



# Freight Rail Customer Alliance

## 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 Final Rule (FR), EP Docket No. 733, *Expediting Rate Cases* and a hopeful future public hearing in EP Docket No. 736, *Intervistas Study*.

### The Issue

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 of 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 <https://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 <http://www.trb.org/Main/Blurbs/172736.aspx>

### **Status**

On June 18, FRCA met with members of the STB *Rate Reform Task Force*.

In May, the STB began exploring ways to streamline its SAC rate review methodology via meetings with stakeholders, practitioners, and consultants with its *Rate Reform Task Force*: <https://www.stb.gov/newsrels.nsf/WEBUNID/EFE3B0A71EC4A98525827800541CF1>. This panel was established in January 2018 by the STB to gain further insight even though its formal proceeding concluded several months earlier.

On November 20, 2017, the STB issued its Final Rule (FR), EP Docket No. 733, *Expediting Rate Cases*. FRCA joined with the Western Coal Traffic League (WCTL), American Public Power Association, Edison Electric Institute, National Association of Regulatory Utility Commissioners, and the National Rural Electric Cooperative Association in filing comments during this proceeding.

This FR adheres to coal shippers’ primary objective stated early-on in this proceeding when the Board, at the group’s urging, decided not to pursue substantive proposals that would have blocked coal shippers’ ability to obtain STB rate relief. In this final Decision, the Board does not change its position. It also aims to allow the STB to pursue certain procedural changes that the Board hopes will help speed-up its consideration of maximum rate cases. A bit of caution as there is now a 70-day pre-complaint mediation, which means that the actual case will start 70 days later, and discovery needs to be served with the complaint. There is no corresponding requirement to make the common carrier rate being challenged available any earlier.

The other joint filings in this proceeding were submitted on June 14, 2017 (Final Reply Comments), August 29, 2019 (Reply Comments), and August 1, 2016 (Comments).

This FR became effective December 30, 2017 and can be accessed via <https://railvoices.org/wp-content/uploads/EP-733-Decision.pdf>

The STB 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.

It is not known if the Board will hold a public hearing on the InterVISTAS Report. Should such a hearing be held, it may provide an opportunity to present and explore alternatives to the three existing rate reasonableness methodologies.

It is possible that the STB might begin discussing, with *ex parte* restrictions waived, rate-reasonableness matters and the InterVISTAS report via its *Rate Review Task Force*.