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TransLaw

VIP Profile: Joe Taney, Federal Security Director

Salt Lake City International Airport, Transportation Security Administration, U.S. Department of Homeland Security

Background: Joe Taney joins the TSA as the FSD for Utah after 11 years as Vice President of Ground Operations for Northwest Airlines (NWA) and 25 years with NWA. A graduate of the University of Wisconsin at River Falls in Social Science, Taney possesses a strong operational background in aviation management.

Family: My wife of 29 years, Karyne; two children, Bryn, 18; Weston, 15.

Favorite Food: It's a tie between a special chow mein (only made in St. Paul, Minn., by a local mom and pop type restaurant) and a specially seasoned "pork chop on a stick" sold only at the Minnesota State Fair (the only food I would ever stand in line for).

Favorite Book: I don't have an all time favorite, but I enjoy anything by Stephen King or Dean Koontz. Both have a similar genre as a science fiction/suspense angle. Even though I read the book *It* years ago, it still scares me.

Favorite Movie: The original *Star Wars, Lord of the Rings, Saving Private Ryan, Pearl Harbor, Pulp Fiction, The Hangover, Blazing Saddles,* and *The Matrix*.

Favorite Character: Tom Hanks in *Saving Private Ryan*, as a former elementary teacher now leading a group of men defending a critical bridge. Either that, or Mongo!

Favorite Pastime: Watching a spring training baseball game on a hot sunny day in Florida or Arizona in March, or dressing up in full leather and riding my Harley, with no particular place to go.

Favorite Hobby: I have a Korg keyboard, and when the creative moment strikes, I can get lost for hours playing music. A close second is playing golf on a hot, calm day with friends.

Biggest Inspiration: My parents, my family, and my high school baseball coach rank highest, but I also get inspired by children, especially those who have a disability, yet live a life of joy. I am also moved by veterans who were put in harm's way and fought for our freedom. Taking the time to visit a Veterans Hospital and talk to those who were in WWII, Vietnam, the Gulf Wars, or in current conflicts.

***

TransLaw: You joined TSA as a Federal Security Director after heading operations for Northwest Airlines. What has been one of the biggest challenges you have experienced while working as an airline and aviation professional?

Taney: The biggest challenge I have faced is the complexity of commercial aviation. Due to all the outside variances or influences, some controllable and some not (like weather), today's aviation is very challenging. From government agencies and regulations, to complex scheduling, marketing, labor, fuel prices, fare structures, capital financing for aircraft and equipment, airport authorities, lease agreements, logistically handling luggage, cargo and people, weather and security requirements—these are only a fraction of the list of elements that need proper orchestration for airlines to operate efficiently.

TransLaw: What facet of your job do you find to be the most interesting?

Taney: As a leader of a large organization, you are normally not dealing with one single issue, nor are the issues sequential. Rather, you're involved in multiple issues, all with varying impacts to the organization, but always mentally prioritizing the work load. Thus the variety and unforeseen problems challenge you to act, which in turn provide for an interesting occupation.

TransLaw: What do you perceive to be your greatest personal accomplishment?

Taney: Professionally, it's seeing those in my organization become successful in their careers knowing I may have had some small influence in their development. Personally, it was starting out at an airline as a part time, temporary new hire, and rising to the position of a Vice President for Northwest Airlines, all the while enjoying my family and watching my kids grow. I'm still on a mission to break 80 in golf, but for now, claiming 82 as my greatest personal accomplishment will just have to do! ❖

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Chair's Corner

Nancy Kessler

I am delighted to take this opportunity to introduce our newly installed section board and preview our 2010 program line-up. I have been asked what my goals are this year and they are simple—to make sure we are the premier, "go-to" organization for legal programs in the areas of transportation and security law. Our mission is to address and educate lawyers on the legislative, judicial, and administrative legal developments affecting the nation's transportation and transportation security systems. With your help, we can present robust and valuable programs responsive to your needs.

We are kicking off the year with a series of Lawyers' Lunches co-hosted by the Department of Transportation (DOT). DOT General Counsel Bob Rivkin, was the featured guest at the March event, and the April event introduced David Heymsfeld, staff director of the House Committee on Transportation and Infrastructure, Gael Sullivan, Democratic professional staff member for the Senate Committee on Commerce, Science, and Technology, and Jim Kolb, staff director for the House Subcommittee on Highways and Transit, who enlightened us on legislative updates and debates in the transportation area. Stay tuned for our transportation security-related programs and our first webinar, which will discuss the needs of airline passengers with a disability and the Air Carrier Access Act. Watch your e-mail for an invitation to a networking social introducing area law school students to transportation and security law careers. And, we hope you will join us this fall at our signature event, a reception on Capitol Hill honoring the general counsels and chief counsels of the Departments of Homeland Security and Transportation, and recipients of the section's awards.

Feel free to let us know whether there are other programs you would like to see us develop, and we will try to incorporate them into our 2010 agenda.

I take this opportunity to welcome Thomas Lehrich as our new *TransLaw* editor. Tom and I worked closely on aviation matters while he was chief counsel with the Department of Transportation's inspector general, and I know that he has exciting ideas in mind for future *TransLaw* issues. Kudos to Tom for taking on the job while recuperating from foot and ankle surgery after a tennis injury!

