BEFORE THE
SURFACE TRANSPORTATION BOARD

STB Docket No. EP 711 (Sub-No. 1)

RECIPROCAL SWITCHING

REPLY COMMENTS OF THE NATIONAL GRAIN AND FEED ASSOCIATION

The National Grain and Feed Association ("NGFA") hereby submits these Reply Comments in response to the Surface Transportation Board's ("Board" or "STB") Notice of Proposed Rulemaking ("NPRM" or "Decision") served on July 27, 2016 in this docket proposing revisions to the current rules governing the provision of reciprocal switching service pursuant to 49 U.S.C. §11102(c), codified at 49 C.F.R. Part 1145.

In its opening comments, the NGFA expressed strong support and enthusiasm for the Board's action in this docket to overturn 30-year-old agency precedent implementing §11102(c) that has stifled its use by rail shippers despite its express purpose and intent to foster competition between railroads via reciprocal switching when it is practicable and in the public interest, or where it is necessary to provide competitive rail service. The NGFA continues to support this long overdue action, and the NPRM as a whole, subject to the modifications the NGFA recommended in its Opening Comments. Herein, the NGFA replies to some of the points raised by parties filing opening comments in this proceeding.

I.
IDENTITY AND INTEREST OF NGFA

The NGFA, established in 1896, consists of more than 1,050 grain, feed, processing, exporting and other grain-related companies that operate more than 7,000 facilities and handle more than 70 percent of all U.S. grains and oilseeds. Its membership includes grain elevators; feed and feed ingredient manufacturers; biofuels companies; grain and oilseed processors and millers; exporters; livestock and poultry integrators; and associated firms that provide goods and services to the nation's grain, feed and processing industry. The NGFA also consists of 26 affiliated state and regional agribusiness associations, has a joint operating and services agreement with the North American Export Grain Association, and has a strategic alliance with the Pet Food Institute.

II.
REPLY COMMENTS

A. The Board Clearly Has Authority to Modify the Existing Reciprocal Switching Rules and the Railroad Interests' Arguments to the Contrary Must be Rejected

As the Board points out, it is hornbook administrative law that an agency is granted broad discretion to administer its governing statutes, and, to the extent that it seeks to depart from a prior interpretation of a statute, it must adequately explain the departure. Decision at 10 (citations omitted). Further, the new interpretation must be permissible under the governing statute. *Chevron U.S.A., Inc. v. Nat. Res. Def. Council*, 467 U.S. 837, 865 (1984) ("*Chevron*"). Under *Chevron*, "If Congress has explicitly left a gap for the agency to fill, there is an express delegation of authority to the agency to elucidate a specific provision of the statute by regulation. Such legislative regulations are given controlling weight unless they are arbitrary, capricious, or manifestly contrary to the statute." *Id*. at 843-44.

Although the NPRM is indeed a significant and welcome change in the past policies that the Interstate Commerce Commission ("ICC") adopted in implementing §11102(c), the NPRM

in-and-of-itself is straightforward from an administrative law standpoint in the sense that it uses as its starting point the plain statutory language, and the Board is fulfilling its duty of filling the gaps of the statutory language through a notice-and-comment rulemaking. For this, the Board is afforded substantial deference. Moreover, as pointed out in the Decision, it long has been recognized that §11102(c) and the Rail Transportation Policy permit a broad range of possible ways to implement §11102(c). Decision at 11, *citing Baltimore Gas & Electric v. U.S.*, 817 F.2d 108, 115 (D.C. Cir. 1987). In addition, the Board has fulfilled its duty at the proposed rulemaking stage to provide a detailed explanation in the NPRM of the salutary and numerous reasons and legal justifications for proposing to make this particular change at this particular time. Decision at 8-13. The Board thus has met the requirement of providing "a reasoned analysis indicating prior policies are being deliberately changed and not casually ignored." *Grace Petroleum Corp. v. FERC*, 815 F.2d 589, 591 (10th Cir. 1987), *cited* at Decision at 10.

