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November 8, 2012

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VIA HAND DELIVERY

Ms. Cynthia Brown
Chief, Section of Administration
Office of Proceedings
Surface Transportation Board
395 E Street, S.W.
Washington, DC 20423-0111

Re: STB Finance Docket No. 35506, *Western Coal Traffic League – Petition for Declaratory Order*

Dear Ms. Brown:

Enclosed for filing in the above-referenced proceeding, please find an original and ten (10) copies of the Joint Comments of the Western Coal Traffic League, American Public Power Association, Edison Electric Institute, National Association of Regulatory Utility Commissioners, National Rural Electric Cooperative Association, Western Fuels Association, Inc., and Basin Electric Power Cooperative, Inc. This filing includes three copies of a CD containing the text of the Joint Comments and the electronic workpapers in support of the Verified Statement of Messrs. Crowley and Fapp, which workpapers have been marked **Highly Confidential**.

Please date stamp the extra copy of this cover letter and the enclosed duplicate filing and return it to our messenger. Thank you for your attention to this matter.

Respectfully submitted,

Daniel M. Jaffe
An Attorney for the Listed Parties

Enclosures

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**BEFORE THE
SURFACE TRANSPORTATION BOARD**

WESTERN COAL TRAFFIC LEAGUE – PETITION FOR DECLARATORY ORDER	)))))	Finance Docket No. 35506

233320

JOINT COMMENTS OF THE WESTERN COAL TRAFFIC LEAGUE AMERICAN PUBLIC POWER ASSOCIATION EDISON ELECTRIC INSTITUTE NATIONAL ASSOCIATION OF REGULATORY UTILITY COMMISSIONERS NATIONAL RURAL ELECTRIC COOPERATIVE ASSOCIATION WESTERN FUELS ASSOCIATION, INC., AND BASIN ELECTRIC POWER COOPERATIVE, INC.

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Dated: November 8, 2012

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BEFORE THE
SURFACE TRANSPORTATION BOARD

WESTERN COAL TRAFFIC LEAGUE – PETITION FOR DECLARATORY ORDER	)))))	Finance Docket No. 35506

JOINT COMMENTS OF THE WESTERN COAL TRAFFIC LEAGUE, AMERICAN PUBLIC POWER ASSOCIATION, EDISON ELECTRIC INSTITUTE, NATIONAL ASSOCIATION OF REGULATORY UTILITY COMMISSIONERS, NATIONAL RURAL ELECTRIC COOPERATIVE ASSOCIATION, WESTERN FUELS ASSOCIATION, INC., AND BASIN ELECTRIC POWER COOPERATIVE, INC.

The Western Coal Traffic League, American Public Power Association, Edison Electric Institute, National Association of Regulatory Utility Commissioners ("NARUC"), National Rural Electric Cooperative Association, Western Fuels Association, Inc. ("WFA"), and Basin Electric Power Cooperative, Inc. ("Basin Electric") (collectively "Coal Shippers/NARUC") present these Joint Comments in response to the Surface Transportation Board's ("STB" or "Board") notice of request for comments ("Notice") served in this proceeding on October 9, 2012.

PREFACE AND SUMMARY

In February 2010, Berkshire Hathaway, Inc. ("Berkshire") acquired BNSF Railway Company ("BNSF"). At that time Berkshire paid an acquisition premium which, for regulatory purposes, equals $8.1 billion. Coal Shippers/NARUC have demonstrated in their prior submissions in this case that the $8.1 billion premium must be excluded from BNSF's Uniform Railroad Costing System ("URCS") and revenue adequacy net investment bases starting in calendar year 2010 and continuing in all future years.

In September 2012, Berkshire informed the Board that it had obtained control of BNSF unlawfully. Berkshire explained its acquisition was unlawful because, at the time it acquired BNSF in February 2010, it controlled two common carriers, and, under the requirements of 49 U.S.C. § 11323, it should have – but did not – obtain prior Board approval for its acquisition of BNSF. Berkshire also informed the Board that its unlawful control continued in 2011 and 2012 and that it planned to remedy its non-compliance with § 11323 by divesting itself of its two non-BNSF common carrier railroad subsidiaries. In response, the Board has ordered BNSF to divest itself of these two common carrier subsidiaries by December 31, 2012. The Board has also reopened this proceeding to obtain comments on how Berkshire's non-compliance with § 11323 impacts the issues raised in this case.

Berkshire has been in non-compliance with § 11323 since February 2010 – when it unlawfully obtained BNSF – and will continue to be in non-compliance until it properly disposes of its two non-BNSF common carrier subsidiaries. Berkshire has benefitted from its non-compliance in two ways that are germane to the issues raised in this case: (1) the Board has included the premium in BNSF's URCS and revenue adequacy net investment bases, pending the outcome of this proceeding; and (2) BNSF has been removed from the composite group the Board uses to calculate the cost-of-capital return factor the Board applies to BNSF's URCS and BNSF's revenue adequacy net investment bases.

The Board has broad equitable powers to enforce § 11323 to ensure that an entity does not retain benefits from unlawful control of a railroad. The Board should first exercise these broad powers by removing the acquisition premium from BNSF's URCS and revenue adequacy net investment bases during the unlawful control years. The unlawful control began in 2010 and will continue until Berkshire properly divests the two non-BNSF common carrier subsidiaries.

This § 11323-based relief supplements Coal Shippers/NARUC's prior demonstration that the Board must remove the premium from both investment bases in all years starting with calendar year 2010. Coal Shippers/NARUC emphasize that the overall relief they have sought, and continue to seek, in this proceeding is the removal of the $8.1 billion premium from BNSF's URCS and revenue adequacy net investment bases for all years starting in calendar year 2010 (not just the unlawful control years).

The Board should also exercise its broad equitable powers to enforce § 11323 by applying BNSF's 2009 regulatory cost of capital – 10.01% – in developing BNSF's return on net investment ("ROI") for URCS and revenue adequacy purposes in each of the unlawful control years. Use of the 2009 calculation ensures that BNSF does not benefit from its exclusion from the industry cost of capital computation starting in 2010 (which occurred solely because of Berkshire's unlawful acquisition of BNSF), avoids complications associated with attempting to calculate a BNSF cost of equity in years after 2009 (the last year BNSF's equity was publicly traded), and has no adverse impacts on any other carrier.

Finally, the Board should exercise its authority under § 11323 to find that BNSF is revenue adequate in 2010 and 2011 (and may be revenue adequate in future unlawful control years) because BNSF's ROI (excluding the premium and applying a 10.01% return factor) exceeds 10.01%.

Coal Shippers present the joint verified statement of Thomas D. Crowley, President of L.E. Peabody & Associates, Inc. and Daniel L. Fapp, Vice-President of L.E. Peabody & Associates, Inc. ("Crowley/Fapp V.S.") in support of these Comments.

BACKGROUND

49 U.S.C. § 11323(a)(5) provides that transactions involving "[a]cquisition of control of a rail carrier by a person that is not a rail carrier but that controls any number of rail carriers" can "be carried out only with the approval and authorization of the Board." *Id.* A non-carrier that controls a rail carrier must submit an application to the Board and obtain Board "approv[al] and authoriz[ation]" *before* it acquires another rail carrier.[1]

Berkshire was aware of the § 11323 prior-approval requirements when it acquired BNSF in February 2010. However, Berkshire publicly represented that its acquisition of BNSF was not subject to the Board's prior approval under § 11323 because

[1] *See* 49 U.S.C. § 11324(a).