We are grateful for the work performed by our past chair, Denise Krepp. She did such an outstanding job of promoting our section, hosting our first networking social for area law school students, and convening exciting programs, that the Federal Bar Association named her as an outstanding section chair for 2009. Additionally, we are proud to announce that Denise currently serves as chief counsel for the Maritime Administration.

Congratulations are also in order for Hector Huezo, our past *TransLaw* editor. At the FBA 2009 annual meeting in Oklahoma City, Okla., *TransLaw* received the Meritorious Newsletter Recognition Award in part due to his work on the publication.

Finally, thank you for your dedication and contributions to the section. Whether you are a new or continuing member, we value your membership and strive to meet your needs. ❖

Letter From the Editor

Thomas K. Lehrich

Welcome to our Summer 2010 edition of *TransLaw*. Our goal for the publication this year is to provide a forum that highlights transport and transport security for our members and the community. We will also feature a key article each quarter on transport and feature a leading transportation figure in our VIP Section. I want to thank Joe Taney, the FSD for Salt Lake City, for lending his time to share with us his insight on his career in aviation. A special thanks to Dave Rifkin, a well known transport and rail practitioner, for providing a informational article on rail rates. Enjoy our issue! ❖

Aviation Matters

Nancy Kessler and Hector Huezo

DOT APPROVES DELTA—US AIRWAYS "SLOT SWAP" SUBJECT TO SLOT REMEDIES AT REAGAN WASHINGTON NATIONAL AND LAGUARDIA AIRPORTS

What did US Airways and Delta Airlines seek? The airlines jointly petitioned the FAA to waive a provision in an FAA Order controlling "slot interests" (i.e., permission for aircraft takeoffs and landings) at LaGuardia Airport (LGA) to facilitate a permanent slot interest exchange. Under the integrated transaction, Delta would sell 42 pairs of slot interests to US Airways at Reagan Washington National Airport (DCA), its international route authorities to Sao Paulo and Tokyo, and its terminal space at the Marine Air Terminal at LGA. US Airways would transfer 125 pairs of slots interests to Delta at LGA and would lease an additional 15 pairs of LGA slot interests with a purchase option, plus terminal space in LGA's Terminal C.

On February 9, 2010, the FAA issued a Notice requesting comments on its tentative approval of the transaction subject to a divestiture of 14 pairs of slots interests at DCA and 20 pairs of slot interests at LGA to new entrant and limited incumbent carriers. US Airways and Delta subsequently proposed a different remedy in which 15 LGA pairs of slot interests (5 pairs each) would be transferred over approximately a 2 year period to AirTran Airways, Inc., Spirit Airlines, Inc. and WestJet, Inc. and 4.5 pairs at DCA to JetBlue Airways, Inc.

What were the terms of the final waiver subject to conditions? On May 4, 2010, the DOT granted the carriers' request for a waiver subject to: slot interest divestitures by US Airways (20 pairs of slot interests at LGA consisting of 2 bundles of 6 pairs each and 2 bundles of 4 pairs each), and by Delta (14 pairs of slot interests at DCA consisting of 1 bundle of 8 pairs and 1 bundle of 6 pairs) to carriers having fewer than 5 percent of total slot holdings at either airport, do not code-share with, or are not subsidiaries of, ineligible carriers; and making gates and associated facilities available upon request. The carriers must notify the FAA within 30 days as to whether they intend to proceed with the transaction and, if so, eligible carriers could make offers to purchase the slot interest bundles through an FAA website in which the purchasers' identities would be concealed. The selling carrier would keep all the sale proceeds. The grant of the waiver would become effective upon FAA approval of all slot interest bundle transactions.

Why do the airlines need a DOT waiver? The FAA's High Density Rule (HDR) historically has applied to slot-controlled airports and allows airlines to buy and sell their slot interests to any person for any consideration. Although DCA remains subject to the HDR, LGA, in contrast, is not. In 2000, Congress directed a phase-out of the High Density Rule at LaGuardia, such that the HDR expired at LGA at the beginning of 2007. Because a cap on operations at this sought-after airport is necessary to alleviate congestion and delays, the FAA has regulated operations at LGA under the terms of an Order, which expires in October, 2011. That Order allows slot interests to be leased or transferred but not permanently sold or purchased.

What factors did DOT rely on for its approval with conditions? The DOT found that the arrangement has a number of benefits—such as, enhancing the carriers' networks, producing efficiencies at LGA, and providing small community service but that the transaction as a whole would result in a substantial increase in market concentration at DCA and LGA that would harm consumers. The DOT found that the FAA and the Secretary have the authority to grant the waiver subject to conditions, that the FAA consistently exercises it slot allocation authority in a pro-competitive fashion; the slot remedies do not constitute unlawful airline "re-regulation" and are not "takings" for purposes of Fifth Amendment "just compensation."

