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D.C. Circuit Affirms Surface Transportation Board's
Finding of Unreasonable Rates in U.S. Magnesium Three Benchmark Case

On December 28, 2010, the United States Court of Appeals for the D.C. Circuit denied the Union Pacific Railroad Company's petition for review of the Surface Transportation Board's January, 2010 decision awarding U.S. Magnesium LLC \$1,000,000 in reparations and future rate relief from the common carrier rates UP established for two rail movements of USM's chlorine. USM had challenged the reasonableness of the rates in STB Docket NOR 42114, under the Three Benchmark framework adopted by the Board in *Simplified Standards for Rate Cases*, STB Ex Parte No. 646 (Sub. No.1). The opinion and order were issued by the court in Case 10-1019, *Union Pacific Railroad Company v. Surface Transportation Board*. GKG Law, P.C. was counsel for USM before the STB and as the intervenor in the D.C. Circuit proceeding. Set forth below are several comments and observations on the court's opinion and the underlying STB decision.

UP's appeal challenged the Board's selection of USM's comparison traffic groups for the Three Benchmark rate analysis. Under the Three Benchmark process, the parties – using data provided by the STB - assemble and submit groups of movements that they believe are most comparable to the movements at issue in the case. These comparison groups are submitted in a "final offer arbitration" format, and the rules provide for simultaneous rounds of evidence and a discretionary technical conference before the Board staff. While the rules don't require oral argument, the current Board has added it to the process. Under the rules, the Board must accept one party's comparison group(s) without any modifications. While the STB concluded in its January decision that neither party's groups were ideal, it determined that USM's groups provided a better gauge of the proper comparison to the issue movements. This was primarily because UP's groups had included "re-billed" traffic (traffic UP interchanges with other railroads as part of a longer joint line movement. Rule 11 movements are also rebilled movements). More specifically, in addition to being operationally different than the issue single line movements, UP's rates for rebilled movements had margins that were well in excess of single line rates of comparable length, indicating that the re-billed movements had much different transportation demand characteristics than the movements at issue, which meant they were not comparable to the issue movements and therefore distorted the overall results.

There are several aspects of the case that might bear on future Three Benchmark cases, particularly cases challenging the reasonableness of chlorine rates.

1. Comparison Group Makeup – In the *USM* case, the Board backed away from its previous acceptance of a comparison group that contained chlorine and other TIH commodities in *E. I DuPont de Nemours and Co. v. CSX Transportation*, STB Docket 42100 (served June 30, 2008). In that case, which also involved challenges to chlorine rates, the Board accepted a mixed TIH traffic group in part based on the rationale that the operating and transportation demand characteristics of other commodities – primarily anhydrous ammonia – were reasonably comparable to chlorine. While the STB in *USM* ultimately accepted USM’s mixed TIH groups, it clearly retreated from its prior acceptance of mixed TIH traffic groups in *DuPont* and indicated it would favor chlorine-only comparison groups in future such cases. The D.C. Circuit decision contains language in support of the Board’s view. While this does not necessarily preclude a mixed TIH comparison group in future Three Benchmark cases challenging chlorine rates, complainants would appear to now have a heavier burden of demonstrating other TIH commodity movements are comparable to chlorine.

2. Rebilled Movements – The *USM* case was the first Three Benchmark case where rebilled movements were included in a comparison group to test the reasonableness of single line rail rates. The court supported the Board’s rejection of UP’s attempt to include rebilled chlorine rates primarily because UP never explained the large discrepancy between the revenues associated with the rebilled movements in its group and the revenues associated with the single line movements in the group. The rejection of rebilled movements in the *USM* case does not necessarily mean that rebilled rates can never be used in a comparison group in a case challenging single line rail rates, but the overall comparability of such movements to the issue movements would have to be convincingly demonstrated.

3. STB Participation in Three Benchmark cases - As proposed, the *Simplified Standards* would have required a mandatory technical conference with STB staff immediately after opening evidence is filed in Three Benchmark cases. This was part of the agency’s stated intent to have a collaborative process for preparing final comparison traffic groups. However, the final version of the rules, despite still referring to STB staff participation in the process, made such technical conferences discretionary. STB staff did not require technical conferences in either *DuPont* or *USM*. Nevertheless, the Board (and the court) criticized both parties in *USM* for choosing to not modify their opening comparison group submissions. Complainants in future Three Benchmark cases should weigh the pros and cons of proactively requesting that a technical conference be held after opening evidence, which in addition to perhaps limiting the issues in dispute, would also limit the STB’s ability to criticize the record after the fact.

For a copy of the decision, or if you have questions, please contact:

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