Berkshire, a non-carrier, did "not control any other railroads" prior to its acquisition of BNSF.[2]

On September 13, 2012, Berkshire informed the Board in a letter that it had "recently become aware" that Berkshire did "own or control . . . two rail common carriers" prior to Berkshire's acquisition of BNSF and, "as a result Berkshire's purchase of BNSF would have been subject to STB jurisdiction pursuant to § 11323(a)(5)."[3] Berkshire also informed the Board that it intended to comply with the requirements of § 11323 "by divestiture of both entities, or by other appropriate means."[4]

On September 18, 2012, the Board acknowledged "Berkshire['s] fail[ure] to comply with the requirements of 49 U.S.C. § 11323" and "directed [Berkshire] to submit within 10 days a letter specifying the method and timing by which it proposes to remedy its failure to comply with §11323."[5] The Board also stated that upon receipt of BNSF's letter it would "consider whether further action is warranted."[6]

On September 25, 2012, Berkshire sent a letter to the Board stating that it intended to comply with § 11323 by divesting the two non-BNSF common carrier

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[2] Berkshire Hathaway Acquisition of BNSF, Frequently Asked Questions at 1 (dated Nov. 3, 2009), http://www.sec.gov/Archives/edgar/data/934612/000095015709000814/form425.htm.

[3] Letter from Roger Nober, Executive Vice President, Law & Secretary of BNSF to the Honorable Daniel R. Elliott, III, Chairman, STB (Sept. 13, 2012) at 1.

[4] *Id.* at 2.

[5] Letter from Lucille L. Marvin, Director, STB Office of Public Assistance, Governmental Affairs, and Compliance to Roger Nober (Sept. 18, 2012) at 1.

[6] *Id.*

railroads "no later than December 31, 2012."[7] On October 9, the Board informed Berkshire that the proposed divestitures "must close no later than December 31, 2012" and that "the STB intends to solicit public input regarding the effect, if any, of Berkshire's non-compliance on the post-February 2010 valuation of BNSF's asset base."[8]

The Board issued its Notice seeking comments in this proceeding on October 9, 2012. In its Notice, the Board states that "Berkshire's 2010 acquisition of BNSF was and remains subject to the Board's jurisdiction pursuant to § 11323"; that "Berkshire will not come into compliance until December 31, 2012 (by its estimates)"; and that the Board "seeks comments from the public on the effect, if any, of Berkshire's non-compliance with § 11323 upon this proceeding."[9]

ARGUMENT

Berkshire acquired, and continues to maintain, unlawful control of BNSF. Under governing law, Berkshire cannot "retain the fruits of its unlawful conduct,"[10] nor can the Board "sit idly by and wink at practices that lead to violations of [statutory] provisions."[11]

The principal "fruits" of Berkshire's unlawful conduct in the context of this case are: (1) the Board's proposed write-up of BNSF's URCS and revenue adequacy net

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[7] Letter from Roger Nober to Chairman Elliott (Sept. 25, 2012) at 2.

[8] Letter from Lucille L. Martin to Roger Nober (Oct. 9, 2012) at 1.

[9] Notice at 3.

[10] *Cent. of Ga. Ry. Control*, 307 I.C.C. 39, 43 (1958) ("*Central of Georgia Ry.*").

[11] *Am. Trucking Assn's, Inc. v. United States*, 344 U.S. 298, 311 (1953) ("*Am. Trucking*"); *Zola v. ICC*, 889 F.2d 508, 516 (3d Cir. 1989) ("*Zola*").

investment bases by the $8.1 billion regulatory acquisition premium Berkshire paid in February 2010 to acquire BNSF; and (2) the Board's exclusion of BNSF from the industry cost of capital computations the Board applies in developing BNSF's URCS and revenue adequacy ROI.

The Board cannot "sit idly by and wink at" Berkshire's unlawful actions. Coal Shippers/NARUC have already demonstrated in their prior submissions in this case that the Board should exclude the $8.1 billion premium from BNSF's net investment base for all years starting in 2010. Berkshire's unlawful conduct provides additional grounds for excluding the premium starting in the unlawful control years.

Coal Shippers/NARUC also request that the Board address the cost-of-capital issue by utilizing the last available BNSF regulatory cost of capital – BNSF's 2009 cost of capital – in making BNSF's URCS and revenue adequacy computations starting in calendar year 2010 and continuing until Berkshire complies with the law.

Finally, Coal Shippers/NARUC demonstrate that with the use of a proper calculation of BNSF's net investment base (excluding the premium), along with the use of a fair calculation of BNSF's cost of capital (10.01%), BNSF was revenue adequate in calendar years 2010 and 2011.

I.

THE BOARD HAS BROAD EQUITABLE POWERS TO PREVENT BERKSHIRE FROM RETAINING THE FRUITS OF ITS UNLAWFUL CONTROL OF BNSF DURING THE UNLAWFUL CONTROL YEARS (2010 TO DATE)

The Board has ordered Berkshire to properly divest its two non-BNSF common carrier subsidiaries by December 31, 2012. Assuming Berkshire does so, it will no longer be in unlawful control of two or more common carriers. Thus, the Board's order is designed to stop Berkshire's unlawful activities, but the order does not address, or provide a remedy for, Berkshire's unlawful control of BNSF between the date when the unlawful control started (February 12, 2010)[12] and the date when the unlawful control ends (projected to be December 31, 2012).

The Board has broad "equitable powers to expunge" a violation of § 11323.[13] These equitable powers include the authority to prevent an entity that obtains unlawful control of a carrier from "retain[ing] the fruits of its unlawful conduct."[14] The Board cannot "sit idly by and wink at practices that lead to violations of [statutory] provisions."[15]

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[12] *See* Notice at 1 n.1 ("[o]n February 12, 2010, Berkshire purchased the common stock of BNSF's parent company that Berkshire did not already own").

[13] *See Gilbertville Trucking Co. v. United States*, 371 U.S. 115, 130 (1962) ("*Gilbertville Trucking*").

[14] *Central of Georgia Ry.*, 307 I.C.C. at 43.

[15] *Am. Trucking*, 344 U.S. at 309; *Zola*, 889 F.2d at 516.

The Board's equitable powers mirror those possessed by courts when setting relief orders in antitrust cases.[16] The touchstone for equitable relief in antitrust cases is that "[t]hose who violate the [antitrust laws] may not reap the benefits of their violations."[17] This equitable relief includes disgorgement of ill-gotten gains obtained through unlawful means.[18]

While the Board has "drastic" remedial powers, these powers are not boundless.[19] The Board's authority is "corrective, not punitive"; its duty is to give "complete and efficacious effect to the prohibition of the statute with as little injury as possible to the interests of private parties or the general public"; and it must "tailor the remedy to the particular facts of each case."[20]

The § 11323 relief that Coal Shippers/NARUC request complies with these governing legal standards. It will prevent Berkshire from "retain[ing] the fruits of its

[16] *Gilbertville Trucking*, 371 U.S. at 130 ("[t]he use of equitable powers to expunge a statutory violation has been fully developed in the context of the antitrust laws").

[17] *United States v. E.I. du Pont de Nemours & Co.*, 366 U.S. 316, 326-27 (1961).

[18] *See United States v. Keyspan Corp.*, 763 F. Supp. 2d 633, 640 (S.D.N.Y. 2011) ("disgorgement comports with established principles of antitrust law"); Phillip E. Areeda et al., *Antitrust Law* ¶ 325a (3d ed. 2007) ("[E]quity relief may include, where appropriate, the disgorgement of improperly obtained gains.").

[19] *M. Bulifant Trucking, Inc. – Investigation & Revocation of Certificates*, ICC No. MC-C-30160, 1989 WL 247027 at *7 (ICC decided Dec. 15, 1989) (citing *Gilbertville Trucking*, 371 U.S. at 130). *Accord Ill. Cent. R.R. v. United States*, 263 F. Supp. 421, 428 (N.D. Ill. 1966) (Board's power "to respond to conditions of illegal control is practically plenary under the Interstate Commerce Act").