Nevertheless, the U.S. Class I railroads, consistent with their collective position in EP 711, *Petition for Rulemaking to Adopt Competitive Switching Rules*, vociferously argue again in unison that despite specific statutory provisions like §11102(c) that expressly grant the Board authority to step in and facilitate rail-to-rail competition under certain circumstances, the Board cannot and must not take *any* additional steps whatsoever to facilitate *any* circumstances under which they could compete more with each other. They do so even though the modest proposals contained in the NPRM could present each of them with opportunities to compete for additional market share and revenues, and therefore strengthen their respective railroads and the railroad industry as a whole.

More specifically, in their opening comments the Class I railroads and their industry association have launched a barrage of faulty legal arguments challenging the validity of the

NPRM and the Board's authority to propose it. They also have reintroduced clearly exaggerated, speculative claims of the alleged potential harm of the NPRM (while some Class I railroads at the same time acknowledge that few shippers would or could seek such relief). This barrage appears to be not-so-subtle fear-mongering intended to intimidate the Board into withdrawing the NPRM and retreating to a more limited role of processing railroad rate reasonableness cases in lieu of enforcing §11102(c), should any shipper ever decide to file a complaint. The railroads strident arguments about the legality of the Board's actions in proposing the NPRM and its potential allegedly Armageddon effects on their respective systems and the rail industry as a whole should be summarily rejected. The NGFA addresses a few of these arguments below.

1. The Railroads' New Claim that the NPRM Does not Account for Their Reliance on Past Policies Concerning Reciprocal Switching Under §11102(c) is Misplaced

In the NPRM, the Board rightfully rejected the arguments made in EP 711 by the Association of American Railroads ("AAR") and its Class I railroad members that the Board does not have authority to change the existing rules governing reciprocal switching at 49 CFR Part 1145. These arguments included primarily their collective, yet misleading and fallacious claim that Congress had "ratified" the prior rules because it had not passed legislation proposed by shipper interests addressing competitive access and bottleneck rates. Despite the Board's lengthy, effective and persuasive explanation in the NPRM for rejecting these arguments, some of them, including the flawed "ratification" claim, have resurfaced yet again. *See e.g.*, Opening Comments of CSX Transportation at 26-30. The Board should continue to reject this baseless argument.

Railroad parties also have raised new arguments in support of a claim that the Board allegedly does not have authority to promulgate the NPRM's proposed rules. Most prominent among these new arguments from Class I railroads is that the Board cannot change the existing

rules regarding reciprocal switching in the NPRM because it has not taken into account that railroads have relied upon the past rules to make investments and business decisions. This new challenge to the NPRM also should be rejected summarily.

It is true that courts have considered an agency's failure to adequately take into account "legitimate reliance" on past policies it desires to change is an exception to the rule of *Chevron* that agencies are afforded a considerable amount of deference in promulgating rules and interpreting their governing statutes. However, there are very few examples of this principle being applied, and the NGFA did not discover any instances where a court applied it to a *proposed* rule, as opposed to a *final* rule or policy that is actually in force and effect. Nevertheless, the railroads now seek to apply this principle to the NPRM. Opening Comments of Union Pacific Railroad ("UP") at 7-21; Opening Comments of Norfolk Southern Railway ("NS") at 12-17. Opening Comments of the AAR at 40. For example, in its opening comments, NS asserts that the STB "has ignored the serious reliance interests engendered by its longstanding forced access policies," and so according to NS the proposed rule is arbitrary and capricious. Opening Comments of NS at 14, citing *Smiley v Citibank*, 517 U.S. 735, 742 (1996). Other railroad commenters also cite the *Smiley* case and other cases cited by NS in support of their version of the "reliance" argument. The railroads' attempt to apply this principle to the NPRM is wrong-headed and fails. In *Smiley*, the U.S. Supreme Court explained the applicable principle in *dictum* as follows:

> Of course the mere fact that an agency interpretation contradicts a prior agency decision is not fatal. Sudden and unexplained change or change that does not take account of legitimate reliance on prior interpretation may be 'arbitrary, capricious [or] an abuse of discretion,' 5 U.S.C. 706(2)(A). But if these pitfalls are avoided, change is not invalidating, since the whole point of *Chevron* is to leave the discretion provided by the ambiguities of a statute with the implementing agency.

