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BEFORE THE

SURFACE TRANSPORTATION BOARD

FINANCE DOCKET NO. 35506

WESTERN COAL TRAFFIC LEAGUE – PETITION FOR
DECLARATORY ORDER

REPLY OF
ALLIANCE FOR RAIL COMPETITION
MONTANA WHEAT & BARLEY COMMITTEE
COLORADO WHEAT ADMINISTRATIVE COMMITTEE
IDAHO BARLEY COMMISSION
IDAHO WHEAT COMMISSION
MONTANA FARMERS UNION
NEBRASKA WHEAT BOARD
OKLAHOMA WHEAT COMMISSION
SOUTH DAKOTA WHEAT COMMISSION
TEXAS WHEAT PRODUCER BOARD
WASHINGTON GRAIN COMMISSION
NATIONAL ASSOCIATION OF WHEAT GROWERS

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Dated: November 28, 2012

As expected, the comments filed November 8, 2012 by BNSF treat the failure to seek STB approval for the Berkshire Hathaway acquisition as irrelevant to the outcome of this proceeding. Although Berkshire Hathaway is now known to have had ownership interests in two small rail carriers (including one with which BNSF interchanged coal trains), and these interests disqualified Berkshire Hathaway from acquiring BNSF without STB approval, BNSF argues that post-acquisition divestiture is legally equivalent to pre-acquisition divestiture.

Even if the error acknowledged after the fact by BNSF can be characterized as relatively minor from a bookkeeping perspective, and even if that error is curable under STB precedent, it does not follow that BNSF's desire for an $8 billion URCS cost write-up should be approved. This is true for two reasons. In the first place, the write-up warranted disapproval even before disclosure of BNSF's error. In the second, BNSF's error was not negligible, for reasons detailed in the comments filed by ARC, et al. on November 8, 2012.

BNSF continues to rely heavily on its argument that its position is consistent with Generally Accepted Accounting Principles ("GAAP"). BNSF Comments at 7. However, the Rail Accounting Principles Board has pointed out that "where GAAP cost reasonably cannot be viewed as a meaningful regulatory measure of value, other measures of value may be used." RAPB Final Report at 39. Moreover, Berkshire Hathaway CEO Warren Buffett has warned against uncritical reliance on GAAP. See the Reply Verified Statement of ARC Witness Fauth at page 2, filed with the November 28, 2011 Reply Comments of ARC, et al. It was Berkshire Hathaway, not BNSF, that paid the premium, and Berkshire Hathaway has expressed high satisfaction with its purchase but has never sought the further reward of a regulatory windfall for BNSF based on the premium.

GAAP does not compel a Board finding in favor of BNSF in this proceeding. Nor do ICC and STB precedents, almost all of which involved a railroad (or two, in the case of Conrail) acquiring another railroad, with approval based on claimed or actual synergies. ARC, et al. agree with WCTL, CURE, and other shipper groups and shippers that the STB is not precluded by law from granting the relief requested by shippers in this proceeding. The central issue in this proceeding therefore involves assessing whether the public interest supports such relief. The public interest may be best understood by considering the interests of the affected parties.

The interests of captive shippers via BNSF, and via other major railroads, would clearly be disserved if the Board were to approve an $8 billion write-up of BNSF's URCS costs. As explained in the November 8, 2012 comments of ARC, et al., the rates of shippers captive to BNSF would be subject to unchallengeable direct rate increases of up to $8 billion, and additional unchallengeable rate increases could occur because of adverse impacts on revenue adequacy and the cost of capital, as well as BNSF's increased RSAM levels.

These adverse impacts would be exacerbated if, as is almost inevitable, a Board decision allowing a write-up of URCS costs and increased freedom for BNSF rate increases were seen on Wall Street as a green light for similar acquisitions of other Class I railroads. Investors, some of whom might have short-term goals, and some of whom are likely to care more about profit than about meeting U.S. freight transportation requirements, would surely be attracted by the prospect of an almost guaranteed recovery from captive customers of high bid prices. The greater the certainty of such recoveries, the greater the danger of future acquisitions that serve narrow private interests rather than the broad public interest.

It might be argued that what is bad for BNSF's customers must be good for BNSF itself. Such reasoning is fallacious. In the first place, BNSF did not pay the acquisition premium, and

Berkshire Hathaway, which did pay the premium, has never asked the Board to approve recovery of the premium from BNSF's captive shippers.