[20] *Gilbertville Trucking*, 371 U.S. at 130.

unlawful conduct";[21] it is "corrective, not punitive"; it is "tailor[ed]" to the facts of this case; and it will advance the "interests of private parties or the general public."[22]

II.

THE BOARD SHOULD EXERCISE THESE BROAD EQUITABLE POWERS IN THIS CASE TO PROTECT THE PUBLIC INTEREST

The Board should exercise its broad authority to enforce § 11323 in this case in a manner that protects and advances the public interest.

A. Berkshire's Unlawful Acquisition of BNSF Provides the Board with an Additional Ground to Exclude the $8.1 Billion Acquisition Premium from BNSF's Net Investment Bases in the Unlawful Control Years

Coal Shippers/NARUC demonstrated in their prior submissions in this case that the Board should exclude the $8.1 billion regulatory premium Berkshire paid to acquire BNSF from the BNSF's URCS and revenue adequacy net investment bases in all years starting in 2010 because:

- It is fundamentally unfair for shippers' regulated rates to increase simply because Berkshire decided to pay a huge premium to acquire BNSF;[23]

[21] *Central of Georgia Ry.*, 307 I.C.C. at 43.

[22] *Gilbertville Trucking*, 371 U.S. at 130.

[23] *See* Coal Shippers/NARUC Joint Opening Evidence and Argument ("Coal Shippers/NARUC Op.") at 24-25, 31-33, 43-46; Coal Shippers/NARUC Joint Reply Evidence and Argument ("Coal Shippers/NARUC Reply") at 16-34; Coal Shippers/NARUC Joint Rebuttal Evidence and Argument ("Coal Shippers/NARUC Rebuttal") at 5-16, 27-29.

- Berkshire's acquisition of BNSF offered no public benefits to offset the massive premium;[24]

- No other regulator in America would permit a pass-through of an acquisition premium under these circumstances; and[25]

- The Board has never approved a regulated merger or acquisition that was premised on increased regulatory costs, and increased captive shipper rates.[26]

Coal Shippers/NARUC will not repeat their supporting evidence and argument here. The Board has a full record on these issues, that record closed in December 2011, and the Board heard oral arguments in March 2012. Instead, as directed by the Board, Coal Shippers/NARUC's comments are directed at "the effect . . . of Berkshire's non-compliance with § 11323 upon this proceeding." Notice at 3.

Berkshire was legally required to comply with § 11323 before it acquired BNSF in 2010. At that time, Berkshire should have either divested itself of its two common carrier subsidiaries before acquiring BNSF or sought regulatory approval for its acquisition of BNSF. Since Berkshire did neither, it should not have acquired BNSF in 2010. Nor should it have acquired BNSF at any later date unless and until it undertook one of these two actions.

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[24] *See* Coal Shippers/NARUC Op. at 25-27; Coal Shippers/NARUC Reply at 11-16; Coal Shippers/NARUC Rebuttal at 3, 21-22.

[25] *See* Coal Shippers/NARUC Op. at 28-31; Coal Shippers/NARUC Rebuttal at 16-20.

[26] *See* Coal Shippers/NARUC Op. at 33-36; Coal Shippers/NARUC Reply at 36-38; Coal Shippers/NARUC Rebuttal at 20-22.

The impact of Berkshire's non-compliance is self-evident. Berkshire should not have paid the $8.1 billion premium in 2010 because Berkshire should not have acquired BNSF at that time. The earliest the premium should have been paid is the date that Berkshire could lawfully acquire BNSF under § 11323. That date remains a future date but, at this point, is tied to BNSF's proper divestiture of its two non-BNSF common carrier railroad subsidiaries.

Berkshire did not lawfully acquire BNSF in 2010, 2011, or in 2012 (to date). The Board should not permit BNSF to "retain the fruits" of its failure to comply with the law.[27] The first remedial action the Board should take to enforce § 11323 in this case is to remove the premium from BNSF's URCS and revenue adequacy net investment bases in all years where Berkshire retains unlawful control of BNSF. As Coal Shippers/NARUC have previously demonstrated, inclusion of the premium unfairly increases BNSF's maximum rates under governing Board standards by unfairly inflating BNSF's URCS net investment base by the $8.1 billion premium.[28]

B. The Board Should Apply a Corrective BNSF Cost of Capital in the Unlawful Control Years

For purposes of developing URCS variable investment costs, and for purposes of determining carrier revenue adequacy, each year the Board develops an

[27] *Central of Georgia Ry.*, 307 I.C.C. at 43.

[28] *See* Coal Shippers/NARUC Op. at 14-19; Coal Shippers/NARUC Reply at 16-32; Coal Shippers/NARUC Rebuttal at 5-13.

industry-average current cost of capital.[29] Generally speaking, the formula the Board applies to develop capital return for URCS and revenue adequacy purposes is: the dollar value of the carrier's net investment base in year "X" multiplied by the STB's calculation of the current industry cost of capital for year "X." *See* Crowley/Fapp V.S. at 10 n.20, 15 n.27.[30]

Berkshire's unlawful acquisition of BNSF affects not only the net investment piece of the return equation, but also affects the cost of capital return component as well. Prior to 2010, the industry average cost of capital was calculated using a "composite group" consisting of BNSF's holding company and three railroad holding companies: CSX Corporation, Norfolk Southern Corporation, and Union Pacific Corporation.[31]

However, starting in 2010, the Board has excluded BNSF from the composite group because BNSF no longer meets two of the Board's criteria for inclusion: BNSF did not represent at least 50% of Berkshire's assets and Berkshire did not pay

[29] *See, e.g., R.R. Cost of Capital – 2011*, Docket No. EP 558 (Sub-No. 15) (STB served Sept. 13, 2012) at 1 ("*2011 Cost of Capital*") ("One of the Board's regulatory responsibilities is to determine annually the railroad industry's cost of capital."); *R.R. Cost of Capital – 2010*, Docket No. EP 558 (Sub-No. 14) (STB served Oct. 3, 2011) at 1 ("*2010 Cost of Capital*") (same); *R.R. Cost of Capital – 2009*, Docket No. EP 558 (Sub-No. 13) (STB served Oct. 29, 2010) at 1 ("*2009 Cost of Capital*") (same).

[30] For ease of reference, all cost of capital figures are stated on an after-tax basis. The Board uses pre-tax cost of capital computations in developing URCS variable costs. *See* Crowley/Fapp V.S. at 10 n.20. Also, there is a significant lag in the development of cost calculations using URCS. For example, the Board's BNSF 2010 URCS – which contains both the premium (subject to exclusion in this proceeding) and the 2010 cost of capital – was not released until December 2011. *See* Crowley/Fapp V.S. at 12.

[31] *See, e.g., 2009 Cost of Capital* at 16-19.

dividends on either its Class A or Class B common equity.[32] Had Berkshire complied with § 11323, it would not have acquired BNSF in 2010, 2011 or 2012 (to date). It also would have not been, or should not be, excluded from the Board's composite group cost of capital calculations in each of these three years.

The Board should remedy BNSF's exclusion from the composite group – an exclusion caused solely by Berkshire's unlawful acquisition of BNSF in 2010 – by using BNSF's 2009 regulatory cost of capital in developing BNSF's URCS variable investment costs, and in determining BNSF's revenue adequacy calculations, in all years where Berkshire exercised unlawful control over BNSF. This remedy is an appropriate one under § 11323, and one that is tailored to the facts of this case.

