

SURFACE TRANSPORTATION BOARD

DECISION

Docket No. EP 290 (Sub-No. 5) (2011-4)

QUARTERLY RAIL COST ADJUSTMENT FACTOR

Digest:¹ The Rail Cost Adjustment Factor (RCAF) is an index formulated to represent changes in railroad costs incurred by the nation's largest railroads over a specified period of time. The statute requires the Surface Transportation Board to publish the RCAF on at least a quarterly basis. Each quarter, the Association of American Railroads computes three types of RCAF figures and submits those figures to the Board for approval. The Board has reviewed the submission and adopts the RCAF figures for the fourth quarter of 2011.

Decided: September 20, 2011

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—Productivity Adjustment, 5 I.C.C. 2d 434 (1989), aff'd sub nom. Edison Electric Institute 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, 1 S.T.B. 739 (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 (Unadjusted) is an index reflecting cost changes experienced by the railroad industry, without reference to changes in rail productivity. The RCAF (Adjusted) is an index that reflects national average productivity changes as originally developed and applied by the ICC; the calculation of those productivity changes is currently based on a 5-year moving average. And the RCAF-5 is an index that also reflects national average productivity changes, however, those

¹ The digest constitutes no part of the decision of the Board but has been prepared for the convenience of the reader. It may not be cited to or relied upon as precedent. Policy Statement on Plain Language Digests in Decisions, EP 696 (STB served Sept. 2, 2010).

productivity changes are calculated 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 2011 are shown in Table A of the Appendix to this decision. Table B shows the second quarter 2011 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 weights for each major cost component of the all-inclusive cost index, on which the RCAF is based, are updated annually in order to reflect the changing mix of index components. See 49 U.S.C. § 10708. This includes rebenchmarking the wages and supplemental rates used in the labor index in the fourth quarter of each year. The weights used by AAR are based on the distribution of railway expenses for the year 2010. Similarly, AAR has used wage and supplemental rates for the year 2010 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.

In its submission, AAR states that it received a correction to the price for one item used for the third quarter 2011 RCAF. According to AAR, this price change caused the original Materials and Supplies (M&S) index of 257.8 (which was rounded down from 257.83) to change slightly, resulting in a corrected M&S index of 257.9 (the actual figure is 257.85, but it is rounded to the nearest tenth place). AAR proposes that the Board use the first quarter 2012 forecast error calculation to account for any differences caused by this revision.

In the past, the Board used the forecast error adjustment procedure to remedy a similar error, and we continue to believe it is the best available method to correct the M&S index. See Quarterly Rail Cost Adjustment Factor, EP 290 (Sub-No. 5) (2001-1), slip op. at 2 (STB served Dec. 20, 2000) (noting that the forecast error adjustment was the best available method to correct an earlier overstated RCAF calculation and not restating that earlier overstated RCAF). Therefore, we will not restate the third quarter 2011 RCAF figures, but will allow the correction to be made using the first quarter 2012 forecast error calculation. As a result, the first quarter 2012 forecast error calculation will include the forecast version of the third quarter 2011 M&S index of the original 257.8, and the actual version of the M&S index of the corrected 257.9 index. In the current fourth quarter 2011 RCAF calculations, the M&S index has been calculated as if the third quarter 2011 version had used the corrected price.

We have examined AAR's calculations and we find that AAR has complied with our procedures. We find that the fourth quarter 2011 RCAF (Unadjusted) is 1.208, an increase of 0.2% from the third quarter 2011 RCAF of 1.206.² The RCAF (Adjusted) is calculated, in part, using the RCAF (Unadjusted) and a 5-year moving geometric average of productivity change for U.S. Class I railroads from 2005-2009, which is 1.014 (1.4% per year). We find the RCAF

² The percent changes for the fourth quarter 2011 RCAF (Unadjusted), RCAF (Adjusted), and the RCAF-5 are all based on the original third quarter 2011 decision.

(Adjusted) is 0.533, a decrease of 0.2% from the previously reported third quarter 2011 RCAF (Adjusted) of 0.534.³

In accordance with Productivity Adjustment—Implementation, 1 S.T.B. at 748-49, the RCAF-5 for this quarter will use a productivity trend for the years 2004-2008, which is 1.012 (1.2% per year). We find the RCAF-5 for the fourth quarter of 2011 is 0.506, no increase or decrease from the previously reported third quarter 2011 RCAF-5 of 0.506.⁴

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

Authority: 49 U.S.C. § 10708.

It is ordered:

1. The Board has approved the fourth quarter 2011 RCAF (Unadjusted) of 1.208, RCAF (Adjusted) of 0.533, and RCAF-5 of 0.506.
2. Notice of this decision will be published in the Federal Register.
3. The effective date of this decision is October 1, 2011.

