



North American Rail Shippers Meeting

REGULATORY UPDATE

May 25, 2016

Karyn A. Booth

PRESENTATION TOPICS

- STB Reauthorization Act
 - Overview
 - Implementation
- STB Proceedings of Broad Significance
 - EP 704: Review of Commodity Exemptions
 - EP 711: Competitive Switching
 - EP 722: Railroad Revenue Adequacy

STB Reauthorization Act

STB REAUTHORIZATION ACT: OVERVIEW

- Bi-partisan bill passed in Dec. 2015
- Expands the Board from 3 to 5 members
- Allows Board members to engage in private discussions, subject to certain disclosure requirements
- Allows STB to initiate investigations of national or regional matters, subject to *de novo* review by the courts
- Directs the STB to report on status of pending cases maintain a database of complaints and to publish quarterly summary reports

STB REAUTHORIZATION ACT: OVERVIEW

- Requires STB consider ways to expedite large Stand-Alone-Cost (SAC) rate cases
- Requires GAO study on rate bundling practices
- Requires STB to create a voluntary arbitration process for rate and practice complaints

STB REAUTHORIZATION ACT: IMPLEMENTATION

- Two new Board members to be added but it's an election year!
 - New appointments unlikely until 2017
 - Commissioner Begeman is in holdover term and must depart after Dec. 31, 2016
- GAO has held stakeholder meetings re: rate bundling practices
 - gathering of facts regarding contract negotiations and purpose of bundling rates in either a tariff or contract

STB REAUTHORIZATION ACT: IMPLEMENTATION

- At the urging of Senator Thune, STB has moved promptly to implement the new law:
 - STB staff held stakeholder meetings in April on the issue of expediting large (Stand Alone Cost) rate cases
 - STB has issued reports on the status of pending proceedings, rate case reviews, and service complaints
 - STB has issued two new rulemakings on its arbitration procedures and investigative powers

STB RULEMAKING ON ARBITRATION

- On May 12, STB proposed to revise its arbitration rules
- Arbitrations would be voluntary and binding
- Proposal permits arbitration of unreasonable rail rates
 - market dominance threshold (i.e. absence of effective competition) remains an STB determination
 - seeks comment on ways to minimize delays due to market dominance determinations
- Disputes over railroad rules, practices and charges remain subject to arbitration
- Comments due on June 13; Replies on July 1

STB RULEMAKING ON ARBITRATION

- Proposal addresses:
 - process for initiation of arbitrations
 - relief caps: \$200,000 cap increases to \$2 million for practice disputes and \$25 million for rate disputes
 - arbitrator roster, qualification and selection
 - timeline for arbitrations—40 days to allow arbitration and decisions issued within 135 days thereafter
 - decisions have no precedential effect and may be appealed to the STB

STB RULEMAKING ON INVESTIGATIONS

- On May 16, STB proposed rules permitting the agency to initiate investigations on its own initiative
- Investigations must relate to matters of regional or national significance (not individual disputes)
- Investigations must be completed within 1 year
- Comments are due on June 15 and Replies on July 15

STB RULEMAKING ON INVESTIGATIONS

- Three-stage process:
 - **Preliminary Fact-Finding:** staff driven nonpublic inquiry; outside of 1 yr. period
 - **Board-Initiated Investigation** (with or without an initial fact-finding): nonpublic investigation to determine if statutory violation has occurred; discovery and settlements permissible
 - **Formal Board Proceeding:** must be started w/in 90 days of receipt of investigation findings; public participation allowed; only prospective relief may be ordered

STB Proceedings of Broad Significance

OTHER STB PROCEEDINGS

- STB has several proceedings pending that involve major policy issues or matters of national significance
- EP 704: Review of Commodity Exemptions
- EP 711: Competitive Switching
- EP 722: Railroad Revenue Adequacy

REVIEW OF COMMODITY EXEMPTIONS

- In the late 1980s/early 1990s many commodities were “exempted” from ICC (now STB) regulation
- STB opened a rulemaking in March 2016 proposing to revoke 5 commodity exemptions:
 - crushed or broken stone
 - hydraulic cement
 - coke produced from coal
 - primary iron or steel products, and
 - iron or steel scrap, wastes, or tailings

REVIEW OF COMMODITY EXEMPTIONS

- Statute authorizes revocation if regulation is necessary to fulfill the National Rail Transportation Policy and to prevent exercise of undue market power by RRs
- STB proposals are based on a Feb. 2011 hearing, waybill rate data for years 1992 through 2013, and other industry information
- STB has invited comments on its proposals and whether other commodity exemptions should be revoked
- Ext. of time granted: Comments due on July 27 and Replies on Aug. 27

