October 5, 2016

The Honorable Daniel Elliott III
Chairman
United States Surface Transportation Board
Washington, DC 20423

The Honorable Deb Miller
Vice Chairman
United States Surface Transportation Board
Washington, DC 20423

The Honorable Ann Begeman
Commissioner
United States Surface Transportation Board
Washington, DC 20423

Dear Chairman Elliott, Vice-Chairman Miller and Commissioner Begeman:

The American Chemistry Council is writing you to highlight several troubling problems with the report, *An Examination of the STB's Approach to Freight Rail Rate Regulation and Options for Simplification* that was released on September 14, 2016. The report by InterVISTAS Consulting, Inc. falls far short of Congressional requirements established in the Surface Transportation Board Reauthorization Act of 2015. Even more troubling, the report offers no new ideas to modernize the STB's burdensome, time consuming and overly complex rate review methodologies. Despite the report's acceptance of the *status quo*, we urge the Board to continue moving forward to implement simpler and more accessible rate review procedures.

The need for new rate methodologies is clear. As stated by Chairman Elliott, "We should never be satisfied with a process that is so expensive and time consuming for all parties." Last year, the National Academy of Sciences' Transportation Research Board issued a report, *Modernizing Freight Rail Regulation*, developed by an independent panel of transportation experts and economists with input from a broad range of stakeholders. The NAS-TRB report concluded that the STB's rate review procedures "lack a sound economic rationale and are unusable by most shippers."

Based on a comprehensive analysis, the NAS-TRB report further determined that

> *"Faster, sounder, more transparent, and more economical methods* ***are available for resolving rate disputes*** *and could give more shippers the opportunity to pursue rate relief." [Emphasis added]*

One such method is rate benchmarking. As noted in the NAS-TRB report, "A wealth of information on unregulated, market-based rail prices now exists." These data can be used to develop models to predict rates in competitive conditions, providing a "benchmark for deciding whether a shipper's rate is unusually high."

In sharp contrast, the InterVISTAS report was prepared without public input by a consulting agency with a history of representing railroad interests. It provides an incomplete assessment the STB's current methodologies, including Stand Alone Cost (SAC). In particular, the report fails to consider how STB procedures have worked for carload traffic, which has very different distribution patterns than the coal shipments that SAC was originally designed to address. As noted by Commissioner Begeman in her dissent in the Sunbelt rate case, "The Board should ask whether the SAC process can provide a meaningful gauge of rate reasonableness for carload traffic shippers." It defies logic that the InterVISTAS report provides no examination of recent rate cases involving carload shippers to help the Board answer this important question.

Despite the extensive analysis presented in the NAS-TRB report, InterVISTAS does not explore the concept of rate benchmarking as a viable alternative to SAC methodology. The only alternative methodologies offered by InterVISTAS are the Board's existing Simplified SAC and Three Benchmark tests. This is baffling, since these procedures have been widely criticized and largely unused by shippers. The only basis for the report's endorsement of Simplified SAC and Three Benchmark is that, in a few examples, these methodologies appear to produce similar results as SAC. The report never explores *whether SAC actually provides the correct answer*.

The report also fails to address the application of the "revenue adequacy" component of Constrained Market Pricing (CMP), the economic foundation of the Board's rate review procedures. The report highlights one side of revenue adequacy, the need for a railroad "to earn revenue sufficient to cover costs, make normal profit and attract capital." However, InterVISTAS neglects to discuss how, under CMP, the Board defines revenue adequacy as

> *"a constraint on the extent to which a railroad may charge differentially higher rates to its captive traffic*."

Recognizing the importance of this rate constraint in the modern rail era, the Board has opened a proceeding, as described by Commissioner Miller, "to take a fresh look at revenue adequacy." Unfortunately, InterVISTAS overlooks the extensive comments and expert testimony presented in the Railroad Revenue Adequacy proceeding (EP 722), including concepts for workable, economically sound methodologies to determine the reasonableness of rail rates.

In the STB Reauthorization Act, Congress required STB to submit a report that indicates whether current large rate case methodologies "are sufficient, not unduly complex and cost effective" and whether "alternative methodologies exist or could be developed." The InterVISTAS report misses the mark on all counts, providing an incomplete analysis of existing methodologies and failing to consider the full range available alternative methodologies. This fundamentally flawed report should not draw any attention away from the Board's efforts to develop and implement simpler and more accessible rate review procedures. As stated recently by Commissioner Begeman, "It may not be easy (or very fast) to ultimately develop a new approach, but it has to be a top Board priority." Fortunately, the STB has a wealth of reliable data and analysis to draw on as it moves forward, including the comprehensive expert report prepared by the NAS-TRB.

If you have questions, please contact me at (jeff_sloan@americanchemistry.com; 202/249-6710).

Sincerely,

Jeff Sloan
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American Chemistry Council