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BEFORE THE
SURFACE TRANSPORTATION BOARD

STB Ex Parte No. 661 (Sub-No. 2)

RAIL FUEL SURCHARGES (SAFE HARBOR)

BNSF RAILWAY COMPANY'S REPLY COMMENTS

BNSF Railway Company ("BNSF") hereby submits its reply comments in response to the Board's request in *Rail Fuel Surcharges (Safe Harbor)*, Ex Parte No. 661 (Sub-No. 2) (served May 29, 2014) ("*Safe Harbor*") for comments relating to the HDF safe harbor established in *Rail Fuel Surcharges*, Ex Parte No. 661 (served Jan. 26, 2007) ("*Rail Fuel Surcharges 1/26/07 Decision*"). BNSF submitted opening comments in this proceeding. As explained below, the opening comments filed in this proceeding show that the HDF index continues to be closely correlated to railroad fuel costs, that the spread between the HDF index and railroad fuel costs has remained relatively stable in recent years, and that there is no consensus among shippers that the HDF safe harbor should be eliminated or modified in any particular way. Some shippers, along with the railroads, support continuation of the safe harbor, while others urge the Board to eliminate the safe harbor. However, those commenters urging elimination of the HDF safe harbor have provided no valid reason for doing so. BNSF continues to believe that the safe harbor provides important benefits to shippers and railroads, and that it should be retained without modification.

I. Introduction

The Board asked for comments on a narrow issue – whether to modify the safe harbor for the use of the HDF index in rail fuel surcharges. Several shippers and shipper organizations submitted opening comments in this proceeding, but most of those comments addressed issues that are wholly outside the scope of this proceeding. For the reasons explained below, the Board should limit its consideration of the record to those comments that are actually related to the purpose of this proceeding.

There is no consistent position among shippers as to how the Board should proceed with respect to the HDF safe harbor. There continues to be broad recognition of the benefits to shippers from the use of the HDF index in fuel surcharges, and some shippers support a continuation of the safe harbor. Several commenters, including the U.S. Department of Agriculture ("USDA"), acknowledge the benefits of the HDF index but at the same time ask the Board to eliminate the safe harbor immunity that applies to the use of the HDF. These commenters cannot have it both ways. The Board cannot both encourage railroads to use a transparent third-party index like the HDF index and also eliminate immunity for its use—a safe harbor without immunity is, by definition, no longer a safe harbor. Eliminating the safe harbor would create a serious litigation risk by exposing a railroad to potential liability for factors outside a railroad's control, such as a possible deviation between the HDF index and the railroad's internal incremental fuel costs, notwithstanding the Board's encouragement to use the HDF index.

In BNSF's experience, the relationship between the HDF index and internal railroad fuel costs has stabilized in recent years. Before 2011, the unprecedented volatility of fuel prices created a divergence between the HDF index and BNSF's internal fuel price, as reflected in the Board's analysis covering the period 2006 through 2010 in *Cargill, Inc. v. BNSF Railway Co.*, STB Docket No. NOR 42120 (STB served Aug. 12, 2013) ("*Cargill 8/12/13 Decision*"). But the evidence in this proceeding shows that the "spread" between the HDF index and BNSF's internal fuel price has stabilized since 2010. The spread has also remained basically stable on an industry-wide basis over the 2011-2013 period. If conditions change in the future and the HDF index begins to diverge significantly from railroads' internal fuel costs, the Board may wish to revisit the safe harbor issue then. But as long as the HDF Index works as a reasonable proxy for changes in railroad fuel costs, as it does today, there is no justification for eliminating the HDF safe harbor and injecting more uncertainty and potential for litigation into fuel surcharge practices.