First, BNSF's 2009 regulatory cost of capital can be calculated using data submitted in the Board's 2009 industry cost of capital proceeding. The resulting cost of capital is 10.01%. Crowley/Fapp V.S. at 7. Using the 2009 cost of capital avoids the complexities that arise in trying to calculate BNSF's cost of capital in later years[33] and reflects the last known calculation of BNSF's regulatory cost of capital before Berkshire's unlawful acquisition of BNSF. Crowley/Fapp V.S. at 4-7.

Second, BNSF's capital costs in 2009 (10.01%) were significantly below the STB's calculation of the capital costs for the industry average composite group in 2009 (10.43%). Crowley/Fapp V.S. at 8. Following BNSF's unlawful acquisition by

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[32] *See 2010 Cost of Capital* at 2 n.4; *2011 Cost of Capital* at 19-24; Crowley/Fapp V.S. at 4.

[33] *See 2010 Cost of Capital* at 8 (rejecting proposal "which would allow for BNSF's inclusion in the [2010] industry cost of capital").

financial powerhouse Berkshire in 2010, it is reasonable to assume that BNSF's actual capital costs decreased from 2009 levels. Crowley/Fapp V.S. at 8-9.

While BNSF's actual capital costs decreased after 2009, the industry average capital costs calculated by the Board – without BNSF in the composite group – increased significantly. The Board calculated the industry average cost of capital as 11.03% for 2010 and 11.57% for 2011.[34] These later costs have been, or will be, those the Board uses in calculating BNSF's URCS, and revenue adequacy, return factors, unless the Board directs otherwise in this proceeding. The Board can deny BNSF some of this windfall – caused solely by Berkshire's unlawful acquisition of BNSF – by applying BNSF's 2009 cost of capital to make its BNSF URCS and revenue adequacy calculations in all of the unlawful control years. Crowley/Fapp V.S. at 10-15.

Third, the Board stated in its 2010 cost of capital decision that it could not change its standards for developing the industry average composite railroad without first having a rulemaking proceeding.[35] Coal Shippers/NARUC are not asking the Board to change its standards for developing its composite group. Instead, Coal Shippers/NARUC are requesting that the Board utilize its broad remedial powers under § 11323 to ensure that Berkshire does not profit from its unlawful control of BNSF through use of the industry average costs of capital in effect during the unlawful control years.

Fourth, Coal Shippers/NARUC's proposed remedy would not impact any carrier other than BNSF. Coal Shippers/NARUC are not asking that the Board include

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[34] *See 2010 Cost of Capital* at 11; *2011 Cost of Capital* at 18.

[35] *See 2010 Cost of Capital* at 7-8.

BNSF in the Board's composite group industry cost of capital calculations. The Board would continue to calculate the industry cost of capital – excluding BNSF – and apply that cost in developing URCS variable costs, and making revenue adequacy determinations, for all carriers other than BNSF.

Fifth, Coal Shippers/NARUC's proposed § 11323 cost of capital remedy is tailored to start when Berkshire's unlawful control started and tailored to end when Berkshire's unlawful control ends. Coal Shippers/NARUC are not requesting that the Board treat BNSF differently than any other carrier after Berkshire comes into compliance with § 11323. Instead, Coal Shippers/NARUC request that the Board take corrective actions under § 11323 that apply only during the unlawful control period.

Sixth, Coal Shippers/NARUC provide a specific example illustrating the consequential financial impact of using a corrective cost of capital on one impacted Board rate prescription. *See* Crowley/Fapp V.S. at 12. The same types of corrective impacts apply across the board to all Board proceedings involving the calculation of BNSF costs during the unlawful control years. *Id.* at 10-11.

C. The Board Should Find that BNSF Is Revenue Adequate in 2010 and 2011

Coal Shippers/NARUC have applied the Board's revenue adequacy calculation procedures as applied using standard BNSF inputs in 2010 and 2011, with three exceptions: (i) they have removed the $8.1 billion acquisition premium from BNSF's net investment base; (ii) they have substituted BNSF's 2009 cost of capital

(10.01%) for the higher industry average costs of capital; and (iii) they have compared the resulting ROI with BNSF's 2009 cost of capital (10.01%). Crowley/Fapp V.S. at 16.

Coal Shippers/NARUC's calculations show that BNSF should be found revenue adequate in both 2010 and 2011 because BNSF's ROI in each year exceeds 10.01%. Specifically, BNSF's ROI in 2010 is 10.66% and its ROI in 2011 is 12.61%. The Board may make similar findings for 2012, and any additional unlawful control years, using data inputs for those years applied to the formula set forth above.

The Board should adopt these calculations as part of its remedial § 11323 relief order in this case. Coal Shippers/NARUC's calculations not only serve to advance the public interest, they also comport with common sense. As Coal Shippers/NARUC have emphasized in their prior filings, it makes no sense for BNSF to be deemed "revenue inadequate" when one of the world's most astute investors paid a huge premium to acquire the carrier in 2010.[36]

[36] *See* Coal Shippers/NARUC Op. at 45-46.

CONCLUSION

Coal Shippers/NARUC respectfully request that the Board issue a declaratory order granting the relief requested in their Opening, Reply and Rebuttal submissions, as supplemented by the relief requested in these Comments.

Respectfully submitted,

WESTERN COAL TRAFFIC LEAGUE
AMERICAN PUBLIC POWER ASSOCIATION
EDISON ELECTRIC INSTITUTE
NATIONAL ASSOCIATION OF REGULATORY UTILITY COMMISSIONERS
NATIONAL RURAL ELECTRIC COOPERATIVE ASSOCIATION
WESTERN FUELS ASSOCIATION, INC., AND
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Dated: November 8, 2012

CERTIFICATE OF SERVICE

I hereby certify that this 8th day of November, 2012, I have caused copies of the forgoing Joint Comments to be served via first-class mail, postage prepaid upon all parties of record to this case.

Daniel M. Jaffe

BEFORE THE
SURFACE TRANSPORTATION BOARD

	)	
	)	
Western Coal Traffic League –	)	
Petition For Declaratory Order	)	**Finance Docket No. 35506**
	)	
	)	
	)	

Verified Statement

Of
Thomas D. Crowley
President

and

Daniel L. Fapp
Vice President

L. E. Peabody & Associates, Inc.

On Behalf Of
Western Coal Traffic League
American Public Power Association
Edison Electric Institute
National Association of Regulatory Utility Commissioners
National Rural Electric Cooperative Association
Western Fuels Association, Inc. and
Basin Electric Power Cooperative, Inc.

November 8, 2012

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LIST OF EXHIBITS

EXHIBIT NO.	EXHIBIT DESCRIPTION
(1)	(2)
1	2009 BNSF Weighted Cost of Debt
2	Comparison of Actual WFA/Basin 2012 Payments to 2012 Payments Using Last BNSF Current Cost of Capital

I. INTRODUCTION

We are Thomas D. Crowley and Daniel L. Fapp. We are the same Thomas D. Crowley and Daniel L. Fapp that submitted an Opening Verified Statement ("OVS") in this proceeding on October 28, 2011, and a Rebuttal Verified Statement ("RVS") in this proceeding on December 20, 2011. A copy of our credentials is included as Exhibit No. 1 and Exhibit No. 2 to our OVS, respectively.