Why didn't the DOT approve the DL-US counterproposal? The DOT found that the number of slot interest pairs in the counter-proposal was insufficient to mitigate the competitive harm that would result from the transaction and that the proposed private arrangements were structured to minimize the competitive impact on Delta and US Airways and thereby lessen consumer benefits.

Docket No. FAA-2010-0109; www.regulations.gov.

DOT PROPOSES TO GRANT ANTITRUST IMMUNITY TO "ONEWORLD" ALLIANCE SUBJECT TO SLOT REMEDIES AT LONDON'S HEATHROW INTERNATIONAL AIRPORT

What did the airlines seek? American Airlines, British Airways, Iberia, Finnair, and Royal Jordanian generally sought antitrust immunity from the Department to form a global alliance to closely coordinate international operations and launch an integrated joint venture in transatlantic markets. American Airlines and British Airways sought approval to expand their code-sharing relationship to implement the expanded opportunities resulting from the "open skies" U.S.-EU Agreement.

Why do the airlines need DOT approval? The Department has the authority to allow code-sharing if it finds that is in the public interest; the Department also has the authority to grant an exemption from the antitrust laws, in the context of foreign air transportation agreements. The Department uses a two-step public interest examination to approve foreign air transportation agreements. The first step relies on a "competitive analysis," and the second step—used when a transaction would substantially reduce or eliminate competition—analyzes whether the agreements are nonetheless necessary to meet a serious transportation need or to achieve important public benefits, such as advancing U.S. foreign policy goals. The Department will grant antitrust immunity when it "is required by the public interest" and when the parties would not otherwise go forward with the transaction. Also, if the Department determines that the transaction would substantially reduce or eliminate competition, yet merits approval, the Department must exempt the parties to the transaction.

What did the Department find? On February 13, 2010, the Department tentatively found the proposed oneworld alliance would enhance worldwide competition by potentially competing with the already-immunized Star Alliance and SkyTeam alliances. The alliance would benefit passengers and shippers through lower fares on more city-pair itineraries, new routes, more flights on existing routes, better schedules, reduced travel and connection times, and product and service (e.g., frequent flyer) enhancements. It would improve the efficiencies of the alliance partners, reduce their costs and strengthen their networks. The Department also tentatively found, however, that the proposed alliance could cause competitive harm between the U.S. and slot-controlled Heathrow International Airport, unless conditions were imposed.

What did the Department propose to do? The Department tentatively found that a grant of antitrust immunity is necessary to achieve the benefits of the proposed alliance and that the carriers must file records on the implementation of the alliance, file annual reports on commercial developments, submit traffic data, and withdraw from IATA tariff coordination. Additionally, to protect consumers against potential harm, the Department proposed that the applicants sell or lease four slot pairs at London Heathrow, for compensation, to competitors for new U.S.-London Heathrow services for a period of ten years, earmarking two slot pairs for Boston-London Heathrow service ("fixed slots") and allowing the other slot pairs to be used at any U.S. gateway ("flex slots"). Airlines would not be eligible for the slot transfers if they are members of oneworld, affiliates of the applicants or airlines in which the applicants have a substantial financial interest.

Objections to the Order to Show Cause are due March 31. DOT Order 2010-2-8, Dockets DOT-OST-2008-0252; 2002-13861, www.regulations.gov.

DOT GRANTS INTERIM STAY OF LOS ANGELES INTERNATIONAL AIRPORT AIRPORT-AIRLINE FEE DISPUTE

What is this proceeding about? Certain carriers operating at LAX asked the Department to declare various new and increased terminal fees to be unreasonable and unjustly discriminatory. These included fees

- based on fair market value/opportunity costs;
- charged for space previously paid for by airport merchants ("rentable" space); and
- based on specific maintenance and operations (M&O) costs.

In June, 2007, after an administrative trial-type proceeding, the Department issued a decision finding some of the disputed fees reasonable and some to be unjustly discriminatory. In August, 2009, the U.S. Court of Appeals for the District of Columbia Circuit issued its decision on the parties' petitions for review, remanding some of the issues to the Department. In November, 2009, the Department issued a Notice on procedures for handling the remanded issues.

What is new about the case? In January, 2010, the Department granted the parties' request for an interim stay to enable them to devote more time to reach agreement on the remanded issues. The Department stayed the proceeding on remand until October 18 and directed the filing of status reports on the progress of settlement discussions at 60 day intervals, beginning March 18.

Docket No. OST-2007-27331; www.regulations.gov

DOT DENIES AIRLINES' EXEMPTION REQUESTS FROM THE TARMAC DELAY RULE

What did the airlines seek? Certain airlines requested an exemption from the DOT tarmac delay requirements at John F. Kennedy International, Newark Liberty International, Philadelphia International and LaGuardia Airports, due to their concerns that their compliance with the rule would be unduly complicated by upcoming runway construction at JFK.

What did the Department do? On August 22, 2010, after giving notice and considering comments, the Department denied the request finding that the carriers did not provide adequate justification showing why the exemption from the rule was in

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Lawyers' Lunch: Transportation Legislative Update

Domenic Senger-Schenck, American University Law School

Speakers: Gael Sullivan, Democratic professional staff member, U.S. Senate Committee on Commerce, Science, and Technology; Jim Kolb, staff director, U.S. House Subcommittee on Highways and Transit; and David Heymsfeld, staff director, U.S. House Committee on Transportation and Infrastructure.

