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CURE
PROMOTING RAIL COMPETITION

RAIL RATE CHALLENGES AT THE
SURFACE TRANSPORTATION BOARD (STB)

- **No Prior Approval of Rail Rates:** First, it is important to understand that the major railroads are not required to obtain prior approval from the STB for any rate quoted to any shipper. Nor are the major railroads required to file their rates with the STB, post them on their web site or otherwise publish their rates. Rather, if a rail customer wants a rate quoted, the customer requests a rate from the railroad.

- **Two Types of Rail Rates:** Rail customers move freight on railroads pursuant to two types of rates. The first type is a rate that is a confidential rate that is included in a contract between the railroad and the customer. The fact that the rate is in a contract doesn't necessarily mean it was "negotiated"; it may have been dictated by the railroad. Contract rates are not jurisdictional to the STB, but are subject to the nation's antitrust laws. Contract compliance issues are litigated in court or in arbitration.

  The second type of rate is in a "tariff" designated by the railroad. These rates are jurisdictional to the STB and may be contested through the "rate reasonableness process" of the STB. These types of rates, being subject to the STB's exclusive jurisdiction, are not subject to the nation's antitrust laws.

- **The STB Rate Challenge Process:**

  - If a rail customer is "captive" to a railroad, the customer can challenge the rate at the STB as being "unreasonably high". The rail customer must prove it is "captive" and that the rate is unreasonably high.

  - The rail customer demonstrates it is "captive" to a railroad by proving (1) that the rate in question has a revenue-to-variable-cost ratio (R/VC) higher than 180% (rates lower than this level are not jurisdictional to the STB) and (2) that the rail customer has no economically viable transportation alternative to moving its freight on the defendant railroad.

  - For purposes of the STB challenge process, the rail rate in question must be converted to its "revenue-to-variable-cost ratio". The cost portion of this information is not provided by the railroad and can be the subject of controversy.

  - In the R/VC ratio, revenue (R) is the rate that is being charged to move the rail car in question. Variable Cost (VC) is the long-term variable cost to the railroad of moving the rail car in question. VC includes such factors as labor cost, fuel cost, and a fee for the use of the locomotive. VC does not include overhead, such as the track bed and rail, the bridges and headquarters costs of the railroad. If the R/VC ratio is 100%, then the revenue being charged to move the car equals the long-term variable cost to the railroad of the movement.

- For purposes of studies of "excessive" rail rates, the STB and most other entities use a 300% R/VC level as a surrogate for "excessive". Many rates charged rail-dependent shippers are far in excess of 300% and can exceed 1,000%.

- To win a reduction in the rate being challenged, the rail customer must prove "stand alone cost" ("SAC") – the cost the rail customer would have to charge itself on a hypothetical, efficient railroad built at current costs. This simple statement describes an incredibly complex and ever changing battle between the customer and the railroad over the details of the "virtual" railroad proposed by the rail customer.

- If the rail customer convinces the Board that these virtual railroad is a "realistic" railroad and that the rate to be charged by this virtual railroad is calculated correctly, the Board may order the rate being charged by the actual defendant railroad to be reduced to the SAC rate.

- These rate cases can cost up to $7 million in legal and economist fees and require three to four years to litigate (if not more). In addition, the rail customer pays the rate being challenged throughout the proceeding until the Board orders the rate reduced. In the case of chemical shippers moving freight on many challenged routes, the "bundling" approach of the defendant railroad can cost the chemical company $15 million or more in increased tariff rate charges during the pendency of the case.

- No other federal, state or local economic regulatory body in the United States uses the "stand alone cost" rate standard. Moreover, we know of no economic regulatory body in any nation in the world that uses the SAC rate standard.

- Obviously, very few rail-dependent shippers can afford to challenge a rate at the STB under this process. Currently, there is one coal rail rate case and three chemical rail rate cases at the STB.

* **The rate challenge process at the STB does not protect rail-dependent shippers from excessive rates and must be changed. Rail customers prefer the protections of market competition to this unworkable rate-challenge process.**