Shippers would lose the benefit of a transparent, third-party index if railroads were forced to abandon the HDF index due to litigation concerns that would arise if safe harbor immunity were eliminated. The Board was right when it concluded in its January 2007 *Fuel Surcharges* decision, based in large part on comments from shippers who sought more transparency in fuel surcharge programs, that shippers benefit from the transparency of a fuel surcharge mechanism that uses the HDF index. The recent history of challenges to rail fuel surcharge programs and the overall tenor of the opening comments by shippers and shipper groups in this proceeding clearly indicate that forcing railroads to use their internal fuel costs rather than the HDF index would only create more uncertainty and mistrust over fuel surcharges, possibly leading to additional litigation.

In these reply comments, BNSF does not respond on the merits to all of the proposals and arguments relating to fuel surcharges that are outside the scope of this proceeding. If shippers believe that the Board should examine aspects of railroad fuel surcharges other than the HDF safe harbor, they should petition the Board to do so through proper procedures. BNSF notes, however, that the premise underlying many of these comments – that fuel surcharge recovery has been excessive – is based on fatally flawed and often nonsensical analysis. Indeed, with respect to BNSF's mileage-based fuel surcharge that applies to agricultural products and industrial products, the Board expressly found in *Cargill*, after detailed analysis, that BNSF's fuel surcharge mechanism was reasonably designed to recover only incremental fuel costs.[1]

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[1] *Cargill 8/12/13 Decision*, at 17.

II. The Evidence Submitted In This Proceeding Does Not Support Removing The Safe Harbor.

A. The Available Evidence Shows That The HDF Index Continues To Closely Track Railroad Fuel Costs, And No One Has Suggested That A Better Index Exists.

The Board initiated this proceeding to determine whether the HDF index continues to reasonably track railroads' fuel prices in light of its finding in *Cargill* that there was a divergence between the HDF index and BNSF's fuel price over the analysis period in the *Cargill* case of 2006-2010. In BNSF's opening comments, BNSF explained that the divergence between the HDF index and BNSF's internal fuel prices that the Board saw in the years 2006-2010 appears to have been the result of historical factors that have not existed in the past three and a half years. The period 2006-2010 was a period of extreme fuel price volatility. But fuel prices have been more stable since 2010, and the spread between the HDF index and BNSF's internal fuel price has also stabilized. *See* BNSF's Opening Comments, at 9-10, STB Docket No. Ex Parte 661 (Sub-No. 2) ("BNSF Op."). While the spread between the HDF index and BNSF's internal fuel price continues to change each quarter, it has remained *virtually unchanged* on an annual average basis from 2011-2013.[2] Figure 2 in BNSF's Opening Evidence showed only a $0.01 change in the average spread during the years 2011 through 2013. *See* BNSF Op. at 10.[3]

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[2] Quarter-to-quarter changes in the spread are not uncommon, but the average annual spread has been stable. Indeed, in 1Q 2014, the spread increased but then declined again in 2Q 2014. *See* BNSF's quarterly STB reports.

[3] The other railroads submitting opening comments appear to have had similar experiences. Comments of Canadian Nat'l Ry. Co., at 3, STB Docket No. Ex Parte 661 (Sub-No. 2) (filed Aug. 4, 2014) ("Since [the second quarter of 2008], changes in the HDF Index and in CN's average fuel costs have generally tracked closely, so that the difference between average retail fuel prices reflected in the HDF Index and CN's actual average fuel costs have remained relatively stable over that time."); Comments of Union Pac. R.R. Co., at 8, STB Docket No. Ex Parte 661 (Sub-No. 2) (filed Aug. 4, 2014) ("[F]rom the first quarter of 2011 through the first quarter of 2014, fuel prices have been relatively more stable, and changes in the spread have been relatively smaller.").

Few of the shipper commenting parties actually submitted evidence addressing the relationship between the HDF index and railroad internal fuel prices, even though that question is at the core of this proceeding. The most extensive discussion of the relationship between the HDF index and railroad internal fuel prices is by Allied Shippers[4] and their witnesses Messrs. Crowley and Mulholland. As an initial matter, Messrs. Crowley and Mulholland acknowledge that the correlation between the HDF index and railroad internal fuel prices is very close. *See* Allied Shippers Op., Opening Verified Statement of Thomas D. Crowley and Robert D. Mulholland, at Exhibit CM-4 ("Crowley/Mulholland Op. VS") (from 1Q 2002 through 1Q 2014, "HDF prices and railroad fuel prices are well-correlated" with a correlation ranging between 0.974 and 0.997 using data from financial reports).