Moderated by: Nancy Kessler, chair of the FBA's Transportation and Transportation Security Law Section.

The 2010 Legislative Update for Transportation & Transportation Security, presented at the U.S. Department of Transportation headquarters on April 6, featured informational presentations and a question and answer session on the pending Federal Aviation Administration program and budgetary re-authorization, upcoming ground transportation legislation, and high-speed rail initiatives. After a brief introduction by moderator Nancy Kessler, the three Capitol Hill panelists addressed each subject in turn, taking questions from attending DOT, Federal Aviation Administration (FAA), and other agency employees and the private bar.

Gael Sullivan began the discussion by reviewing the pending FAA Reauthorization bill. Noting the series of extensions since the most recent authorization's expiration in 2007, he expressed optimism that, despite changing committee leadership, a new bill would be passed shortly. The primary obstacles to an earlier authorization included user fees and NextGen, issues which have been partially mitigated this year by putting aside user fees and focusing on modernization. Stressing a dedication to safety after recent aviation mishaps, Sullivan stated that modernization projects such as NextGen were the primary focus of the upcoming reauthorization. Answering questions from the audience, Sullivan explained that the new bill would not contain congestion fees but that a best-equipped and best-served policy was being considered.

Following Sullivan, Jim Kolb spoke about recent developments on surface transportation legislation. Calling the current bill one of the most important and difficult since the interstate system was constructed, he expressed reserved optimism about the bill's probable success. Kolb considered the pending $450 million, multi-modal bill as having advantageous features, including a successful consolidation program. He also highlighted the bill's main objectives of promoting safety and asset preservation. Given the current economic situation, Kolb expects the bill's objectives to focus on short-term job creation rather than long-term infrastructure development. Overall, the bill's primary hurdle at this point is to overcome funding issues, as Congress explores options for appropriating the necessary funds without raising taxes. During the question and answer session, Kolb spoke about public/private partnerships, such as the Virginia high occupancy/toll lanes project, and explained that such approaches are being considered, although oversight is a concern.

Rounding out the presentations, David Heymsfeld spoke about rail and hazardous material legislation. Heymsfeld's comments focused on high speed rail, as he described recent initiatives to get the program started. After a funding level of $1.5 billion in 2008 and $8 billion from the American Recovery and Reinvestment Act of 2009, additional funding could be expected in the upcoming reauthorization, though no dollar figure has yet been set. Speaking to other topics, Heymsfeld noted additional funding for conventional rail, as well as initiatives in hazardous materials to outlaw "wet lines" in trucking and establishing new safety standards for shipping lithium batteries, but stressed that such initiatives were still struggling through the Senate. Answering questions about high-speed rail, Heymsfeld noted that Buy-America requirements were being strongly considered, and that general enthusiasm for the new rail system was high. ❖

MATTERS *continued from page 5*

the public interest. The rule requires carriers to adopt contingency plans for lengthy tarmac delays, including an assurance that an air carrier will not permit its aircraft to remain on the tarmac for more than 3 hours in the case of a domestic flight (and for more than a set number of hours in the case of international flights) without providing passengers an opportunity to deplane, with certain exemptions for safety, security, or air traffic control-related reasons. The Department found that the carriers can adjust their schedules and that the public interest would be better served by keeping the full protections of the tarmac delay rule in place.

75 Federal Register 21,692 (April 26, 2010); Docket No. DOT-OST-2007-0022, www.regulations.gov

DOT LITIGATION NEWS

Don't miss the 10th Anniversary (March 26, 2010) Edition of *DOT Litigation News*, found by visiting www.dot.gov/ost/ogc/News_March2010.pdf !

Growing Pains of the STB's Rail Rate Dispute Methodology for Small Sized Cases: *US Magnesium LLC v. Union Pacific Railroad Company*, STB Docket 42114 (Jan. 28, 2010)

David Rifkind

On January 27, 2010, the Surface Transportation Board ("STB" or "Board") ruled in a 2 to 1 decision that the Union Pacific's rates for shipment of chlorine between Rowley, Utah to Eloy, Arizona and to Sahuarita, Arizona were unreasonable. *US Magnesium, L.L.C. v. Union Pacific RR Co.*, STB Docket No. 42114 (served Jan. 28, 2010) ("*US Magnesium*"). This decision was just the fourth by the STB under its simplified rate case procedures for small-sized shipments.[1] Those procedures were revised in 2007, with the goal of making the rate reasonableness challenge process "more affordable and accessible to shippers of small and medium-sized shipments, while simultaneously ensuring that the new guidelines do not result in arbitrary ratemaking." *Simplified Standards for Rail Rate Cases*, STB Ex Parte No. 646 (Sub-No. 1), at 31 (Sept. 5, 2007) *("Simplified Standards")*. *US Magnesium* casts doubt on whether the STB has achieved its goals, in particular, its goal of avoiding arbitrary ratemaking.

