

**BNSF Ry. Co. v. S.T.B.**, 748 F.3d 1295 (D.C. Cir. 2014) (holding: (1) hypothetical routes proffered by shippers challenging the reasonableness of market-dominant railroads' rates under the Stand-Alone-Cost-Test need not follow an existing, actual route—even in unitary joint rate cases; and (2) when one railroad moves a shipper's freight over lines leased from another railroad, the railroad that actually moved the shipper's freight must be inputted as the relevant railroad for purposes of the Uniform Rail Costing System).

Plaintiff Arizona Electric Power Cooperative, Inc., (“Arizona Electric”) supplies coal for its Arizona power plant from mines in New Mexico, Wyoming, and Montana. Defendant Burlington Northern Santa Fe Company (“BNSF”) first transports coal southward to either Deming, New Mexico, or Pueblo, Colorado (the “interchange locations”). BNSF contracts with Southwest Railroad to ship the coal partway to Deming. From the interchange locations, Defendant Union Pacific Railroad Company (“Union Pacific”) then ships the coal to its final destination in Arizona. BNSF and Union Pacific charged Arizona Electric joint rates for these routes, a common industry practice. Defendants are dominant railroads with little competition.

Arizona Electric challenged Defendants' joint rates in action before the Surface Transportation Board (the “STB”), arguing the joint rates were unreasonable. To demonstrate Defendants' joint rates were unreasonable, Arizona Electric proffered a hypothetical Stand-Alone Railroad that did not use Defendants' interchange locations. The STB concluded Defendants' joint rates were unreasonable, relying on Arizona Electric's hypothetical Stand-Alone Railroad, and capped Defendants' maximum chargeable rates at 180 percent of their actual variable costs.

All parties appealed. Defendants argued the STB erred because their prior rates were reasonable, based on their interchange locations. Arizona Electric contended the STB erred with respect to its remedy, that the prescribed rates were still too high. Overall, at issue were Defendants' routes, routes needing two or more railroads to ship goods to their final destination.

The D.C. Circuit reviewed the STB's statutory interpretations under the *Chevron* framework, and the STB's exercise of discretion under the arbitrary and capricious standard from the Administrative Procedures Act (“APA”). The *Chevron* framework provides that courts must uphold agencies' interpretations of law if they are statutorily mandated or if they are a reasonable interpretation of ambiguous statutory language.

The court first addressed Defendants' reasonableness argument. Defendants argued that Arizona Electric's hypothetical Stand-Alone Railroad should have used Defendants' actual interchange locations. If so,

Defendants alleged their rates were reasonable. Congress has charged the STB to assess whether rates are reasonable by considering statutory factors. Congress, however, expressly did not limit consideration only to those factors. To determine reasonableness, the STB uses a Stand-Alone-Cost test that employs an optimally efficient, hypothetical Stand-Alone Railroad to determine a maximum rate that would be charged in a competitive market.

Key in the court's reasoning was *Chevron* deference. Congress did not unambiguously provide a particular process the STB must use in determining reasonableness, particularly with respect to joint routes. STB precedent under the hypothetical Stand-Alone Railroad does not require the Stand-Alone Railroad to follow particular routes, or even an existing one. Legislative history surrounding Congressional enactment of the STB's mandate shows that reasonableness for joint rates should be the same as for all rates. As such, the STB's use and application of its hypothetical Stand-Alone Railroad was a reasonable interpretation of an ambiguous mandate. The STB expressed its reasons in using the Stand-Alone Railroad in joint route situations: for practical purposes when carriers offer a joint rate they are treated as a single entity. Hence, the STB's decision was neither arbitrary nor capricious under the APA. Therefore, the D.C. Circuit affirmed the STB's determination that Defendants' rates were unreasonable.

The D.C. Circuit then addressed Arizona Electric's argument that the STB's remedy was too low. Arizona Electric contended the STB erred in inputting Southwest Railroad's lease rates when determining Defendants' variable costs.

Again, the *Chevron* framework guided the court's reasoning. Here, Congress has expressly provided that the maximum rate the STB may set is 180 percent of the railroad's variable costs. The STB calculates variable costs using the Uniform Rail Costing System. The STB relied on the rule expressed in *Kansas City Power and Light Company v. Union Pacific Railroad Company*, S.T.B. Docket No. 42095 (May 19, 2008). There, the STB decided that when one railroad moves a shipper's freight over lines leased from another railroad, the lease rate from the railroad that actually moves the shipper's freight must be inputted into the Uniform Costing system, exactly what the STB did here. Arizona Electric failed to show the *Kansas City Power* rule was somehow unreasonable, contrary to statute, or unreasonably applied in this case. Therefore, the D.C. Circuit concluded the STB's calculation of Defendants' variable costs was reasonable and not arbitrary and capricious under the APA.

*Ian Griffin*