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SURFACE TRANSPORTATION BOARD FINDS CERTAIN KOCH PIPELINE CO. RATE INCREASES UNREASONABLY HIGH, ORDERS RATE ROLLBACK & REPARATIONS

Surface Transportation Board (Board) Chairman Linda J. Morgan announced today that the Board has issued a decision finding that certain rates increased in 1996 by the Koch Pipeline Company (Koch) for the pipeline transportation of anhydrous ammonia (an agricultural fertilizer) were unreasonable. The Board accordingly ordered Koch to reduce its rates to the pre-increase levels and to pay reparations to two shippers, CF Industries, Inc. (CF) and Farmland Industries, Inc. (FI), for past transportation to 19 pipeline destination points in the Midwest. The Board declined to order rate relief for two other destination points where it found that the shippers have effective competitive alternatives to the pipeline.

Under Section 15301 of Titled 49, United States Code (49 U.S.C. 15301), the Board is charged with the economic regulation of pipeline transportation of commodities other than water, oil, or energy-related gases. The rates for such transportation must be reasonable (49 U.S.C. 15501(a)), and a pipeline carrier may not unreasonably discriminate among its users (49 U.S.C. 15505). In prescribing pipeline rates, the Board must consider, among other factors, the availability of other economic transportation alternatives (49 U.S.C. 15503(b)).

Because pipeline carriers--like railroads--serve both shippers who have effective transportation alternatives and shippers who do not, the Board determined that it would evaluate the reasonableness of Koch's rates using the Constrained Market Pricing (CMP) principles that it applies to railroads. In this case, CF and FI chose to use the CMP's "top-down" approach in which a carrier's existing system is examined to determine whether it is earning sufficient funds to cover its costs and provide an adequate return on investment.

Applying that test, the Board determined that Koch was already earning adequate revenues at the pre-increase rate levels. Even without the rate increases, the Board found that Koch had already recovered nearly all of its investment in the pipeline, that by the end of 1999 the pipeline would generate an after-tax cash flow of almost $13 million annually, and that Koch's yearly return on investment exceeded the "cost of capital" measure used by the parties in this case. The Board further determined that Koch could not justify these rate increases on the ground that it will need substantial funds to rehabilitate and maintain the pipeline. As the Board explained:

"In essence, Koch seeks to establish a cash reserve to replace the pipeline before reinvesting in the pipeline itself. Under the revenue adequacy constraint, however, a carrier can 'recover no more than its total costs over the life of its investment.' [citation omitted]. Thus, the constraint permits a carrier to recover, over the useful life of its investment, all of the costs that it has incurred, so that it then has the opportunity--and, like other businesses, the burden of risk--to attract needed capital at currently prevailing rates to replace and maintain its assets. Koch is not entitled to 'put the cart before the horse' by requiring captive pipeline shippers to provide in advance a revenue stream to pay for investments not yet made and assets that are not in place."

The Board's decision was issued today in *CF Industries, Inc. v. Koch Pipeline Co., L.P.*, Docket No. 41685. Vice Chairman Burkes commented with a separate expression.

A printed copy of today's decision is available for a fee by contacting: **Da-To-Da Office Solutions, Room 405, 1925 K Street, N.W., Washington, DC 20006, telephone (202) 466-5530.** Today's decision is also available for viewing and downloading via the Board's website at **www.stb.dot.gov.**

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