The Regulatory Background

The STB has jurisdiction to hear rate reasonableness challenges where the carrier is "market dominant," *i.e.*, the rate exceeds 180% Revenue/Variable Cost ("R/VC") and there is no effective competition from other railroads or other transportation modes. *See US Magnesium* at 4. If the STB finds that a rate is unreasonable, it may prescribe rates subject to the 180% R/VC jurisdictional floor.

Prior to 2007, virtually all rate reasonableness challenges were brought under the Stand Alone Cost ("SAC") methodology. SAC is one of four pricing constraints under the constrained market pricing" ("CMP") principles adopted by the STB's predecessor, the Interstate Commerce Commission ("ICC"). *See Coal Rate Guidelines, Nationwide*, 1 I.C.C.2d 520 (1985) ("*Coal Rate Guidelines"), aff'd sub nom. Consol. Rail Corp. v. United States*, 812 F.2d 1444 (3d Cir. 1987). In addition to the SAC constraint, CMP contains a revenue adequacy constraint, a management efficiency constraint, and a phasing constraint. However, it is the SAC constraint that complainants primarily rely upon in rate challenges.

Under CMP principles, a reasonable rate (1) reflects the amount a captive shipper would have to pay for efficient service; (2) allows the carrier to recover its costs and reasonable return on capital investment; and (3) prevents cross-subsidization by assuring that the captive shipper does not bear the cost of facilities from which it derives no benefit. *Id.* at 523-24. CMP recognizes the need for differential pricing—*e.g.*, charging higher rates to shippers who lack a competitive alternative. Consequently, CMP meets the "dual objectives of providing railroads the real prospect of attaining revenue adequacy while protecting captive coal shippers from 'monopolistic' pricing practices." *Id.* at 524-25.

The SAC test simulates a market that is free from barriers to entry—a "contestable market." It seeks to "simulate the competitive price" if the market were contestable. *Major Issues in Rail Rate Case*s, STB Docket No. 657 (Sub-No. 1), at 7 (Oct. 30, 2006) ("*Major Issues*"). Put another way, the test attempts to identify the rate at which it would be worthwhile for a competitor railroad to enter the market.

In order to establish that a challenged rate is unreasonable under the SAC constraint, a shipper hypothecates a least-cost, optimally-efficient stand-alone railroad ("SARR") that is free of barriers to entry and that is capable of serving the issue traffic. The challenged rate "cannot be higher than what the SARR would need to charge to serve the complaining shipper while fully covering its costs, including a reasonable return." *Id.*, at 6.

SAC cases are, in a word, complex. SARR modeling entails, among other things, selection of a traffic group; determination of network configuration; estimation of the required investments in infrastructure; design of detailed operating and maintenance plans; estimation of operating expenses including maintenance of way; and allocation of revenue for traffic that connects to other carriers. To test SARR operations against the chosen traffic group, the parties rely on sophisticated computerized models. Calculated revenue requirements are compared to projected revenues, with adjustment for revenue based taxes. *Major Issues*, at 6-7.

Notably, SAC cases come with a substantial price tag—reportedly costing a shipper as much as $5 million to litigate. *Simplified Standards*, at 31. Not surprisingly, the expense and complexity of a full SAC test has been criticized as not providing a viable option for shippers to challenge rates involving small-sized shipments.

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[1]The other three decisions involved challenges brought by DuPont against CSX. *See E.I. DuPont de Nemours and Co. v. CSX, Trans. Inc.*, STB Docket Nos. 42099, 42100, and 42101 (served June 30, 2008).

RAIL RATES *continued from page 7*

Following the ICC's adoption of CMP, the ICC embarked on an unsuccessful and protracted quest for a methodology for use in rate cases where application of SAC was impracticable. In 1995, Congress terminated the ICC, established the STB in its place, and gave the new agency a year "to establish a simplified and expedited method for determining the reasonableness of challenged rail rates in those cases in which a full stand-alone cost presentation is too costly, given the value of the case." 49 U.S.C. § 10701(d) (3).

In response to the Congressional mandate, in 1996 the STB adopted the Three Benchmark ("3-B") methodology which is described below. *Rate Guidelines—Non-Coal Proceedings*, 1 S.T.B. 1004 (1996) ("*Simplified Guidelines*"). Few shippers sought relief, and no cases were decided, under the new 3-B methodology.

The *Simplified Guidelines* Achilles' heel appears to have been a lack of certainty as to the methodology that would be applied in a rate challenge. A shipper seeking to challenge a rate under the 3-B rules could find itself litigating under the SAC test. Additionally, the 3-B rules were criticized as too vague. The vagueness of the rules and the uncertainty as to which methodology would apply had a chilling effect on potential complainants leaving the simplified procedure unused for years. *Simplified Standards*, at 3.

In 2007, the STB revised the *Simplified Guidelines*, adopting a "three tiered" system for large, medium and small-sized shipment rate disputes:

- the SAC test for large cases (unlimited relief);
- a "Simplified SAC" test for medium-sized cases (relief limited to $5 million over five years, with a decision within 510 days from the date of the complaint); and
- the 3-B test for small cases (relief limited to $1 million over five years, with a decision within 240 days from the date of the complaint).