By the Board, Chairman Elliott, Vice Chairman Begeman, and Commissioner Mulvey.

³ The fourth quarter 2011 RCAF Adjusted (0.533) is calculated by dividing the fourth quarter 2011 RCAF Unadjusted (1.208) by the fourth quarter productivity adjustment factor of 2.2645. The fourth quarter 2011 productivity adjustment factor is calculated by multiplying the third quarter 2011 productivity adjustment of 2.2566 by the fourth root (1.0035) of the 2005-2009 annual average productivity growth rate of 1.4%.

⁴ The fourth quarter 2011 RCAF-5 (0.506) is calculated by dividing the fourth quarter 2011 RCAF Unadjusted (1.208) by the fourth quarter productivity adjustment factor-5 (PAF-5) of 2.3894. The fourth quarter 2011 PAF-5 is calculated by multiplying the third quarter 2011 PAF-5 of 2.3823 by the fourth root (1.0030) of the 2004-2008 annual average productivity growth rate of 1.2%.

APPENDIX**TABLE A**

EP 290 (Sub-No. 5) (2011-4)
All Inclusive Index of Railroad Input Costs
 (Endnotes Following Table B)

LINE NO.	INDEX COMPONENT	2010 WEIGHTS	THIRD QUARTER 2011 FORECAST	FOURTH QUARTER 2011 FORECAST
1	LABOR	33.3%	382.1	375.3
2	FUEL	18.0%	392.3	396.9
3	MATERIALS AND SUPPLIES ¹	5.0%	257.9	265.7
4	EQUIPMENT RENTS	6.2%	208.8	205.9
5	DEPRECIATION	12.8%	206.1	208.4
6	INTEREST	2.9%	84.5	90.6
7	OTHER ITEMS ²	21.8%	222.3	220.3
8	WEIGHTED AVERAGE	100.0%	301.0	299.8
9	LINKED INDEX ³		291.8	290.6
10	PRELIMINARY RAIL COST ADJUSTMENT FACTOR ⁴		118.7	118.2
11	FORECAST ERROR ADJUSTMENT ⁵		0.020	0.026
12	RCAF (UNADJUSTED) (LINE 10 + LINE 11)		1.207	1.208
13	RCAF (ADJUSTED)		0.535	0.533
14	RCAF-5		0.507	0.506

TABLE B

EP 290 (Sub-No. 5) (2011-4)
Comparison of Second Quarter 2011 Index
Calculated on Both a Forecasted and an Actual Basis

Line No.	INDEX COMPONENT	2009 WEIGHT	SECOND QUARTER 2011 FORECAST	SECOND QUARTER 2011 ACTUAL
1	LABOR	34.7%	379.6	379.6
2	FUEL	14.9%	368.4	408.3
3	MATERIALS AND SUPPLIES	5.1%	249.0	249.0
4	EQUIPMENT RENTS	7.1%	203.1	205.7
5	DEPRECIATION	13.9%	204.6	205.8
6	INTEREST	3.0%	84.5	84.5
7	OTHER ITEMS	21.3%	212.9	216.6
8	WEIGHTED AVERAGE	100.0%	290.1	297.1
9	LINKED INDEX		284.4	291.0
10	RAIL COST ADJUSTMENT FACTOR		115.7	118.3

Endnotes:

¹ For calculation purposes, the third quarter 2011 forecast includes a revision made to the M&S index. This revision caused the M&S index and all weighted averages to increase by 0.1 index points.

² “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.

³ Linking is necessitated by a change to the 2010 weights beginning in the fourth quarter 2011. The following formula was used for the current quarter’s index:

$$\begin{array}{rcl}
 \frac{\text{4th Qr. 2011 Index}}{\text{(2010 Weights)}} & \text{Times 3rd Quarter Linked Index} & \text{Equals Linked Index} \\
 \text{3rd Qr. 2011 Index} & \text{(1980 = 100 Linked)} & \text{(Current Quarter)} \\
 \text{(2009 Weights)} & & \\
 & \text{Or} & \\
 \frac{299.8}{301.0} \times 291.8 & = & 290.6
 \end{array}$$

⁴ The first quarter 2008 RCAF was rebased using the October 1, 2007 level of 245.9 in accordance with the requirements of the Staggers Rail Act of 1980 (10/1/2007 = 100).

⁵ The fourth quarter 2011 forecast error adjustment was calculated as follows: (a) second quarter 2011 RCAF using forecasted data equals 115.7; (b) second quarter 2011 RCAF using actual data equals 118.3; and (c) the difference equals the forecast error (b-a) of 2.6. Because the actual second quarter value is greater than the forecast value, the difference is added to the Preliminary RCAF.