We have been requested by Counsel for Western Coal Traffic League, American Public Power Association, Edison Electric Institute, National Association of Regulatory Utility Commissioners, National Rural Electric Cooperative Association, Western Fuels Association, Inc. and Basin Electric Power Cooperative ("Coal Shippers/NARUC") to comment on issues arising from the Surface Transportation Board's ("STB" or "Board") Notice of Request for Comments in Docket No. FD 35506, *Western Coal Traffic League -- Petition For Declaratory Order*, served October 9, 2012 ("Order") regarding the failure of Berkshire Hathaway Inc. ("Berkshire") to disclose its ownership of two subsidiary railroad companies during Berkshire's acquisition of the Burlington Northern Santa Fe Corporation and its primary subsidiary, the BNSF Railway Company (collectively "BNSF").

Specifically, Counsel has requested that we determine BNSF's weighted average cost of capital ("WACC") for the year 2009, which is the last full year BNSF was a publicly traded, independent corporation, and compare the 2009 BNSF WACC to the WACC for the railroad industry as a whole for the years 2009, 2010 and 2011. Counsel has also requested that we estimate the impact on various regulatory economic issues, including the STB's Uniform Railroad Costing System ("URCS"), if the BNSF's 2009 WACC were used instead of the railroad industry WACC. Finally, we have been requested to compare the 2009 BNSF WACC to the BNSF's return on investment ("ROI") as determined in the STB's Annual Railroad Revenue Adequacy determinations.

Our testimony is discussed further below under the following topical headings:

II. 2009 BNSF WACC

III. Impact Of Using The BNSF WACC Instead Of The Railroad Industry WACC

IV. Comparison of BNSF 2009 WACC And BNSF's Return On Investment

II. 2009 BNSF WACC

The STB established the current methodologies for determining the WACC in its decision in *Multi-Stage DCF*.[1] As explained in *Multi-Stage DCF*, the Board calculates the railroad industry WACC as the weighted average of the cost of debt, the cost of common equity and the cost of preferred equity, with the weights determined by the capital structure (the fraction of capital from debt or equity on a market-value basis) of the railroad industry.[2] The cost of debt capital is based on the market-value yields of the major forms of long-term debt instruments for the railroad holding companies used in the composite. These debt instruments include; (1) bonds, notes, and debentures ("bonds"), (2) equipment trust certificates ("ETCs"), and (3) conditional sales agreements ("CSAs"). The yields of these debt instruments are weighted based on their market values.[3] The cost of common equity is equal to the simple average of the capital asset pricing model ("CAPM") cost of equity based upon a portfolio of Class I railroad companies and the cost of equity determined using a multi-stage discounted cash flow ("MS-DCF") approach.[4]

The railroads included in the STB's annual cost of capital determination must meet certain specific criteria. These criteria pertain to the railroad's publicly traded parent corporations and include:

1. The common equity is listed on the either the New York Stock Exchange or the NYSE MKT exchange;[5]

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[1] See Ex Parte No. 664 (Sub-No. 1), *Use of a Multi-Stage Discounted Cash Flow Model in Determining the Railroad Industry's Cost of Capital*, served January 28, 2009 ("*Multi-Stage DCF*").

[2] See *Multi-Stage DCF* at page 2.

[3] See STB Ex Parte No. 558 (Sub-No. 15), *Railroad Cost of Capital – 2011*, served September 13, 2012 ("*2011 Cost of Capital*").

[4] See *Multi-Stage DCF* at page 15. The STB's procedures also call for the inclusion of the cost of preferred equity in the WACC calculation, but no railroad included in the cost of capital group has had outstanding preferred equity since 2002.

[5] NYSE Euronext, the owner of the New York Stock Exchange, purchased the American Stock Exchange in 2008. Since its acquisition, the American Stock Exchange has gone through several name changes and is now known as the NYSE MKT LLC. Today, almost all trading on the NYSE MKT exchange is in small-cap stocks, exchange-

2. The corporation paid dividends on its common equity throughout the year;
3. The corporation's railroad assets were at least 50 percent of its total assets;
4. The corporation's debt was rated investment grade; and
5. The corporation must be primarily a U.S. company.

As of the year 2011, only three Class I railroad companies met all of the criteria to be included in the cost of capital composite group -- CSX Corporation, Norfolk Southern Corporation and Union Pacific Corporation.[6] BNSF's holding company dropped out of the railroad industry cost of capital group beginning with the year 2010 cost of capital calculation due to failing to meet two of the required criteria.[7] First, BNSF's new parent corporation Berkshire does not pay dividends. Second, rail assets make up less than 50 percent of Berkshire's total assets. In other words, 2009 is the last year one could include BNSF in the cost of capital calculation using the STB's criteria.

The exclusion of BNSF from the cost of capital group was significant from a regulatory perspective because, as we have previously shown, BNSF's cost of common equity and cost of net debt was lower than the industry average, and thus its exclusion from the cost of capital group led to an artificial increase in the railroad industry WACC.[8] To demonstrate this, we have calculated the BNSF 2009 cost of common equity and cost of debt using the STB's WACC procedures and compared it to the STB's 2009 and 2010 WACC calculations.

A. BNSF COST OF <u>COMMON EQUITY</u>

The STB estimates the cost of common equity as the simple average of the CAPM cost of equity and the MS-DCF cost of equity. To estimate the BNSF's 2009 CAPM cost of equity, we

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traded funds and derivatives. None of the railroads included in the cost of capital group is traded on this exchange.

6 These companies are the publicly traded parent companies of the railroad operating companies.

7 See Ex Parte No. 558 (Sub-No. 14), *Railroad Cost of Capital – 2010*, served October 3, 2011 ("*2010 Cost of Capital*"), at page 2, note 4.

8 See the Reply Verified Statement of Thomas D. Crowley and Daniel L. Fapp in the *2010 Cost of Capital* proceeding at pages 26 to 28.

utilized the data set relied upon by the STB to determine the 2009 CAPM Beta for the portfolio of railroad companies, but excluded the data for all railroads other than the BNSF. In other words, we left in only the BNSF historic stock prices and shares outstanding, the historic S&P 500 prices, and the average weekly yield on Three-Month T-Bill rates. Regressing the return on the BNSF common equity against the return on the S&P 500 resulted in a BNSF Beta of 0.983.[9] The BNSF specific Beta estimate was significantly lower than the composite industry 2009 Beta of 1.0915 determined by the STB.[10]

Next, using the 2009 average yield to maturity for a 20-year Treasury Bond and the market risk premium of 6.67 percent used by the STB and combined with the BNSF Beta estimate of 0.983, we developed the BNSF CAPM cost of equity as shown in Table 1 below.

Table 1
2009 BNSF CAPM Cost of Equity

Item (1)	2009 CAPM Cost of Equity (2)
1. Risk Free Rate [1/]	4.11%
2. Beta [2/]	0.983
3. Market Risk Premium [3/]	6.67%
4. Cost of Equity [4/]	10.66%

[1/] See *2009 Cost of Capital* at page 7.
[2/] See Crowley/Fapp e-workpaper "BNSF 2009 Cost of Capital Workpapers.xlsx."
[3/] See *2009 Cost of Capital* at page 7.
[4/] Line 1 + (Line 2 x Line 3).

As shown in Table 1 above, the 2009 BNSF CAPM cost of common equity equals 10.66 percent. In comparison, the STB calculated a CAPM cost of common equity for the composite railroad group in 2009 of 11.39 percent.

[9] See e-workpaper "BNSF 2009 Cost of Capital Workpapers.xlsx."
[10] See Ex Parte No. 558 (Sub-No. 13), *Railroad Cost of Capital – 2009*, served September 30, 2010 ("*2009 Cost of Capital*") at page 7.

The 2009 BNSF MS-DCF required no calculations on our part as the STB included the 12.62 percent cost in its *2009 Cost of Capital* decision.[11] Pursuant to the STB's procedures, the cost of common equity is equal to the simple average of the CAPM and MS-DCF costs of equity as shown in Table 2 below.