517 U.S. at 742 (citations omitted). While *Smiley* is cited by the railroad parties in their opening comments as authority for their position that they legitimately relied on the past reciprocal

switching rules, it does nothing of the sort. In that case, the Court did not even find a change in a prior official agency position, so it never reached the issue of whether the agency adequately took into account any legitimate reliance. *Id.* [1] As explained below, the other cases cited by the railroads also do not support their position in this proceeding.

Distilled to its essence, the railroads' "reliance" argument is that (1) the prior agency interpretations of §11102(c) created a regulatory environment in which there was zero risk to them that a captive shipper would obtain an order from the ICC or the Board establishing competition with another railroad through reciprocal switching; and so (2) for the next 30 years they exploited this absence of risk by making investments and business decisions focused on single line movements without fear of having to compete with other railroads. *See, e.g,* NS Opening Comments at 13 (NS poured hundreds of millions of dollars into its system "based on the assumption that it would reap the rewards from providing single line service, knowing that the Board's forced access rules that could require the company to forego this single line, long haul service were sharply cabined by longstanding Board policy.") *See also,* UP Opening Comments at 15 (stating "[UP] would not have proceeded with the consolidations that created our current system had we been subject at that time to the proposed forced switching rules.").

In the first place, the longstanding policy of promoting single line railroad service has *always* existed side-by-side with statutory provisions promoting rail-to-rail competition. The development of railroads and markets through competition is a fundamental underpinning of the Staggers Rail Act. As one obvious example, statutes and policies promoting competition through

[1] Similarly, in its opening comments, UP cites *FCC v. Fox Television Stations, Inc.,* 556 U.S. 502, 515 (2009) as authority for its "reliance interests" arguments. However, legitimate reliance on past agency action that the agency did not take into account was not even raised by the parties in that case, and the only reference to this principle was in an introductory, general discussion of the applicable rules by the Court.

rail build outs and rail crossings always have been in place under 49 U.S.C. §10901. Shipper-funded rail build-outs to create rail-to-rail competition at locations physically served by a single railroad in single-line service were an effective way for some rail customers to negotiate acceptable rates and service terms through competition from the early 1990s until approximately 2004, when prior levels of competition between Class I railroads decreased to the point that making such investments became infeasible.[2] These build outs sometimes resulted in large single line segments of track of one railroad not being used for certain traffic for the term of a contract for that traffic awarded to a competing carrier. Yet, the railroads constructed their systems that exist today knowing this risk. Thus, for U.S. Class I railroads to claim now that their entire systems have been constructed in reliance on the past implementation of §11102, and that the limited rules proposed by the Board in this proceeding concerning reciprocal switching orders under §11102(c) will immediately result in the evaporation of single line service and the "re-Balkanization" [3] of the nation's rail system (UP Opening Comments at 7) is simply hyperbole.

More significantly, an argument that an agency failed to adequately account for "legitimate reliance" requires a showing of actual harm from such reliance. For example, in *U.S. v. Pennsylvania Industrial Chemical Corp*., 411 U.S. 655 (1973), a party had been convicted of a

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[2] *See, e.g.*, EP 705, *Competition in the Railroad Industry*, Joint Initial Comments of Omaha Public Power District, The AES Corporation, Oklahoma Gas & Electric Company and Colorado Springs Utilities (filed April 12, 2011); and Comments of Ameren Corporation, (filed April 12, 2011).

[3] The term "Balkanize" is frequently used by Class I railroads when measures to increase competition are proposed, but this term really is not applicable to them or the 21st century railroad industry. The typical definition of the term is "to break up (as a region or group) into smaller and often hostile units." See https://www.merriam-webster.com/dictionary/balkanize. Voluntary reciprocal switching occurs all the time in the railroad industry now, and it does not have the effect of divesting the rail assets owned by a particular Class I railroad, let alone produce the outcome of breaking up a Class I railroad into smaller railroads that are often hostile to or uncooperative with each other. Nor would the modest measures proposed in the NPRM trigger the breaking up of a Class I railroad into numerous, "hostile" smaller railroads in today's railroad industry.

criminal violation of a provision of the Rivers and Harbors Act. The U.S. Supreme Court, in a split decision,[4] found it was permissible for a trial court to permit evidence that by relying on a "longstanding, official administrative construction of" a particular statute, the convicted party may have been "affirmatively misled" into believing that its conduct was not criminal." *Id.* at 674. Thus, the complaining party incurred *actual* harm from its alleged reliance. Similarly, *Encino Motor Cars, LLC v. Navarro*, 136 S Ct. 2117 (2016), a case cited by NS and UP, addressed the question of whether an auto dealership that was being sued for its refusal pay overtime to certain employees could rely on a past U.S. Department of Labor position that supported the refusal to pay in spite of a subsequent regulation that took a different view but under which the agency did not adequately explain why it had changed its mind – in fact "the Department offered barely any explanation." *Id*. at 2126. Again, the party claiming reliance had incurred actual harm because of it.

