

Surface Transportation Board Opens Proceeding To Address Costing Issues in Rail Rate Cases Involving Smaller Railroads

Surface Transportation Board (Board) Chairman Linda J. Morgan announced today that the Board has instituted a proceeding to address costing issues in rate cases involving smaller railroads.

Under the law, the Board may not review the reasonableness of a challenged rail rate unless it first finds that the railroad has "market dominance" over the traffic involved. Market dominance refers to "an absence of effective competition from other rail carriers or modes of transportation for the transportation to which a rate applies." There are various "qualitative" aspects to the market dominance analysis, but the statute also contains a "quantitative" provision precluding a finding of market dominance where the revenue produced by the movement is less than 180 percent of the railroad's "variable cost" of providing the service (expenses that vary with the level of service provided by the railroad).

The Board has a standard methodology, known as the Uniform Rail Costing System (URCS), for computing a railroad's variable costs. URCS relies on data compiled under the Uniform System of Accounts (USOA), a Board-prescribed accounting system. Because the USOA's data requirements are not insubstantial, however, only the larger ("Class I") railroads have been required to file data and maintain their records in accordance with USOA. Class I railroads account for about 92 percent of United States rail freight traffic (measured by carloadings), and prior rate challenges were, until recently, directed almost exclusively to their rates.

Because smaller railroads are not required to comply with the USOA, when their rates are challenged, the detailed, uniform cost and operational data needed to develop variable costs using URCS are not available. The Board was faced with this issue a few years ago, when a shipper filed a rate complaint against a Class II (medium-sized) railroad [See *Minnesota Power, Inc. v. Duluth, Missabe and Iron Range Railway Company*, STB Docket No. 42038 (*Minnesota/DMIR*)]. Although the parties to the *Minnesota/DMIR* case ultimately settled, the Board recognizes that it must be prepared to deal with any future cases that may be filed against smaller railroads.

Accordingly, the Board instituted this proceeding. In its decision, the Board raised the possibility of requiring small railroads that become the subject of rate complaints to compile data, for a period of time, that could be used to develop URCS variable costs. But it expressed concern that such a procedure could delay the disposition of rate cases involving smaller railroads, and that it could impose additional litigation costs on parties least able to bear them. Therefore, absent the submission of a practical alternative, the Board proposed in its decision to use what are known as URCS regional average variable costs, which are calculated routinely by the Board on the basis of aggregate data filed by large railroads, as a surrogate for the variable costs of smaller railroads. Although the Board recognized that URCS regional average costs are not as accurate as URCS data for a particular railroad, it noted that such URCS regional average costs previously have been used in a variety of regulatory proceedings, including past proceedings challenging the reasonableness of a non-Class I railroad's rates. Accordingly, citing an old adage that "the best should not be the enemy of the good," the Board proposed to apply a policy of estimating non-Class I railroads' variable costs using Class I regional average variable costs. Noting that it would also welcome suggestions on how such regional average variable costs can practically be adjusted to better reflect the operations of non-Class I railroads, the Board asked interested parties to file comments on its proposed approach and/or any alternative proposal they may wish to make by **July 1, 2002**, with replies due by **July 31, 2002**.

The Board issued its decision yesterday opening the case entitled *Calculation of Variable Costs in Rate Complaint Proceedings Involving Non-Class I Railroads*, STB Ex Parte No. 589. A printed copy of the decision is available for a fee by contacting **D~ 2 D~ Legal Copy Service, Suite 405, 1925 K Street, N.W., Washington, DC 20006, telephone (202) 293-7776**, or via da2dalegal@earthlink.net. The decision also is available for viewing and downloading via the Board's website at <http://www.stb.dot.gov>.

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