Id. at 34.

The limits on relief available in the small and medium-sized cases served two purposes. First, the limits addressed, to a degree, railroads' concerns that the *Simplified Guidelines* exposed a significant portion of their revenues to challenge under methodologies that were cruder and less accurate than the SAC test. Second, the limits allowed the STB to hand the shipper control of the methodology to be applied to its rate challenge. *Id.* at 27.

The STB based the limits on estimates of cost of litigation—$250,000 under the 3-B approach and $1 million under the Simplified SAC approach. *Id.* at 34, Table 4.

The Three-Benchmark Standard

As its name would suggest, the 3-B methodology determines the reasonableness of rates by comparing the R/VC of the challenged traffic to three benchmarks:

- the Revenue Shortfall Allocation Method (RSAM) benchmark—the amount that a carrier would need to charge its potentially captive traffic (traffic with R/VCs above 180%) in order to achieve revenue adequacy;
- the $R/VC_{>180}$ benchmark—the current markup over variable costs earned by the carrier on potentially captive traffic; and the
- the R/VC_{COMP} benchmark—the R/VCs of a comparison group of traffic with similar movement characteristics to the issue traffic.

Under the methodology, each R/VC of the comparison traffic group is adjusted by the ratio of the two other benchmarks, *i.e.*, the ratio of the RSAM to the $R/VC_{>180}$. The Board then calculates an upper boundary for reasonableness based on the mean (R/VC_{COMP}) and standard deviation of the adjusted comparison group. The Board also considers "other relevant factors." *US Magnesium* at 14-15.

The key issue in a 3-B case is the selection of the comparison traffic group. Under the *Simplified Guidelines*, each party proffers in baseball final-offer arbitration style a comparison traffic group (from the defendant's Waybill Sample[2]). The STB selects the comparison traffic group that it determines is most similar to the issue traffic.

Importantly, the selection is an "either/or" selection; the STB may not modify the traffic group. *Simplified Standards*, at 18. According to the STB, the procedure is intended "to create the proper incentives for litigants not to take extreme positions." *Id.*

Selection of the traffic group generally determines the outcome, as was the case in *US Magnesium*.

The US Magnesium Decision—Bad Facts Make Bad Law

The STB faced a dilemma in *US Magnesium*—a choice between what it described as two "imperfect" and "relatively extreme comparison groups." *US Magnesium*, at 9. Ideally, a traffic group would have been comprised of single-line chlorine movements. While Union Pacific's ("UP's") traffic group included chlorine-only movements with similar movement characteristics as the issue traffic, the majority of movements were "rebilled" (a rebilled movement moves on more

RAIL RATES *continued on page 11*

[2]A waybill contains information regarding the "characteristics of an individual rail shipment" including, *inter alia*, the commodity, the origin and destination, interchange points, participating carriers, freight revenue, and number of cars. Carriers are required to report waybill information in the Waybill Sample for a subset of the line-haul revenue waybills terminating on its lines. *See Waybill Data Reporting for Toxic Inhalation Hazards*, STB Ex Parte No. 385 (Sub-No. 7), at 1-2 (served Jan. 28, 2010).

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FEDERAL BAR ASSOCIATION APPLICATION FOR MEMBERSHIP (CONTINUES ON REVERSE)

Applicant Information

First Name | M.I. | Last Name | Suffix (e.g. Jr.) | Title (e.g. Attorney At Law, Partner, Assistant U.S. Attorney)

❍ Male ❍ Female Have you been an FBA member in the past? ❍ yes ❍ no Which do you prefer as your primary address? ❍ business ❍ home

Business

Firm/Company/Agency | Number of Attorneys

Address | Suite/Floor

City | State | Zip | Country

( ) | ( )

Phone | Fax | E-mail

Home

Address | Apt. #

City | State | Zip | Country

( ) | ( )

Phone | Fax

/ /

Date of Birth | E-mail

Bar Admission and Law School Information (required)

U.S.

Court of Record: _____

State/District: _____ Original Admission: / /

Tribal

Court of Record: _____

State: _____ Original Admission: / /

Foreign

Court/Tribunal of Record: _____

Country: _____ Original Admission: / /

Students

Law School: _____

State/District: _____ Expected Graduation: / /

Practice Information

PRACTICE TYPE

Private Sector: ❍ Private Practice ❍ Corporate/In-House

Public Sector: ❍ Government ❍ Association Counsel ❍ Nonprofit ❍ University/College ❍ Military ❍ Judiciary

PRIMARY PRACTICE AREAS

❍ Administrative
❍ Admiralty/Maritime
❍ ADR/Arbitration
❍ Antitrust/Trade
❍ Bankruptcy
❍ Communications
❍ Criminal
❍ Environment/Energy
❍ Federal Litigation
❍ Financial Institutions
❍ General Counsel
❍ Government Contracts
❍ Health
❍ Immigration
❍ Indian
❍ Intellectual Property
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- ❍ *Criminal Law* $10
- ❍ *Environment, Energy, and Natural Resources* $15
- ❍ *Federal Litigation* $10
- ❍ *Government Contracts* $20
- ❍ *Health Law* $10
- ❍ *Immigration Law* $10
- ❍ *Indian Law* $15
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- ❍ *International Law* $10
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- ❍ *Social Security* $10
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- ❍ *Taxation* $15
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- ❍ Montgomery
- ❍ North Alabama