In contrast, the courts have *not* found an agency to have acted arbitrarily or capriciously when the potential harm from such reliance is insubstantial, speculative or prospective. In *NLRB v. Bell Aerospace*, 416 U.S. 267 (1974), where the issue was whether the National Labor Relations Board should have changed a prior policy through an adjudication or a notice-and-comment rulemaking, the Court held, in relevant part:

> The possible reliance of industry on the Board's past decisions with respect to buyers does not require a different result [i.e. a rulemaking instead of an adjudication]. It has not been shown that the adverse consequences ensuing from such reliance are so substantial that the Board should be precluded from reconsidering the issue in an adjudicative proceeding. Furthermore, this is not a case in which some new liability is sought to be imposed on individuals for past actions which were taken in good-faith reliance on Board pronouncements. Nor are fines or damages involved here. In any event, concern about such consequences is

[4] Chief Justice Stewart and Justice Powell dissented, disagreeing with the majority's decision to reverse the Court of Appeals on the reliance evidence issue.

> largely speculative, for the Board has not yet finally determined whether these buyers are "managerial."

Id. at 296.

The railroads' newfound claim in this proceeding –incorrectly alleging that the Board has failed to account adequately for their purported reliance on prior precedent in developing the NPRM – is based on claims of economic, operational, and service harms from the proposed rules that are by definition hypothetical, highly speculative (and the NGFA maintains wildly exaggerated) and ill-founded *since no agency-ordered reciprocal switching has taken place in more than 30 years*! The railroads certainly have not incurred any actual harm from the *proposed* regulations, and there simply is not a shred of actual evidence that adoption of the NPRM, even as proposed, actually would result in the speculative gloom-and-doom the reams of railroad comments and expert statements allege will occur.

2. The Board's Action in Proposing the NPRM Clearly is Supported by the Statutory Language, Legislative History and Administrative Law Principles

In addition to their newfound "reliance" claim, the railroad parties spend a great deal of effort claiming the NPRM is not lawful based upon a conclusion of legislative history and past precedent. Opening Comments of AAR at 8-12. However, they do not, and cannot, argue that the Board's overall approach of proposing rules that closely track the statutory language of §11102(c) is, in and of itself, unlawful. This language plainly and unambiguously states that "the Board may require rail carriers to enter into reciprocal switching arrangements [1] where it finds such agreements to be practicable and in the public interest, or [2] where such agreements are necessary to provide competitive rail service." Instead, the railroad parties assert various arguments that the legislative history of §11102(c) does not support the changed interpretation of §11102 it has advanced.

However, the legislative history of §11102(c) contains ample evidence that Congress intended for §11102(c) to be a pro-competitive statute, and for the Board to implement it in such a manner. For example, the House Report on H.R. 7235 stated:

> This section empowers the Commission to approve reciprocal switching arrangements and joint service agreements upon the request of a carrier or shipper. In geographic areas where reciprocal switching is feasible, it provides competition to the benefit of shippers served. While the Commission now has the power to order the joint use of terminal facilities, its power to order reciprocal switching is less clear. In particular, reciprocal switching has been limited to situations where competition between carriers has not been threatened. *The Committee intends for the Commission to permit and encourage reciprocal switching as a way to encourage greater competition*. Likewise, joint service agreements should be encouraged in order to improve shipper service and efficiency.

H. Rep. No. 96-1935, on Staggers Rail Act of 1980 at 67 (emphasis added). The House Conference Report on the bill contained similar language stating that "the Senate authorized the Commission to require railroads to enter into reciprocal switching where it finds such agreements to be practicable and in the public interest" and "[i]n areas where reciprocal switching is feasible, it provides an avenue of relief where only one railroad provides service and it is inadequate." House Conference Report No. 96-1430 at 67. This statement was informed by the Conference Committee's overarching view that §11102(c) was one of "[a] number of provisions . . . included to foster greater competition." *Id*. at 80.