Table 2
2009 BNSF Average Cost of Equity

Item (1)	2009 Average Cost of Equity (2)
1. CAPM Cost of Equity 1/	10.66%
2. MS-DCF Cost of Equity 2/	12.62%
3. Average Cost of Equity 3/	11.64%

1/ Table 1, Line 4.
2/ See *2009 Cost of Capital* at page 18.
3/ Simple Average of Lines 1 and 2.

As shown in Table 2 above, the BNSF's 2009 cost of common equity using the STB's procedures equals 11.64 percent.

B. BNSF COST OF DEBT

To calculate the BNSF's 2009 cost of debt, we relied almost exclusively on data contained in the STB's *2009 Cost of Capital* decision. The one exception to this data source was the estimated market value of BNSF's un-modeled ETC, which the STB did not include in its decision. We were able, however, to obtain from the AAR's Rebuttal workpapers in the *2009 Cost of Capital* proceeding the required information. As shown in Exhibit No. 1 to this Verified Statement, the BNSF's 2009 cost of debt, including flotation costs, equaled 5.63 percent. Once again, the BNSF's debt cost was lower than the STB's cost of debt determination of 5.72 percent for the railroad industry.[12]

[11] Id at page 18.
[12] Id at page 12.

C. BNSF CAPITAL STRUCTURE

The STB included the BNSF's 2009 capital structure in its *2009 Cost of Capital* decision. As shown by the STB, the BNSF's capital structure consisted of 72.89 percent common equity and 27.11 percent debt.[13]

D. BNSF WACC

Using the data identified above, we determined the BNSF's 2009 cost of capital as shown in Table 3 below.

Table 3

BNSF 2009 Cost of Capital

Item (1)	**2009** (2)
1. Weighted Cost of Equity	
a. BNSF Cost of Equity [1/]	11.64%
b. Common Equity Portion of Capital Structure [2/]	72.89%
c. Weighted Cost of BNSF Common Equity [3/]	8.48%
2. Weighted Cost of Debt	
a. BNSF Cost of Debt [4/]	5.63%
b. Debt Portion of Capital Structure [2/]	27.11%
c. Weighted Cost of BNSF Debt [5/]	1.53%
3. Weighted Cost of Preferred Equity [6/]	
a. BNSF Cost of Preferred Equity	0.0%
b. Preferred Equity Portion of Capital Structure	0.0%
c. Weighted Cost of BNSF Preferred Equity	0.0%
4. BNSF Weighted Cost of Capital [7/]	10.01%

[1/] Table 2.
[2/] See *2009 Cost of Capital* at page 19.
[3/] Line 1a x Line 1b.
[4/] Exhibit No. 1.
[5/] Line 2a x Line 2b.
[6/] The BNSF had no preferred equity issued in 2009.
[7/] Line 1c + Line 2c + Line 3c.

[13] Id at page 19.

As shown in Table 3 above, the BNSF 2009 WACC equaled 10.01 percent. In comparison, the STB determined the industry WACC for 2009 was 42 basis points higher at 10.43 percent.[14] In addition, there are strong indications that the Berkshire acquisition of BNSF lowered BNSF's cost of capital.

Berkshire had, and continues to have, a higher credit rating, which logically lowers BNSF's cost of debt. Additionally, Berkshire's acquisition of the BNSF impacted the BNSF's implicit cost of equity by lowering the railroad's debt to capital ratio. A company's cost of equity can generally be thought of incorporating two types of risk. First, business risk undertaken by the firm and borne by the equity shareholders based on the industry and general economic factors, and second, financing risks from the company's issuance of debt.[15] While BNSF may or may not have changed its business risk by being acquired by Berkshire, it did change its financial risks. Prior to its acquisition by Berkshire, BNSF had a debt to capital ratio of 0.4 or 40 percent as measured by Compustat.[16] In contrast, Berkshire's debt to capital ratio is 0.3 percent, after the acquisition of BNSF.[17] Berkshire's lower debt to capital ratio means it, and its divisions including BNSF, face less financial risks and lower implicit costs of equity.

The fact that the BNSF's 2009 WACC was lower than the average for the industry means that its removal from the cost of capital group will lead to an increase in the industry average while BNSF's own cost of capital is decreasing.

The above analysis highlights the obvious, i.e., the exclusion of the BNSF will lead to a higher WACC and has implications for the 2010 and 2011 industry average WACC as calculated

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[14] Id at page 12.

[15] See SBBI Ibbotson 2011 Valuation Yearbook at page 80, "Therefore, a levered beta incorporates the business and financing risks undertaken by the company and borne by the equity shareholders."

[16] See "Compustat Company Research: Burlington Northern Santa Fe Corp," January 2010. A copy of the Compustat report is included in our workpapers.

[17] See "Compustat Company Research: Berkshire Hathaway Inc.," May 2011. A copy of the Compustat report is included in our workpapers.

by the STB. The STB determined the WACC in those years equaled 11.03 percent and 11.57 percent, respectively.[18] We can safely presume, based on our discussion above, that had the BNSF still been included in the cost of capital group, the 2010 and 2011 WACC would have been lower, and BNSF's own cost of capital lower still.

[18] See *2010 Cost of Capital* at page 12 and *2011 Cost of Capital* at page 18.

III. IMPACT OF USING THE BNSF WACC INSTEAD OF THE RAILROAD INDUSTRY WACC

The STB calculates the railroad industry WACC as one of its annual regulatory responsibilities. The WACC determination is one component used in evaluating a railroad's revenue adequacy, as well as other regulatory actions, including, but not limited to, the evaluation of railroad abandonments, the determination of railroad access fees and the prescription of maximum reasonable rates.[19]

It is this last regulatory action, the prescription of maximum reasonable rates, that the Berkshire Acquisition, and its subsequent impact on the WACC, that has had the most direct impact on shippers. The STB currently uses its WACC calculations in nearly all aspects of a maximum reasonable rate proceeding. The STB uses its WACC determination as part of the stand-alone cost ("SAC") constraint by assuming the WACC for the stand-alone replacement for the incumbent carrier is equal to the railroad industry WACC. The WACC is also used in the determination of a railroad's Uniform Railroad Costing System ("URCS") variable cost of service, which has become an increasingly integral part of maximum rate cases.[20] First, the railroad's URCS variable cost is used in the quantitative market dominance calculations by demonstrating that the issue rate has a revenue to variable cost ("R/VC") ratio greater than the 180 percent Jurisdictional Threshold. Second, URCS variable cost is used to calculate revenue divisions on cross-over traffic under the STB's Average Total Cost ("ATC") revenue division methodology. Third, the STB's rate prescription process uses URCS variable costs as part of the Maximum Markup Methodology ("MMM"). Fourth, once the MMM process has developed

[19] See *2011 Cost of Capital* at page 1.

[20] Specifically, the pre-tax WACC is applied to the railroad's Way and Structures Investment in URCS Worktable B5 Part 6 and to the railroad's Equipment Investment in Worktable B5 Part 7 to develop the required return on investment portion of the URCS developed variable cost of service.

R/VC ratios over the 10-year rate prescription period, URCS variable costs are applied to the annual R/VC ratios to determine the prescribed rates per unit.

Any input factor that artificially increases a railroad's URCS variable costs will ultimately increase the prescribed rates to the shipper since rate prescriptions are now entirely dependent upon URCS variable costs. For example, if after the MMM process it is found that the R/VC ratios are less than the 180 percent jurisdictional threshold, rates are set at 180 percent of the URCS variable cost of service. If the MMM R/VC ratios are greater than 180 percent, then the rates are set based on the MMM R/VC ratios and the URCS variable costs. In either case, the final rates a shipper pays are dependent upon URCS variable costs. [21] Any factor that increases URCS variable costs will increase the prescribed rates.