Alaska
- ❍ Alaska

Arizona
- ❍ Phoenix
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Arkansas*
- ❍ At Large

California
- ❍ Central Coast
- ❍ Inland Empire
- ❍ Los Angeles
- ❍ Northern District of California
- ❍ Orange County
- ❍ Sacramento
- ❍ San Diego
- ❍ San Joaquin Valley

Colorado
- ❍ Colorado

Connecticut
- ❍ District of Connecticut

Delaware
- ❍ Delaware

District of Columbia
- ❍ Capitol Hill
- ❍ D.C.
- ❍ Pentagon

Florida
- ❍ Broward County
- ❍ Jacksonville
- ❍ North Central Florida
- ❍ Orlando
- ❍ Palm Beach County
- ❍ South Florida
- ❍ Southwest Florida
- ❍ Tallahassee –$25
- ❍ Tampa Bay

Georgia
- ❍ Atlanta–$10

Hawaii
- ❍ Hawaii

Idaho
- ❍ Idaho

Illinois
- ❍ Chicago

Indiana
- ❍ Indianapolis

Iowa
- ❍ Iowa–$10

Kansas
- ❍ At Large

Kentucky
- ❍ Kentucky

Louisiana
- ❍ Baton Rouge
- ❍ Lafayette/ Acadiana
- ❍ New Orleans
- ❍ North Louisiana

Maryland
- ❍ Maryland

Maine*
- ❍ At Large

Massachusetts
- ❍ Massachusetts –$10

Michigan
- ❍ Eastern District of Michigan
- ❍ Western District of Michigan

Minnesota
- ❍ Minnesota

Mississippi
- ❍ Mississippi

Missouri*
- ❍ At Large

Montana
- ❍ Montana

Nebraska*
- ❍ At Large

Nevada
- ❍ Nevada

New Hampshire*
- ❍ At Large

New Jersey
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- ❍ New Jersey

New Mexico*
- ❍ At Large

New York
- ❍ Eastern District of New York
- ❍ Southern District of New York

North Carolina
- ❍ Middle District of North Carolina
- ❍ Western District of North Carolina

North Dakota*
- ❍ At Large

Ohio
- ❍ John W. Peck/ Cincinnati/ Northern Kentucky
- ❍ Columbus
- ❍ Dayton
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Oklahoma
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- ❍ Northern/ Eastern Oklahoma

Oregon
- ❍ Oregon

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Rhode Island
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South Carolina
- ❍ South Carolina

South Dakota*
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Utah
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Vermont*
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- ❍ Tidewater

Virgin Islands
- ❍ Virgin Islands

Washington*
- ❍ At Large

West Virginia*
- ❍ At Large

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- ❍ At Large

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- ❍ Wyoming

Chapter Total: $ _____

Payment Information and Authorization Statement

TOTAL DUES TO BE CHARGED
(membership, section/division, and chapter dues): $ _____

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By signing this application, I hereby apply for membership in the Federal Bar Association and agree to conform to its Constitution and Bylaws and to the rules and regulations prescribed by its Board of Directors. I declare that the information contained herein is true and complete. I understand that any false statements made on this application will lead to rejection of my application and/or the immediate termination of my membership. I also understand that by providing my fax number and e-mail address, I hereby consent to receive faxes and e-mail messages sent by or on behalf of the Federal Bar Association, the Foundation of the Federal Bar Association, and the Federal Bar Building Corporation.

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RAIL RATES *continued from page 8*

than one railroad and each railroad issues a bill for its portion of the move). According to the STB, the R/VCs for the rebilled movements, were significantly higher than R/VCs for single line movements. *Id.*

By contrast, US Magnesium's ("USM's") comparison traffic group was comprised mostly of anhydrous ammonia movements, with only a small number of chlorine movements. While both anhydrous ammonia and chlorine are hazardous materials, the STB acknowledged that anhydrous ammonia and chlorine "do not share the same relative demand characteristics, and there is some evidence that they may have dissimilar transportation risks." *Id.* at 7.

Neither party sought to compromise its comparison traffic group prior to final submission.

In order to select the comparison traffic group, the STB performed a "quantitative analysis of the likely impact of these deficiencies." *Id.* The STB concluded that the weighted impact of the inclusion of rebilled chlorine movements in UP's traffic group was a 19% overstatement of the single-line chlorine movement R/VCs. By contrast, the weighted impact of the inclusion of non-chlorine traffic in USM's traffic group was a 16% to 17% understatement of single-line chlorine movement R/VCs. The STB acknowledged that this difference in "the weighted impact may not be statistically significant." *Id.* at 10. Nevertheless, based on this quantitative analysis and its findings that the USM traffic groups were stronger than UP's in terms of sample size and mileage, the STB concluded that "USM's comparison groups provide the best evidence." *Id.* at 11.