The railroad parties devote a significant amount of effort in their opening comments trying to refute this clear legislative intent by engaging in semantics and parsing language from ICC and court decisions discussing the legislation history. However, their analysis cannot (1) undo or change the clear intent of Congress when it enacted §11102(c) that it was to be used to foster rail-to-rail competition when circumstances dictated; or (2) alter the fact that the Board is afforded substantial discretion and deference in implementing this Congressional directive.

B. The Creation of Competition and Access in Accordance with the Statutory Directive of §11102(c) is not a "Back Door" Attempt at Rate Reasonableness Relief

Railroad parties also argue extensively that reversing the "competitive abuse" standard for reciprocal switching ordered under §11102(c) is solely a means for shippers to obtain lower rates in lieu of seeking them via the Board's rate reasonableness rules. *See e.g.*, Opening Comments of KCS at Part I. Apart from being a telling admission that rail rates in the absence of reciprocal switching are too high and might be reduced if true competition was introduced, this argument fundamentally is inconsistent with the railroads' persistent mantra that railroad rates should be set, to the maximum extent possible, by competition and market forces. The railroads cannot have it both ways. They cannot, on one hand, argue that increased competition between them should be stifled at every turn, leaving rail rates for captive shippers to be set by the Board via regulatory intervention dependent upon flawed rate-challenge methodologies that have proven to be unworkable for many shippers and then on the other hand argue that the Board should let all rail rates be set by market forces. A group of service providers would only make such an argument if (1) they were in a highly concentrated market; (2) they were collectively satisfied with the level of market power and market share they each currently possess; and (3) they were confident that the governing agency's rules for challenging unreasonable rates for their service were ineffective and insurmountably burdensome. The latter component has been demonstrated in the railroad industry by the reams of evidence and testimony collected by the Board in EP 705, EP 711, EP 715, EP 665, EP 665-1, EP 665-2, and other proceedings.

The claim that the NPRM is merely an end run around the Board's ineffective rate reasonableness rules also is wrong because it ignores the fact that the need for reciprocal switching also includes the critical need for reliable service. A primary benefit to many agricultural rail

shippers of having access to two railroads, which the railroads for the most part gloss over, is that it meets the needs for a rail shipper to have the opportunity to mitigate the substantial harms that occur in the event of the recurring periodic service meltdowns in the railroad industry. As the Board witnessed most recently in 2013-2015 (as it did previously in 2006-07), the current structure of today's consolidated railroad industry, where four railroads handle over 95 percent of all freight, is susceptible to serious, nationwide service meltdowns that cause considerable uncompensated economic harm to railroad customers. In EP 711 and EP 724, *United States Rail Service Issues*, the Board received oral and written testimony from some rail shippers that having access to another railroad could have alleviated some of the significant commercial harms they incurred because the service of the only railroad they are connected to had deteriorated as a result of a variety of factors, including weather-induced disruptions, constrained capacity, and insufficient supplies of locomotives, equipment and crews. Further, access to two railroads through reciprocal switching also meets the need of many agricultural shippers to access customers and market opportunities in different geographies. These aspects of today's railroad industry provide additional ample support for the Board's decision to change its prior policies regarding reciprocal switching requests under §11102(c).

C. The Railroads Have Once Again Wildly Overstated the Potential Impact of the NPRM on their Systems and the Railroad Industry

Class I railroad commenters take the Board to task for its brief mention of the information gathered pursuant to its request for information issued in EP 711 on July 25, 2012, modified by its decision served October 25, 2012. Opening Comments of AAR at 4; Opening Comments of NS at 46-47; Opening Comments of CSX at 5-6. This attack is ironic, given that the Class I railroads for the most part refused to meaningfully participate in that phase of EP 711, claiming that to comply with the Board's requests for empirical evidence on the impacts of the NITL proposal was

"impossible," among other excuses.[5] Moreover, to the extent railroad parties provided any data to the Board in that proceeding, it was simplistic and incomplete. *See, e.g.*, EP 711, Opening Comments of the AAR at 3, which absurdly and without substantiation asserted that more than one-third of all rail shippers could be eligible for relief under the NITL's proposal based simply on a determination by AAR's expert of how many shippers were within 30 miles of a junction point with a second railroad. Moreover, the railroads collectively refused to even discuss potential access-price formulas. Rather than submit the empirical evidence the Board requested, the railroad parties in EP 711 presented a litany of unsupported, speculative impacts on the railroad industry. Consequently, the complaints of Class I railroads in this proceeding that the data collected by the Board in EP 711 on the impacts of the NITL proposal may not have been extensively relied upon in drafting the NPRM ring hollow.

