SURFACE TRANSPORTATION BOARD

Decision

STB Ex Parte No. 290 (Sub-No. 5) (2005-4)

QUARTERLY RAIL COST ADJUSTMENT FACTOR

Decided: September 15, 2005

In Railroad Cost Recovery Procedures, 1 I.C.C.2d 207 (1984), the Interstate Commerce Commission (ICC) outlined the procedures for calculating the all-inclusive index of railroad input prices and the method for computing the rail cost adjustment factor (RCAF). Under the procedures, the Association of American Railroads (AAR) is required to calculate the index on a quarterly basis and submit it on the fifth day of the last month of each calendar quarter. In Railroad Cost Recovery Procedures, 5 I.C.C.2d 434 (1989), aff'd sub nom. Edison Electric Institute, et al. v. ICC, 969 F.2d 1221 (D.C. Cir. 1992), the ICC adopted procedures that require the adjustment of the quarterly index for a measure of productivity.

The provisions of 49 U.S.C. 10708 direct the Surface Transportation Board (Board) to continue to publish both an unadjusted RCAF and a productivity-adjusted RCAF. In Productivity Adjustment-Implementation, Ex Parte No. 290 (Sub-No. 7) (STB served Oct. 3, 1996), the Board decided to publish a second productivity-adjusted RCAF called the RCAF-5. Consequently, three indices are now filed with the Board: the RCAF (Unadjusted), the RCAF (Adjusted), and the RCAF-5. The RCAF (Adjusted), which reflects national average productivity changes as originally developed and applied by the ICC, is currently based on a 5-year moving average. The RCAF-5 reflects national average productivity changes as if a 5-year moving average had been applied consistently from the productivity adjustment's inception in 1989.

The index of railroad input prices, RCAF (Unadjusted), RCAF (Adjusted), and RCAF-5 for the fourth quarter 2005 are shown in Table A of the Appendix to this decision. Table B shows the second quarter 2005 index and the RCAF calculated on both an actual and a forecasted basis. The difference between the actual calculation and the forecasted calculation is the forecast error adjustment.

The Board's rules mandate that the weights for each major cost component of the all-inclusive cost index, on which the RCAF is based, be updated annually in order to reflect the changing mix of index components. The procedure also requires the wages and supplement rates used in the labor index to be rebenchmarked in the fourth quarter of each year. See Railroad Cost Recovery Procedures, 364 I.C.C. 841 (1981). The weights used by the AAR are based on the distribution of railway expenses for the year 2004. Similarly, AAR has used wage and supplemental data for the year 2004 to calculate hourly labor rates that reflect the changing mix

of employees. We have reviewed the reweighting and rebenchmarking calculations performed by AAR, and we find that they comply with the prescribed method.

Both the RCAF (Adjusted) and the RCAF-5 are currently calculated using a moving 5-year average of productivity change for U.S. Class I railroads. An average productivity change rate of 1.029 (2.9% per year) for the period 1999-2003 is currently used for the RCAF (Adjusted). In accordance with Ex Parte No. 290 (Sub-No. 7), supra, the RCAF-5 will continue to use the 1998-2002 average productivity change rate of 1.022 (2.2%) until January 1, 2006.

We have examined AAR's calculations for compliance with our procedures and find that the fourth quarter 2005 RCAF (Unadjusted) is 1.185, an increase of 4.3% from the third quarter 2005 RCAF of 1.136. The RCAF (Adjusted) is 0.572, an increase of 3.6% from the third quarter 2005 RCAF (Adjusted) of 0.552. The RCAF-5 is 0.548, an increase of 3.8% from the third quarter 2005 RCAF-5 of 0.528.

This decision will not significantly affect the quality of the human environment or the conservation of energy resources.

Pursuant to 5 U.S.C. 605(b), we conclude that our action will not have a significant economic impact on a substantial number of small entities within the meaning of the Regulatory Flexibility Act.

AUTHORITY: 49 U.S.C. 10708.

It is ordered:

1. The Board has approved the fourth quarter 2005 Rail Cost Adjustment Factor (Unadjusted) of 1.185, RCAF (Adjusted) of 0.572, and RCAF-5 of 0.548.

2. Notice of this decision will be published in the Federal Register.

3. The effective date of this decision is October 1, 2005.

By the Board, Chairman Nober, Vice Chairman Buttrey, and Commissioner Mulvey.

