs would be balanced as benchmarks. The Board also should solicit comments on whether it may be possible to standardize certain elements of a basic rate complaint case and to make standardized information publicly available, at least for use in "simplified" cases.

Respectfully submitted,

A handwritten signature in black ink, appearing to read "Kendell Keith". The signature is fluid and cursive, with the first name "Kendell" and last name "Keith" clearly distinguishable.

Kendell W. Keith, President
National Grain and Feed Association

April 16, 2003