The railroads and their experts again have introduced a long "parade of horribles" in response to the NPRM. However, their strident claims of massive harm and disruption are again undermined and refuted by several factors. First, as even AAR and KCS acknowledge, only a small percentage of shippers potentially would or could seek relief under the new rules, thereby mitigating any potential widespread harm to the railroad industry. *See* AAR Opening Comments at 21 (The rail industry is "mature," and "[s]ince the market already provides for multi-carrier access where such access is economically viable, there is no reason to expect many cases seeking to require it."); and KCS Opening Comments at 5-6 (where KCS cites to the comments of the NGFA and other shippers in EP 711 that the NITL proposal would have only potentially benefitted

[5] *See* EP 711, Opening Comments of CSX Transportation Inc. at 3; Opening Comments and Evidence of Kansas City Southern Railway at 19; Comments of Norfolk Southern Railway Company at 7; and Opening Comments and Evidence of Union Pacific Railroad Company at 58-61.

a small number of agricultural shippers, and makes no case that the NPRM would materially expand that number).

Second, railroad parties have made similar claims regarding "avalanches" of cases and widespread railroad industry disruption whenever the Board has adopted changes to its rate reasonableness rules, and such apocalyptic outcomes, of course, have never come to pass. As the NGFA has explained in past proceedings with respect to agricultural shippers, this is because not every shipper that might be eligible for regulatory relief will choose to seek it. Many will forego such an effort because of cost, business considerations, or fear of retaliation by their serving railroad. Moreover, the NGFA submits that the result of changing the rules governing reciprocal switching orders to eliminate the "competitive-abuse" standard and replace it with rules that more closely track the statutory language and Congressional intent merely will have the beneficial result of encouraging dialogue between railroads and their customers, altering the negotiating parameters that underlie commercial rail transportation service arrangements that will be consummated outside the Board's purview, as Congress intended when passing the Staggers Rail Act. Consequently, the NGFA anticipates only the most economically meaningful cases where such agreements cannot be struck may find their way to the Board.

Third, the railroad parties once again completely ignore the extensive evidence and testimony presented in EP 711 that in Canada, where reciprocal switching regulations are much more liberal than the United States, the inherent advantages of the incumbent railroad mean that it retains its single line haul the vast majority of the time. *See e.g.*, EP 711, Opening Submission of the National Industrial Transportation League (filed March 1, 2013) at 60, and Verified Statement of Thomas Maville (demonstrating that less than 4 percent of traffic that could be interswitched in Canada actually is). Ironically, though, it is the NGFA's understanding that the Board is aware

that in instances in Canada which reciprocal switching does occur because of the greater distances for interswitching zones permitted in Canada, it is U.S. Class I carriers (*e.g.*, BNSF Railway and others) that benefit from the increased access to routes and customers they previously did not have. Oddly, such Class I carriers apparently have no "issue" with reciprocal switching in these instances!

And finally, the railroads for the most part ignore or try to belittle the fact that the NPRM would provide them with a critical protection against a Board-issued order requiring reciprocal switching: namely, a switching arrangement will not be approved under either "prong" if "either rail carrier shows that the proposed switching is not feasible or is unsafe, or that the presence of such switching will unduly hamper the ability of that carrier to serve its shippers." Decision at 19; proposed 49 CFR §§1145.2(a)(1)(iv) and 1145.2(a)(2)(iv). This proposed "affirmative defense" would afford an affected Class I railroad with ample opportunity to present evidence arguing that reciprocal switching should not be ordered because it would result in one or more of the claimed harms the railroads portray in their opening comments. This being said, for all the reasons set forth in the NGFA's Opening Comments in this proceeding, given the troubling uniform and emphatic objection of all of the Class I railroads to the establishment of conditions that would foster some modicum of competition between them through reciprocal switching ordered by the Board, the NGFA urges the Board to be very cautious and wary when establishing rules for presenting and entertaining such claims in proceedings under the new regulations. *See* NGFA Opening Comments at 17-18.

