STB Update

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NATIONAL COAL TRANSPORTATION ASSOCIATION

2015 National Conference, September 16, 2015
Denver, CO
PTC Extension and Railroad Shutdown?

- Railroads have pressured Congress to extend the PTC implementation deadline of December 31, 2015.
- Pending legislation would grant three additional years to comply with the mandate (H.R. 22).
- If the legislation is not enacted, railroads are threatening that they may be forced to halt some or all of their rail services without the extension.
- STB Chairman Elliott has told Congress that the carriers may be excused from their common carrier obligation in this circumstance.
Transportation Research Board Report

- TRB conducted a study of Post-Staggers Act rail performance; ability to handle projected future demand; effectiveness of public policy balancing railroad and shipper needs; future role of the STB.
- TRB held hearings in 2014 and issued its report in June 2015
- TRB report sharply criticized the current regulatory regime on many fronts.
Transportation Research Board Report

• URCS is fundamentally flawed and, as a result, so is the rate relief mechanism the STB uses
• Allow reciprocal switching as a method of rate relief
• Revenue adequacy determination is outdated. Instead, the STB should perform periodic reviews of the industry as whole and related competitive conditions
• Transfer merger authority to traditional authorities and use customary antitrust principles
Rail Fuel Surcharges – EP 662 (Sub-No. 2)

*Rail Fuel Surcharges (Safe Harbor), Ex Parte 662 (Sub-No. 2)*

- **Background**
  - EP 661, *Rail Fuel Surcharges*, STB bans percent-of-price fuel surcharges on regulated traffic as of April 25, 2007; states that if any shipper wants further relief it can file an unreasonable practice complaint
  - 2 cases brought, *Dairyland* (settled 2008) and *Cargill v. BNSF* (relief denied 2013)

- STB-initiated proceeding to consider whether the “safe harbor” that the STB established in 2007 for railroad percentage-based fuel surcharges tied to highway diesel fuel (HDF) should be removed or modified
- Outgrowth of *Cargill* where Cargill showed that the surcharge produces substantial over recovery, but STB was unwilling to order any relief because BNSF had followed the STB’s rules
Rail Fuel Surcharges – EP 662 (Sub-No. 2)

- **Shippers’ position**
  - Surcharges should accurately reflect changes in costs, nothing more
  - Safe harbor produces over recovery by overstating the spread between the railroads’ actual price and the strike price
  - The formula overstates fuel consumption by ignoring improved efficiency
  - Low strike prices lead to double recovery (base rate reflects a higher fuel costs)
  - STB should eliminate safe harbor, require carriers to use changes in actual fuel prices and actual consumption, eliminate double recoveries, and certify and demonstrate accuracy in surcharges

- **Recent Developments**
  - Falling fuel prices
  - On December 16, BNSF announced it would end fuel surcharge for carload traffic in February, going with all-in rate (AG shippers then complain about the “largest freight rate increases in wheat freight rates in recent history”)
  - Upcoming increases in base rates to reflect decreasing surcharge revenues?
Railroad Revenue Adequacy

*Railroad Revenue Adequacy, Ex Parte No. 722*

- **Background**
  - STB reconsidering its standard for measuring railroad revenue adequacy
  - STB also considering implementation for railroads of Revenue Adequacy Constraint under *Coal Rate Guidelines*

- **Why It Matters**
  - Rebalance rights of railroads and captive shippers
  - Sharper scrutiny of captive coal rates assessed by revenue adequate railroads
  - Correct false impression that railroads are not earning enough to be sustainable for the long-term
# Railroads’ Historical Revenue Adequacy, Using STB Cost of Capital

<table>
<thead>
<tr>
<th>Year</th>
<th>Cost of Capital</th>
<th>BNSF</th>
<th>UP</th>
<th>NS</th>
<th>CSX</th>
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<tbody>
<tr>
<td>2004</td>
<td>10.10%</td>
<td>5.84%</td>
<td>4.54%</td>
<td>11.64%</td>
<td>4.43%</td>
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<tr>
<td>2005</td>
<td>12.20%</td>
<td>10.32%</td>
<td>6.34%</td>
<td>13.21%</td>
<td>6.23%</td>
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<tr>
<td>2006</td>
<td>9.94%</td>
<td><strong>11.43%</strong></td>
<td>8.21%</td>
<td>14.36%</td>
<td>8.15%</td>
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<tr>
<td>2007</td>
<td>11.33%</td>
<td>9.97%</td>
<td>8.90%</td>
<td>13.55%</td>
<td>7.61%</td>
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<tr>
<td>2008</td>
<td>11.75%</td>
<td>10.51%</td>
<td>10.46%</td>
<td>13.75%</td>
<td>9.34%</td>
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<tr>
<td>2009</td>
<td>10.43%</td>
<td>8.67%</td>
<td>8.62%</td>
<td>7.69%</td>
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<tr>
<td>2010</td>
<td>11.03%</td>
<td>10.28%</td>
<td><strong>11.54%</strong></td>
<td>10.96%</td>
<td>10.85%</td>
</tr>
<tr>
<td>2011</td>
<td>11.57%</td>
<td><strong>12.39%</strong></td>
<td>13.11%</td>
<td>12.87%</td>
<td>11.54%</td>
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<td>2012</td>
<td>11.12%</td>
<td><strong>13.47%</strong></td>
<td>14.69%</td>
<td>11.48%</td>
<td>10.81%</td>
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<td>2013</td>
<td>11.32%</td>
<td><strong>14.01%</strong></td>
<td>15.39%</td>
<td>12.07%</td>
<td>10.00%</td>
</tr>
<tr>
<td>2014</td>
<td>10.65%</td>
<td><strong>12.88%</strong></td>
<td>17.35%</td>
<td>11.69%</td>
<td>10.18%</td>
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</table>
Railroad Revenue Adequacy