Significantly, due to a scarcity of comparable movements in UP's Waybill Sample, both parties submitted traffic groups comprised of contract-only movements. *Id.* at 18-19. UP argued for a "common carrier adjustment" in order to reflect the fact that "common carrier rates are, on average, higher than contract rates. *Id.* at 18. While noting that applying an adjustment "adds an unwanted layer of complexity to the 3-B process," the STB agreed that an adjustment was appropriate. The STB was concerned that prescribing a rate at contract levels would discourage carriers from entering into contracts "for fear those lower contract rates would be used in rate cases without adequate consideration" and would discourage shippers from negotiating for a contract rate in good faith. *Id.*

In his dissent, Commissioner Nottingham criticized the majority for selecting a traffic group that contained almost no chlorine movements, particularly given the fact that chlorine is "one of the most dangerous of all 'toxic inhalation commodities' (TIH) commodities." In his view, the majority failed to hold the shipper to its burden of proof. *Id.* at 24-25.

Further, he faulted the application of the 3-B methodology to TIH movements in general since the system that the Board used to calculate variable costs does not "attribute any unique cost characteristics to the transportation of TIH, including especially dangerous TIH such as chlorine." *Id.* at 22.

Commissioner Nottingham also criticized the parties for "testing the outer boundaries of what might qualify as an acceptable comparison group." *Id.* at 21. As a result, due to the "either/or" design of the comparison group selection, STB was "a prisoner of the parties' submissions." Notably, Commissioner Nottingham called for a procedural change in 3-B cases that would enable the STB to direct parties "to submit new traffic comparison groups that more closely resemble the traffic at issue [rather than] accept two intentionally distorted traffic groups." *Id.* at 22.

The Lessons and Potential Ramifications of US Magnesium

It appears that the Board has made progress toward meeting its goals of providing shippers with an accessible and affordable means of obtaining relief in small-sized cases. In terms of accessibility, the fact that the Board has now issued four decisions[3] awarding shippers relief speaks for itself.

Affordability is achieved in part by the expedited nature of the 3-B proceedings—just nine months from USM's filing of the complaint on May 4, 2009, to the Board's decision on January 27, 2009. The compressed schedule is an important factor in limiting litigation costs. Similarly, the focus on the comparison traffic group evidence drastically reduces the evidentiary burdens associated with a SAC presentation.

That said, *US Magnesium* is illustrative of the difficulties in simplifying a rate case. To begin with, the decision itself is 20 pages, required sophisticated quantitative analyses, and raised several difficult issues. The Board's openness to consider "other factors" such as the common carrier adjustment advocated by UP, while appropriate and necessary, underscores the potential expandable scope of 3-B cases.

Less clear is whether the STB succeeded in "ensuring that the new guidelines do not result in arbitrary ratemaking." In order to achieve this goal, the Board depends on the parties to provide a sound evidentiary basis for decision, *i.e.*, the comparison traffic group that the Board selects must be sufficiently similar to the issue traffic for the Board to judge the reasonableness of the challenged rate. If the Board is forced to choose between two comparison traffic groups, neither of which is all that similar to the issue movement, then the Board is simply awarding relief based on which litigant was less unreasonable, which has nothing to do with the core question of whether the challenged rate is unreasonable.

RAIL RATES *continued on page 12*

[3]In addition to *US Magnesium*, the Board issued three decisions in rate cases filed by DuPont against CSXT (*see supra* n. 1).

RAIL RATES *continued from page 11*

The *US Magnesium* parties' "extreme" positions with respect to their respective comparison traffic group proffers appear to have dented the Board's expectation that the final-offer, baseball arbitration style procedures would force parties to be reasonable, thereby providing the Board with a sound evidentiary basis for its decision. Neither party altered its final comparison traffic group from its opening proffer.

To some extent, the parties "extreme" positions appear to be attributable to the lack of chlorine movements in the Waybill Sample.[4] This highlights another problem with the application of the 3-B methodology to certain commodities or to movements with unique characteristics. In some instances, the defendant carrier's Waybill Sample simply may not contain a sufficient number of comparable movements for the Board to draw a fair conclusion concerning the reasonableness of a particular rate.

Paradoxically, the Board's decision to award relief under these circumstances might have the unintended consequence of encouraging similar behavior by future litigants. Indeed, it remains to be seen whether this decision will encourage parties to future rate cases to moderate their behavior or embolden parties to test further the boundaries of the 3-B process. If the latter, the STB may need to change its procedures in order to ensure that rate cases are decided based on sound evidence, and not based on aggressive litigation tactics. ❖

David F. Rifkind is a Partner with the Washington, D.C., office of Leonard Street and Dienard and focuses on regulatory and litigation in the transportation industries. He received a J.D. from Georgetown University and a B.A. from Emory University.

[4]In a separate regulatory proceeding, the STB is attempting to remedy the lack of TIH data in the Waybill Sample by requiring 100% reporting of TIH movements. *See Waybill Data*, Ex Parte No. 385 (Sub-No. 7).

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