D. The Compensation Formula Adopted by the Board Must not Include a Component that Provides the Incumbent with "Lost Profits" or "Opportunity Costs"

In its Opening Comments the NGFA advised the Board to summarily reject the suggestion by UP that the incumbent railroad which is ordered to provide reciprocal switching should be paid for lost contribution or opportunity costs if reciprocal switching is ordered. NGFA Opening Comments at 15-16; Decision at 25. In doing so, the NGFA cited the submission of the Agricultural Parties in EP 711 demonstrating that the Board long ago disposed of the dubious notion that the creation of competition where shippers are captive requires paying the incumbent opportunity costs or lost profits. EP 711, Reply Comments of the Agricultural Parties at 11-13. The NGFA cited as a representative example of such precedent Finance Docket No. 32630, *Omaha Public Power District- Petition under 49 U.S.C. 10901(d)*(served August 1, 1996) 1996 WL 428901 at *2. In that case, in which UP obtained competitive access to a coal fired power plant via a shipper build out that involved crossing the predecessor to the BNSF Railway, the STB rejected Burlington Northern Railroad's ("BN") claim that its compensation merely for competitive access being established by the crossing should have been a fee set at the level of BN's potential lost profit minus the cost to the shipper of establishing the access. Accordingly, BN's proposed crossing fee of $28.2 million was rejected and a fee of $5,320 was established by the Board, which added that "BN's proposed [lost profits] compensation plan is contrary to the Congressional directive that we foster competition." *Id*. at *3).

In their opening comments, railroad parties predictably advocate, contrary to this established precedent, that any compensation formula developed by the Board under the reciprocal switching rules must include the payment to the incumbent railroad of their lost profits or opportunity costs. UP Opening Comments at 51-52; KCS Opening Comments at 45-49; and CSX Opening Comments at 93-95. For its part, KCS argues that the compensation for lost profits is required to ensure the incumbent attains revenue adequacy. KCS Opening Comments at 46. The

arguments of KCS and other railroads for compensation that includes lost profits are obviously intended to, and would, defeat the entire purpose of the NPRM by ensuring that an incumbent railroad charging high, arguably unreasonable, rates would always retain the single-line movement because its monopoly profits would be preserved through the compensation paid by the competing railroad. This would remove the incentive of a competitor to offer a lower rate or better service terms, or the shipper from pursuing the reciprocal switching in the first instance. For this reason, the claim for "lost profits" was disposed of by the Board in *OPPD*, where BN's "exorbitant" crossing fee including lost profits would have discouraged UP from building a competing rail line, "a result that, if effective, would limit UP's ability to provide service and hence constrain UP's ability to earn adequate revenues. Enhancing one carrier's opportunity to earn revenues at the expense of another's does not enhance the Congressional policy that we assist the railroad industry in achieving revenue adequacy." *OPPD* at *3.

KCS and CSX also float the creative, but illogically flawed, argument that failure to reimburse an incumbent railroad for its full opportunity costs would be an unconstitutional taking of a carrier's "property" by the government. KCS Opening Comments at 49-50; CSX Opening Comments at 94. However, for the Board to even entertain such an argument, it would first have to make the giant leap of equating reciprocal switching – the mere operation by a carrier of another carrier's equipment *over the first carrier's tracks* – with the actual *forced sale to another party under or sale of abandoned rail line* 49 U.S.C. §10907 or §10903, respectively. KCS Opening Comments at 49, note 47. Similarly, CSX would have the Board treat reciprocal switching as the equivalent of a taking of private property by the government for public use. CSX Opening Comments at 94-95. Such comparisons are *prima facie* untenable for numerous reasons, not the least of which is that in the case of reciprocal switching, no rail assets are being taken from the