Vernon A. Williams
Secretary

APPENDIX

TABLE A
Ex Parte No. 290 (Sub-No. 5) (2005-4)
All Inclusive Index of Railroad Input Costs
(Refer to Endnotes Page 5)

LINE NO.	INDEX COMPONENT	2004 WEIGHTS	THIRD QUARTER 2005 FORECAST	FOURTH QUARTER 2005 FORECAST
1	LABOR	36.0%	291.1	287.7
2	FUEL	12.1%	193.6	276.2
3	MATERIALS AND SUPPLIES	4.4%	179.8	179.9
4	EQUIPMENT RENTS	8.9%	182.8	181.4
5	DEPRECIATION	10.6%	180.3	185.1
6	INTEREST	3.0%	90.2	92.7
7	OTHER ITEMS [1]	25.0%	179.5	176.2
8	WEIGHTED AVERAGE	100.0%	219.1	227.5
9	LINKED INDEX [2]		217.0	225.3
10	PRELIMINARY RAIL COST ADJUSTMENT FACTOR [3]		113.0	117.3
11	FORECAST ERROR ADJUSTMENT [4]		0.006	0.012
12	RCAF (UNADJUSTED) (LINE 10 +LINE 11)		1.136	1.185
13	RCAF (ADJUSTED) [5]		0.552	0.572
14	RCAF-5 [6]		0.528	0.548

APPENDIX

TABLE B

Ex Parte No. 290 (Sub-No. 5) (2005-4)
Comparison of Second Quarter 2005 Index
Calculated on Both a Forecasted and an Actual Basis

Line No.	INDEX COMPONENT	2003 WEIGHT	SECOND QUARTER 2005 FORECAST	SECOND QUARTER 2005 ACTUAL
1	LABOR	37.5%	289.5	289.5
2	FUEL	10.6%	186.9	204.2
3	MATERIALS AND SUPPLIES	4.4%	176.4	176.4
4	EQUIPMENT RENTS	9.4%	182.4	181.6
5	DEPRECIATION	10.7%	176.3	175.9
6	INTEREST	3.2%	90.2	90.2
7	OTHER ITEMS	24.2%	178.9	176.3
8	WEIGHTED AVERAGE	100.0%	218.3	219.4
9	LINKED INDEX		214.9	217.2
10	RAIL COST ADJUSTMENT FACTOR		111.9	113.1

Endnotes:

[1] "Other Items" is a combination of Purchased Services, Casualties and Insurance, General and Administrative, Other Taxes, Loss and Damage, and Special Charges, price changes for all of which are measured by the Producer Price Index for Industrial Commodities Less Fuel and Related Products and Power.

[2] Linking is necessitated by a change to the 2004 weights beginning in the fourth quarter 2005. The following formula was used for the current quarter's index:

$$\frac{\text{4th Qr. 2005 Index (2004 Weights)}}{\text{3rd Qr. 2005 Index (2004 Weights)}} \quad \text{Times} \quad \text{4}^{\text{th}} \text{ Quarter Linked Index} \quad \text{Equals Linked Index}$$
$$(1980 = 100 \text{ Linked}) \quad (\text{Current Quarter})$$

Or

$$\frac{227.5}{219.1} \ \times \ 217.0 \ = \ 225.3$$

[3] The first quarter 1998 RCAF was rebased using the October 1, 2002, level of 192.1 in accordance with the requirements of the Staggers Rail Act of 1980 (10/1/2002 = 100).

[4] The fourth quarter 2005 forecast error adjustment was calculated as follows: a. second quarter 2005 RCAF using forecasted data equals 111.9; b. Second quarter 2005 RCAF using actual data equals 113.1; c. The difference equals the forecast error (b-a) of 1.2. Since the actual first quarter value is greater than the forecast value, the difference is added to the Preliminary RCAF.

[5] The fourth quarter 2005 RCAF Adjusted (0.572) is calculated by dividing the fourth quarter RCAF Unadjusted (1.185) by the fourth quarter productivity adjustment factor of 2.0715. The fourth quarter 2005 productivity adjustment factor is calculated by multiplying the third quarter 2005 productivity adjustment of 2.0567 by the fourth root (1.0072) of the 1999-2003 annual average productivity growth rate of 2.9%.

[6] The fourth quarter 2005 RCAF-5 (0.548) is calculated by dividing the fourth quarter 2005 RCAF Unadjusted (1.185) by the fourth quarter productivity adjustment factor-5 (PAF-5) of 2.1616. The fourth quarter 2005 productivity adjustment factor is calculated by multiplying the third quarter 2005 PAF-5 of 2.1498 by the fourth root (1.0055) of the1998-2002 annual average productivity growth rate of 2.2%.