



Rate-Reasonableness Standards

FRCA POSITION

The *Surface Transportation Board (STB) Reauthorization Act of 2015*, P.L. 114-110 directs the STB (or Board) to review its three tests used when evaluating if a railroad is charging a reasonable rate for shipping goods or commodities when a rate is challenged before the Board. FRCA strongly supports this requirement.

Moreover, FRCA supports the efforts of the STB to meet this requirement in its Advanced Notice of Proposed Rulemaking (ANPRM), EP Docket No. 733, *Expediting Rate Cases* and the expected future public hearing in EP Docket No. 736, *Intervistas Study*.

ISSUE BACKGROUND

The STB has the statutory authority and duty to review the reasonableness of rates and service terms for non-exempt commodities if shipped under common tariff. Under its statutory authority, the STB considers the reasonableness of a challenged rate using its three tests, as chosen by the shipper filing the rate complaint before the Board.

These tests are:

- Stand-Alone Cost (SAC), which requires the shipper to design a hypothetical railroad tailored to serve the specific route, to simulate the competitive rates that would exist in a competitive or contestable network.
- Simplified SAC, which eliminates or restricts the SAC evidence parties can submit to the actual operations and services provided by the railroad, which is likely to result in higher rates than under the SAC test.
- Three Benchmark, under which the STB determines the reasonableness of a challenged rate by examining three benchmarks, or tests, that assess rate markups of revenues to variable costs.

FRCA, along with other shipper groups and other stakeholders, have significant concerns involving not only the cost and length of STB reviews of challenged rate rates, but also the fundamental principles on which each method is based:

- The SAC method entails an increasingly complicated and arbitrary comparison of the railroad's actual rates with those that would be charged by a hypothetical railroad replacement.
- The Simplified SAC method involves a simplified application of SAC principles, but has yet to be used for a completed STB rate review.
- The Three-Benchmark method tests the shipper's rates against a combination of three benchmarks of revenues to variable cost ratios; those ratios are subject to bias both individually and collectively.

The tests have been the subject of several recent studies, including a 2016 STB-commissioned study conducted by the consulting firm, InterVISTAS, and a 2015 report by the Transportation Research Board (TRB) of the National Academy of Sciences, "*Modernizing Freight Rail Regulation*".

INTERVISTAS REPORT

FRCA had understood that the purpose of the InterVISTAS report was to evaluate current rate reasonableness methodologies used by the STB, other Federal agencies, and foreign entities for the purpose of developing alternatives to the SAC test. The report instead starts by assuming the SAC is a sound and even ideal railroad rate reasonableness methodology, regardless of the costs incurred in utilizing the SAC or its complexity. The Report does consider and finds some value in other existing alternatives (or ways to simplify the SAC) only insofar as they incorporate SAC principles or approximate SAC results.

The InterVISTAS Report can be found via www.stb.gov/stb/elibrary/IndependentStudy.html

TRB REPORT

The TRB reached very different conclusions in its 2015 report. The TRB Report found severe flaws in both the SAC and the basic effort to calculate and regulate based on revenue to variable cost ratios. Further, it recommends developing a whole new structure/methodology for rate cases.

The TRB Report can be accessed via www.trb.org/Main/Blurbs/172736.aspx

STATUS

On March 31st, the STB issued a Notice of Proposed Rulemaking (NPRM), EP Docket No. 733, *Expediting Rate Cases*. This NPRM can be accessed via https://www.stb.gov/_85256593004F576F.nsf/0/CDC3729E21C9B0B3852580F400639806?OpenDocument This rulemaking is required by the *STB Reauthorization Act of 2015* where the Board is reviewing comments on proposals that the STB asserts may expedite its handling of major rail rate cases.

Previously, FRCA signed on to three joint filings that were submitted by the Western Coal Traffic League, American Public Power Association, Edison Electric Institute, National Association of Regulatory Utility Commissioners, and the National Rural Electric Cooperative Association – initial comments on August 1, 2016, reply comments on August 29, 2016, and [final reply comments on June 14th](#). This ANPRM originally was issued on June 14, 2016.

The STB has also created a new proceeding, EP Docket No.736, *Intervistas Study*. The STB held an Economic Roundtable on this Report, “*An Examination of the STB’s Approach to Freight Rail Rate Regulation and Options for Simplification (Report)*”, on October 25, 2016. Participation in this Economic Roundtable was by invitation only – notably academics including some individuals who participated in either the InterVISTAS Report or the TRB Report. There is a possibility that the Board will hold a public hearing on the InterVISTAS Report. Such a hearing may provide an opportunity to present and explore alternatives to the three existing rate reasonableness methodologies.