• **Shippers’ position:**
  • Railroads are strong financially
  • Additional factors should be considered in measuring health
  • Implementation of the Revenue Adequacy Constraint is overdue

• **Railroads’ position:**
  • Railroads remain far from achieving long-term revenue adequacy
  • Financial improvement has not come at expense of captive shippers
  • Measure revenue adequacy using replacement costs
  • No separate Revenue Adequacy Constraint should be developed
  • The STB should instead rely on stand-alone (replacement) cost as the “gold standard”

• STB Hearings held in July 2015
Petition of the Western Coal Traffic League to Institute a Rulemaking Proceeding to Abolish the Use of the Multi-Stage Discounted Cash Flow Model in Determining the Railroad Industry’s Cost of Equity Capital, EP 664 (Sub-No. 2)

- Filed in 2013
- The COC is a critical input for calculating variable costs, the associated jurisdictional threshold, and stand-alone costs.
- MSDCF-CAPM Hybrid overstates the COE
- In turn, overstates COC
- Hearings held in July 2015
# CAPM v. MSDCF COE

<table>
<thead>
<tr>
<th>Year</th>
<th>CAPM COE</th>
<th>MSDCF COE</th>
<th>Difference</th>
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<tbody>
<tr>
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<td>10.39%</td>
<td>15.95%</td>
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<tr>
<td>2009</td>
<td>11.39%</td>
<td>13.34%</td>
<td>1.95%</td>
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<tr>
<td>2010</td>
<td>11.84%</td>
<td>14.13%</td>
<td>2.29%</td>
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<tr>
<td>2011</td>
<td>11.31%</td>
<td>15.83%</td>
<td>4.52%</td>
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<tr>
<td>2012</td>
<td>10.27%</td>
<td>16.53%</td>
<td>6.26%</td>
</tr>
<tr>
<td>Average</td>
<td>11.04%</td>
<td>15.16%</td>
<td>4.12%</td>
</tr>
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</table>

MSDCF increased the COE by a substantial amount, an average of 206 basis points during 2008-2012.
Maximum Reasonable Rate Proceedings

• Several coal (SAC) rate cases have been adjudicated/filed:
  • *WFA v. BNSF* (No. 42088) (2009, settled/dismissed 2015)
  • *AEPCO v. BNSF & UP* (No. 42113) (STB served Nov. 22, 2011) – Rate Relief at JT Level

• Recently – chemical rate cases:
  • *TPI v. CSXT* (No. 42121) – Pending
  • *M&G Polymers v. CSXT* (No. 42123) (Settled)
  • *DuPont v. NS* (No. 42125) – Rate Found Reasonable
  • *SunBelt v. NS & UP* (No. 42130) – Rate Found Reasonable
  • *Canexus v. BNSF Chemical* (Three-Benchmark) (No. 42132) (Settled)

• SAC chemical rate case issues – enormous complexity/costs
  • Multiple commodities
  • Multiple Origins/Destinations
  • Massive stand alone railroad systems
  • Massive burdens/expenses to litigate
Terminal Switching – EP 711


- Offshoot of NITL petition raised in STB Ex Parte No. 705, addressing terminal access
- STB asks for empirical information/study on shipper rate impacts, railroad industry impacts, and access pricing
- Requires detailed waybill sample analysis; matter in initial “study” stages
- NITL generally argues that proposal will have a modest impact on competition (affect only 4% of all carloads), but will result in meaningful competitive benefits to qualifying shippers, with a limited RR revenue impacts
- Railroads generally argue that proposal will have significant impact and will unreasonably disrupt rail service/operations
- STB holds hearings in March 2014
Questions?

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