incumbent by any party, let alone by the government. KCS and CSX also would have the Board completely ignore the fact that railroads by law own and operate on their lines subject to the requirement that such ownership and operations must be in the public interest. *See* KCS Opening Comments at 50, alleging that the right to operate over a track is a property right that cannot be diminished by the Board without full compensation. *See* CSX Opening Comments at 95 (a railroad's ability to control access to a facility is a property right that cannot be taken without full compensation for lost profits). However, in the end, the argument for "full compensation" in exchange for access by another carrier for the purpose of creating competition is simply another version of the "exorbitant crossing fee" disposed of by the Board in *OPPD.* It wrongly seeks to preserve the monopoly of the incumbent railroad at the expense of the ability of a competing railroad to provide service and earn adequate revenues, which is contrary to law.[6]

E. Other Comments

In addition to the foregoing, the NGFA has the following comments on several points raised by rail shipper interested parties and short line interests in their opening comments.

1. Evidentiary Sequence

The NGFA concurs with the suggestion of the Shipper Coalition for Railroad Competition that an incumbent railroad which seeks to raise the affirmative defense that the requested switching is infeasible, unsafe or will unduly hamper service to other shippers should present such evidence in the opening evidentiary round. Opening Comments of Shipper Coalition for Railroad Competition at 27-29. Similarly, an incumbent should identify and support claims of the alleged detriments of the proposed switching arrangement at this stage of the process. *Id.*

[6] Further, the NGFA also notes that interswitching rates established by the Canadian Transportation Agency do not include opportunity costs for Canadian railroads. http://laws.justice.gc.ca/eng/regulations/SOR-88-41/page-1.html#docCont

2. "Can be" a Working Interchange

The NGFA notes that the Shipper Coalition for Railroad Competition supports the NGFA's assertion that the Board's proposed definition of whether there "can be" a working interchange at a particular location is far too narrow. *Id*. at 41. The NGFA reiterates its recommendation at page 8 of its Opening Comments that the Board should not exclude from consideration instances where necessary switching infrastructure is not present, but the shipper and the involved railroads can mutually agree on how to finance the cost of needed construction and how to properly allocate liability and insurance considerations. *See also*, Shipper Coalition Opening Comments at 41.

3. Class II and Class III Railroads

In its Opening Comments the NGFA recommended that all Class II and Class III railroads should be subject to the new reciprocal switching rules. NGFA Opening Comments at 4-5. After review of the opening comments submitted by shipper and short line railroad interested parties in support of the proposed categorical exclusion, the NGFA has slightly modified its view on this issue. Specifically, while the NGFA understands why Class III railroads should be excluded for the reasons expressed by various parties, it still maintains that some Class II railroads have grown large enough to be considered for requests under §11102(c) on a case-by-case basis. It therefore reiterates its recommendation that this feature be included in the new rules for Class II railroads.

4. Market Dominance

Finally, the NGFA reiterates its prior recommendation that the second "prong" under the new rules should either eliminate the requirement of demonstrating market dominance, or greatly simplify the rules and standards for market dominance under rules implementing §11102(c). The NGFA disagrees with other shipper commenters that the Board should apply the market dominance rules it applies in coal rate cases, or the so-called "limit-price" standards, to reciprocal switching

requests when it is necessary to provide competitive rail service. *See* Opening Comments of Shipper Coalition at 42-43.

III.
CONCLUSION

In conclusion, the NGFA continues to enthusiastically support the Board's publishing of the NPRM and its general approach of (1) overturning the "competitive abuse" standard of *Midtec*; and (2) replacing the prior standards with new regulations that more closely adhere to the statutory language of 11102(c).

The arguments of Class I railroad commenters that the Board has acted arbitrarily or capriciously simply are wrong and have no support in law or case precedent. Their claims of the potential harm this modest proposal will cause the railroad industry are wildly speculative and exaggerated. Their collective position that the Board should take absolutely no steps that could result in increased competition in the 21st century railroad industry is both revealing and troubling, as well as contrary to the express language of §11102(c), its legislative history, and the fundamental principles of the Staggers Rail Act and ICCTA. Accordingly, the NGFA urges the Board to press forward with all deliberate speed to promulgate a final rule, and to provide more details and guidance in the final regulations and the decision adopting them to address the points raised by the NGFA in its Opening Comments and these Reply Comments.

Respectfully submitted,

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January 13, 2017