COMPETITIVE SWITCHING

- Current law broadly permits competitive switching where it would be “practicable or in the public interest”
- But, no shipper has ever been granted switching access under STB rules adopted in 1985
- In 2011, NITL asked STB for new rules allowing captive rail shipper to “switch” its traffic to another rail carrier
 - shipper must meet certain conditions of captivity; lack of inter/intra-modal competition; reasonable distance to an interchange (30 miles)
 - carrier could avoid switching if unsafe, infeasible or harmful to existing service

COMPETITIVE SWITCHING

- NITL study shows shippers would save \$1.4 billion (2.6% of the Big Four RR gross revenue) across multiple commodities
- NITL estimated 1.4 million carloads would be impacted (or only 4.6% of all traffic); and most cars would not “switch” based on mandated switching exp. in Canada
- Railroads claim CSP would impact 7.5 million cars and cause severe congestion and service disruptions
- Railroads assert that Canadian network is different and not a good model for comparison

COMPETITIVE SWITCHING CONSIDERATIONS

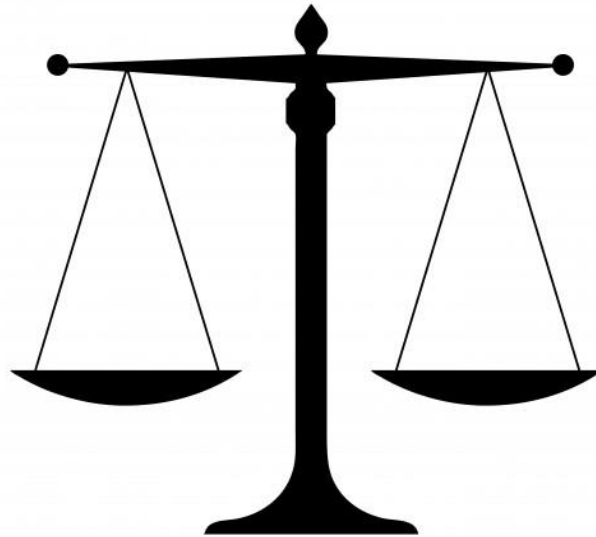
- Railroad service problems in late 2013 / 2014 may have caused further delays in STB decision-making
- In its pursuit of NS, CP touted “competitive access” as a viable competitive enhancement in rail mergers
- In April 2016, Executive Order issued by President Obama encouraging federal agencies to promote competition
- STB Report indicates a decision is expected in **June 2016**

REVENUE ADEQUACY

- STB determines whether each Class I railroad is revenue adequate annually, based on whether the railroad is earning the STB-calculated industry cost-of-capital
- Whether railroads are revenue adequate has been a key consideration in STB decisions and policy

STB MUST BALANCE OFTEN CONFLICTING POLICIES

**Rail
Competition**



**Railroad
Revenue
Adequacy**

RECENT STB REVENUE ADEQUACY DETERMINATIONS

	RR cost of capital	CSXT	NS	BNSF	UP	KCS	CN (U.S. part)	CP (U.S. part)
2014	10.65%	10.18%	11.69%	12.88%	17.35%	8.18%	11.30%	-0.42%
2013	11.32%	10.00%	12.07%	14.01%	15.39%	8.67%	11.84%	12.03%
2012	11.12%	10.81%	11.48%	13.47%	14.69%	9.54%	10.19%	5.15%
2011	11.57%	11.54%	12.87%	12.39%	13.11%	10.76%	8.74%	7.13%
2010	11.03%	10.85%	10.96%	10.28%	11.54%	9.77%	9.21%	8.01%
2009	10.43%	7.30%	7.69%	8.67%	8.62%	6.51%	6.04%	6.28%
2008	11.75%	9.34%	13.75%	10.51%	10.46%	7.72%	9.89%	9.29%
2007	11.33%	7.61%	13.55%	9.97%	8.90%	9.37%	10.11%	15.25%

REVENUE ADEQUACY

- STB initiated EP 722 proceeding to consider a **revenue adequacy rate standard** and to reconsider its methodology for calculating revenue adequacy
 - cost, complexity, and timing of SAC cases have increased calls for a more effective rate remedy
 - SAC relief has been especially elusive for carload shippers
 - as more railroads have achieved revenue adequacy, more opportunities to use as a rate standard

REVENUE ADEQUACY

- **Issues in the EP 722 Revenue Adequacy rulemaking:**
- How should the STB measure revenue adequacy and over what time period?
 - Book value, replacement costs, financial markets
 - Changes could bring RRs closer to, or further from, RA
- How can/should the STB apply a revenue adequacy constraint?
 - Rate increase limits
 - Benchmark comparisons to competitive rates
 - Refunding excess revenue to captive shippers

REVENUE ADEQUACY

- STB held a hearing on July 22-23, 2015
- STB exploring synergies between the major policy issues
- Record in the proceeding is now closed
- STB decision expected in Oct. 2016

Thank You!

Karyn A. Booth

Karyn.Booth@ThompsonHine.com

202.263.4108