Because the BNSF is now excluded from the STB's WACC determination, the STB's 2010 WACC is presumptively higher than if the BNSF were still included in the WACC calculation. We demonstrated above that the 2009 BNSF WACC equaled 10.01 percent, but we are unable to develop a 2010 BNSF WACC using the STB's procedures because the common equity information required is no longer available. However, as we also showed above, the 2009 industry average WACC was 42 basis points higher than the BNSF WACC. From this, and Berkshire's lower capital costs, we can infer that the 2010 industry average WACC was higher than the 2010 BNSF WACC, and therefore, the 2010 industry WACC is higher than it would be if the BNSF were still in the cost of capital group. Stated differently, the 2010 railroad industry WACC has been artificially increased due to the removal of the BNSF from the calculation.

To demonstrate the impact on prescribed rail rates of artificially increasing the URCS variable costs, we have developed a comparison of the payments WFA/Basin actually paid to

[21] See STB Ex Parte No. 657 (Sub-No. 1), *Major Issues In Rail Rate Cases*, served October 30, 2006 ("*Major Issues*") at page 14.

BNSF for the first three quarters of 2012, and what WFA/Basin would have paid to BNSF if the prescribed rates used BNSF's 2010 URCS Phase III variable costs calculated using the 2009 BNSF WACC instead of the 2010 industry WACC.[22] The results are included in Exhibit No. 2 to this Verified Statement and are summarized in Table 4 below.

Table 4
Comparison of Actual WFA/Basin 2012
Payments to 2012 Payments Using BNSF 2009 URCS

Quarter	Actual Payments	Payments Using 2009 WACC In The 2010 URCS Variable Costs	Difference [1/]
(1)	(2)	(3)	(4)
1. 1Q 2012	$8,306,117	$8,101,622	$204,495
2. 2Q 2012	$9,292,351	$9,048,390	$243,962
3. 3Q 2012	$7,215,406	$7,032,083	$183,323
4. Total [2/]	$24,813,875	$24,182,095	$631,779

Source: Exhibit No. 2
[1/] Column (2) – Column (3).
[2/] Sum of Lines 1 to 3.

As demonstrated in Table 4 above, WFA/Basin paid approximately $632,000 in higher transportation costs solely due to a higher WACC included in BNSF's URCS variable costs.[23] The over-payments shown above are not a one-time issue. Because of the lag between the end of the calendar year and the Class I railroads' issuance of their Annual Report Form R-1, and the lag from the issuance of the Annual Reports and the STB's release of its annual railroad URCS formulas, it takes nearly a year for current information to be incorporated into a shippers rate prescription. Therefore, even if the STB were to make adjustments to its URCS calculations, it would not take effect for years to come. The STB is scheduled to release the BNSF 2011 URCS in time to calculate WFA/Basin's first quarter 2013 rates, while the BNSF 2012 URCS will

[22] We used the BNSF 2010 URCS as it is the most recent issued by the STB.
[23] This calculation does not include the additional reductions produced by removing the acquisition premium from BNSF's 2010 URCS.

presumptively be released in time to calculate WFA/Basin's first quarter 2014 rates. In other words, due to the regulatory lag in railroad reporting, shippers such as WFA/Basin will incur the impact on its rates for at least two more years.

IV. COMPARISON OF BNSF 2009 WACC AND BNSF'S RETURN ON INVESTMENT

As we indicated above, the railroad industry WACC determination is one component used in evaluating a railroad's revenue adequacy. The STB has repeatedly noted that this determination is essentially mechanical in nature with a railroad being considered revenue adequate if it achieves an ROI equal to or greater than the industry WACC.[24] Table 5 below shows the industry average WACC as determined by the STB and the STB's calculations of the BNSF ROI for the years 2009 to 2011.

Table 5
Industry Average WACC and BNSF ROI

Year	Industry Average WACC	STB's BNSF ROI
(1)	(2)	(3)
1. 2009	10.43%	8.67%
2. 2010	11.03%	9.22%
3. 2011	11.57%	9.86%

Sources: *2009 Revenue Adequacy*, *2010 Revenue Adequacy* and *2011 Revenue Adequacy*.

As shown in Table 5 above, the BNSF did not reach revenue adequacy in any of the years 2009 through 2011 based on the STB's current methodologies.

As we demonstrated in our OVS and RVS in this proceeding, determining the BNSF's revenue adequacy without taking into consideration the premium Berkshire paid for the BNSF, which was subsequently partially rolled into the BNSF's investment base, and without taking in to consideration the removal of the BNSF from the cost of capital group could lead to faulty

[24] See for example STB Docket No. EP 552 (Sub-No 14), *Railroad Revenue Adequacy – 2009 Determination*, served November 10, 2010 ("*2009 Revenue Adequacy*"), STB Docket No. EP 552 (Sub-No 15), *Railroad Revenue Adequacy – 2010 Determination*, served November 3, 2011 ("*2010 Revenue Adequacy*"), and STB Docket No. EP 552 (Sub-No 16), *Railroad Revenue Adequacy – 2011 Determination*, served October 16, 2012 ("*2011 Revenue Adequacy*").

conclusions.[25] We determined in the initial phase of this proceeding, and the BNSF's experts agreed, that Berkshire's acquisition of the BNSF increased the railroad's net investment base by $8.1 billion due to the purchase accounting adjustment.[26] Including the purchase premium within the investment base fundamentally lowered the BNSF's ROI, as the denominator in the ROI calculation increased for no other reason than to follow an accounting rule. BNSF's operations did not change as part of the acquisition, nor did its physical infrastructure. BNSF only appeared to become less revenue adequate due to the dictates of accountants.

In a similar fashion, BNSF appeared to become less revenue adequate because the railroad industry WACC increased when the BNSF fell out of the cost of capital group. As we explained above and in our verified statement in the *2010 Revenue Adequacy* case, the BNSF consistently had a lower cost of common equity and WACC than the industry average, indicating its removal from the calculation lead to an increase in the industry average. Therefore, the revenue adequacy comparison shown in Table 5 above is impacted not only by the suppression of the BNSF's ROI due to the purchase accounting adjustment for the purchase premium, but also by the inflated industry average WACC.[27]

To account for both of these issues, we have expanded the comparison shown in Table 5 above to include the BNSF's 2009 WACC and to include the BNSF's 2010 and 2011 ROI adjusted to remove the purchase premium. We show the expanded comparison in Table 6 below.

[25] See OVS at pages 23-24 and RVS at pages 23-24.

[26] See Joint Reply Verified Statement of Michael R. Baranowski and Benton V. Fisher filed November 28, 2011 in this proceeding ("Baranowski/Fisher VS").

[27] The Board determines whether a carrier is revenue adequate by comparing the industry average cost of capital in year "X" to the ROI calculated by dividing a carrier's net railway operating income in year "X" by its tax adjusted net investment base in year "X." Another way of expressing this formula is that a carrier is deemed revenue adequate in year "X" if its net railway operating revenue in year "X" exceeds its tax adjusted net investment base in year "X" multiplied by the current cost of capital in year "X". See, e.g., *2011Revenue Adequacy*.

Table 6
Industry Average WACC, 2009 BNSF
<u>WACC, STB BNSF ROI And Adjusted ROI</u>

Year	Industry Average WACC	2009 BNSF WACC	STB's BNSF ROI	Adjusted BNSF ROI
(1)	(2)	(3)	(4)	(5)
1. 2009	10.43%	10.01%	8.67%	8.67%
2. 2010	11.03%	10.01%	9.22%	10.66% [1/]
3. 2011	11.57%	10.01%	9.86%	12.51% [2/]

[1/] See RVS at page 23.
[2/] See Crowley/Fapp e-workpaper "Impact on Revenue Adequacy 2011.xlsx."