In the second place, when speaking on its own behalf, BNSF has been dismissive of the fears of captive shippers. In its November 28, 2011 Reply Comments in this proceeding, BNSF argued (at page 12) that the "overwhelming majority" of its rates are non-jurisdictional, and that its "rate base" is irrelevant to its pricing decisions. Summing up, BNSF argues that "there is no reason to believe that use of GAAP purchase accounting will have any material impact on rates paid by captive shippers." (Id.) [1]

Certainly, BNSF has not experienced increased costs of service as a result of becoming a subsidiary (through Burlington Northern Santa Fe, LLC) of Berkshire Hathaway, and BNSF has managed to improve its financial performance notwithstanding the current economic slump, with some of its revenue increases presumably coming from non-captive customers.

Taking these comments at face value, BNSF evidently bases its call for an $8 billion URCS cost write-up solely on a claim of fidelity to GAAP, and not on any desire for unchallengeable increases in rates paid by captive shippers. Why would the Board give BNSF rate freedoms it does not need or want, and further injure captive shippers who have already done more than their share to enable BNSF to reach revenue adequacy, merely because Berkshire Hathaway purchased the rest of BNSF's stock?

The Board itself has an institutional interest in the outcome of this proceeding. Permitting BNSF's URCS costs and RSAM level to rise, with no corrective action to offset revenue adequacy, cost of capital, and market dominance impacts, will clearly limit regulatory remedies

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[1] BNSF concedes that its RSAM level will rise, and that level is important under the Three Benchmark approach, which is the only way smaller shippers represented by ARC, et al. could afford to challenge rates and rate increases. (BNSF Reply Comments at 16-17). BNSF nevertheless goes on to deny any interest in unchallengeable rate increases.

the Board is able to implement in the future. In addition, the Board's ability to approve, disapprove, or impose conditions on future acquisitions will be restricted. Nor should the failings of BNSF's due diligence be condoned as de minimis. That would further weaken STB regulatory authority, leaving the Board less able to object if similar or worse deficiencies are disclosed as to future railroad acquisitions of national significance.

If the Board concludes (as it should) that it has discretion under the circumstances of this case to depart from strict GAAP as interpreted by BNSF, and that applicable precedents are distinguishable, the Board can and should consider fundamental fairness. In this proceeding, the Board does not face a difficult decision. One choice involves a windfall for BNSF, which paid no premium and experienced no increased costs, doesn't need a windfall, fell short of meeting basic disclosure and procedural requirements, and disclaims any intent to raise captive shippers' rates. Berkshire Hathaway, for its part, voluntarily paid what it did for BNSF but has never sought the contested write-up.

The other choice involves protecting vulnerable captive shippers from rate increases that, to the extent based on the $8 billion acquisition premium, BNSF says it does not seek. Of course, BNSF would not lose its ability to price its services, including its services for its captive customers, as it sees fit, subject to the remedies Congress authorized the Board to provide. However, those remedies would not be artificially circumscribed by an URCS cost write-up, artificially delayed revenue adequacy, artificially reduced capital costs, and an artificially elevated RSAM level.

It is clear that the public interest is better served by the second choice than by the first, even if the precedential value of this proceeding is ignored. But the Board must not ignore the impact for future acquisitions of subordinating the public interest to private interests in this proceeding. It is hard to imagine a worse message to Wall Street than for the Board to say, in effect, that there is nothing wrong with using future increases in captive shipper rates to fund a multi-billion dollar acquisition of UP, CSX, NS or any other major railroad. While a windfall for BNSF would doubtless encourage future acquisitions of other railroads, acquisitions driven by the prospect of increased monopoly rents are the acquisitions least likely to serve the public interest. Does the Board want to establish this precedent?

For the foregoing reasons and the reasons set forth in prior filings by ARC, et al. in this proceeding, the Board should adjust BNSF URCS costs to exclude the contested acquisition premium, exclude the premium in assessing BNSF revenue adequacy, and avoid an unwarranted increase in the cost of capital calculated for the railroad industry.

Respectfully submitted,

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Dated: November 28, 2012

CERTIFICATE OF SERVICE

I hereby certify that I have this 28th day of November, 2012, caused copies of the foregoing document to be served on all parties of record by first class mail.

John M. Cutler, Jr.

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