As demonstrated in Table 6 above, including the 2009 BNSF WACC and the 2010 and 2011 Adjusted BNSF ROI provides clarity as to BNSF's true position relative to revenue adequacy. In 2010, removing the purchase accounting adjustments from the BNSF's ROI calculation leads to an adjusted ROI of 10.66 percent, which, while still below the inflated industry average WACC, is above the BNSF's 2009 WACC.[28] The 2011 picture is even clearer. Adjusting the BNSF's 2011 ROI to remove the purchase accounting adjustments leads to an adjusted ROI of 12.51 percent.[29] This places BNSF's ROI not only above the 2009 BNSF WACC, but also above the inflated 2011 railroad industry WACC.

[28] As a basis of comparison, Baranowski/Fisher estimated BNSF's adjusted ROI to equal 10.91 percent.

[29] The increase in BNSF's adjusted ROI between 2010 and 2011 is consistent with the increases in ROI for the three other major U.S. based Class I railroads over the two years. Between 2010 and 2011, CSX saw a 0.69 percentage point increase in ROI, while NS and UP saw 1.91 and 1.57 percentage point increases in ROI, respectively.

VERIFICATION

COMMONWEALTH OF VIRGINIA)
)
CITY OF ALEXANDRIA)

I, THOMAS D. CROWLEY, verify under penalty of perjury that I have read the foregoing Verified Statement of Thomas D. Crowley, that I know the contents thereof, and that the same are true and correct. Further, I certify that I am qualified and authorized to file this statement.

Thomas D. Crowley

Sworn to and subscribed
before me this 7th day of November, 2012

Diane R. Kavounis
Notary Public for the State of Virginia

My Commission Expires: November 30, 2012
Registration Number: 7160645

VERIFICATION

COMMONWEALTH OF VIRGINIA)
)
CITY OF ALEXANDRIA)

I, DANIEL L. FAPP, verify under penalty of perjury that I have read the foregoing Verified Statement of Daniel L. Fapp, that I know the contents thereof, and that the same are true and correct. Further, I certify that I am qualified and authorized to file this statement.

Daniel L. Fapp

Sworn to and subscribed
before me this day 7th day of November 2012.

Diane R. Kavounis
Notary Public for the State of Virginia

My Commission expires: November 30, 2012
Registration Number: 7160645

2009 BNSF Weighted Cost of Debt

Item	Source	Calculation
(1)	(2)	(3)
Value of Debt		
1. Traded Debt	*2009 STB Cost of Capital* at 14	$5,736,076
2. Untraded Debt	*2009 STB Cost of Capital* at 14	2,179,741
3. Sub-Total Long-Term Debt	Line 1 + Line 2	$7,915,817
4. Equipment Trust Certificates	*2009 STB Cost of Capital* at 15	$236,659
5. Conditional Sales Agreements	*2009 STB Cost of Capital* at 15	0
6. Total ETC and CSA	Line 4 + Line 5	$236,659
7. Total Modeled Debt	Line 3 + Line 6	$8,152,476
8. Unmodeled CSA	BNSF had no CSA in 2009	$0
9. Unmodeled ETC	AAR 2009 Rebuttal Appendix C, Page 2	27,885
10. Capital Leases	*2009 STB Cost of Capital* at 15	1,565,435
11. Miscellaneous Debt	*2009 STB Cost of Capital* at 15	-11,353
12. Total Other Debt	Sum of Lines 7 to 10.	$1,581,967
13. Total Debt	Line 7 + Line 12	$9,734,443 1/
Debt yields		
14. Average Yield On Long-Term Debt	*2009 STB Cost of Capital* at 15	5.575%
15. Average Yield on ETC	*2009 STB Cost of Capital* at 15	3.816%
16. Average Yield on CSA	*2009 STB Cost of Capital* at 15	0
Market Percentages of Debt		
17. Bonds, Notes and Debentures	Line 3 ÷ Line 7	97.1%
18. Equipment Trust Certificates	Line 4 ÷ Line 7	2.9%
19. Conditional Sales Agreements	Line 5 ÷ Line 7	0.0%
20. Total Market Percentages	Sum of Lines 17 to 19	100.0%
Flotation Cost of Debt		
21. Bonds, Notes and Debentures	*2009 STB Cost of Capital* at 16	0.103%
22. Equipment Trust Certificates	*2009 STB Cost of Capital* at 16	0.078%
23. Conditional Sales Agreements	*2009 STB Cost of Capital* at 16	0.073%
24. Weighted Flotation Cost	Sum product of Lines 17-19 and Lines 21-23	0.102%
BNSF Weighted Cost of Debt		
25. Bonds, Notes and Debentures	Line 14 x Line 17	5.413%
26. Equipment Trust Certificates	Line 15 x Line 18	0.111%
27. Conditional Sales Agreements	Line 16 x Line 19	0.000%
28. Flotation Costs	Line 24	0.102%
29. Average Cost of Debt	Sum of Lines 25 to 28	5.626%

1/ Equals the value of BNSF debt shown on page 19 of the *2009 Cost of Capital* decision.

Comparison of Actual WFA/Basin 2012 Payments to 2012 Payments Using Last BNSF Current Cost of Capital

Time Period / Origin	Tons 2/	Payments: Actual Paid 2/	Payments: Using BNSF 2009 WACC 3/	Payments: Difference 4/
(1)	(2)	(3)	(4)	(5)
1Q12				
1. Antelope	580,506	$2,798,041	$2,728,380	$69,661
2. Black Thunder	82,245	$461,393	$449,878	$11,514
3. Caballo	180,829	$1,146,456	$1,119,332	$27,124
4. Caballo Rojo	66,225	$413,908	$403,974	$9,934
5. Cordero	82,320	$500,503	$487,332	$13,171
6. Dry Fork	379,481	$2,652,572	$2,588,060	$64,512
7. North Antelope	65,989	$333,244	$324,666	$8,579
8. Subtotal	1,437,595	$8,306,117	$8,101,622	$204,495
2Q12 1/				
9. Antelope	549,106	$2,663,162	$2,591,779	$71,384
10. Caballo Rojo	82,215	$515,332	$503,158	$12,174
11. Cordero	131,792	$806,565	$786,796	$19,769
12. Dry Fork	479,708	$3,377,144	$3,286,000	$91,145
13. North Antelope	380,700	$1,930,148	$1,880,657	$49,491
14. Subtotal	1,623,520	$9,292,351	$9,048,390	$243,962
3Q12				
15. Antelope	282,891	$1,397,483	$1,360,707	$36,776
16. Caballo	33,051	$214,833	$209,214	$5,619
17. Caballo Rojo	181,754	$1,166,858	$1,137,777	$29,081
18. Cordero	82,351	$513,868	$500,692	$13,176
19. Dry Fork	380,802	$2,726,542	$2,657,998	$68,544
20. North Antelope	231,748	$1,195,822	$1,165,695	$30,127
21. Subtotal	1,192,597	$7,215,406	$7,032,083	$183,323
22. Total - 1Q12 through 3Q12	4,253,713	$24,813,875	$24,182,095	$631,779

1/ Does not include Train 21 from Caballo (Train CCAMMOL021), because WFA/Basin did not provide this freight bill.

2/ BNSF Freight Bills sent to WFA/Basin.

3/ Rate based on revised STB 2010 URCS formula for BNSF with BNSF's 2009 pre-tax WACC.

4/ Column (3) - Column (4)