Moreover, the evidence submitted by Messrs. Crowley and Mulholland confirms BNSF's opening evidence on the stabilization of spread between the HDF index and BNSF's internal fuel prices since 2010. In fact, the Crowley/Mulholland analysis shows that after increasing between 2006 and 2010, the spread actually *decreased* from 2011-2013. *See* Crowley/Mulholland Op. VS at Exhibit CM-3, showing a decline in the BNSF spread from $0.798 in 2011 to $0.778 in 2013. The size of the spread in the Crowley/Mulholland analysis is different from the spread in the analysis that BNSF presented on opening because Crowley/Mulholland use financial reports to establish BNSF's internal fuel price rather than the reports that BNSF files with the Board, which BNSF used for the spread analysis. But the Crowley/Mulholland analysis confirms the basic results that BNSF presented on opening showing that the spread has stabilized.

[4] Comments of The W. Coal Traffic League, Am. Public Power Ass'n, Edison Elec. Inst., Nat'l Rural Elec. Coop. Ass'n, S. Mississippi Elec. Power Ass'n & Consumers Energy Co., at 36-41, STB Docket No. Ex Parte 661 (Sub-No. 2) (filed Aug. 4, 2014) ("Allied Shippers Op.").

The Crowley/Mulholland analysis also shows that the spread between the HDF index and railroads' internal fuel prices has remained basically stable on an industry-wide basis over the 2011-2013 period. While the spread changes period-to-period and differs among railroads, the average industry-wide spread shown in Crowley/Mulholland Exhibit CM-5 (lines 54-56) for the years 2011, 2012 and 2013 is $0.656, $0.692 and $0.672 respectively, for a total change over the period of $0.016.[5]

The Mercury Group suggests that the "spread" has increased in recent years, but it is impossible to assess Mercury's conclusions because they are based on "proprietary" data regarding "Wholesale Rail Diesel" prices that cannot be evaluated. Indeed, the industry-wide spreads calculated by Mercury are inconsistent with the spread calculations based on data filed with the Board by the railroads. *See* Initial Comments of the Mercury Group, at 6, STB Docket No. Ex Parte 661 (Sub-No. 2) (filed July 11, 2014) ("Mercury Op.").

Moreover, no commenting party has identified a superior index to the HDF index. One shipper specifically states that it "is not aware of any index that would serve [the] purpose [of a safe harbor] better than the HDF Index." Comments of Arkansas Electric Cooperative Corporation, at 2, STB Docket No. Ex Parte 661 (Sub-No. 2) (filed Aug. 4, 2014) ("AECC Op."). The USDA advocates that the HDF index "be retained for the purposes of providing accuracy, transparency, and accountability in the marketplace." Comments of USDA, at 7, STB Docket No. Ex Parte 661 (Sub-No. 2) (filed Aug. 4, 2014) ("USDA Op.").[6]

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[5] Kansas City Southern Railway ("KCS") is not included in these calculations because Crowley/Mulholland Exhibit CM-5 does not include KCS data for most of 2011. The railroads' STB reports, which include KCS, can be used to determine a weighted average spread, which also shows overall stability –$0.727 (2011), $0.740 (2012), $0.752 (2013), for a total change of $0.025 for the years 2011 through 2013.

[6] USDA does not number the pages of its opening comments. To identify page numbers on USDA's comments, we assume the first page with text would be page number 1.

B. The Analyses By Allied Shippers And Others Are Fundamentally Flawed.

The central issue in this proceeding is the relationship between the HDF index and railroad fuel costs, which, as shown above, has basically stabilized after diverging during the volatile period of fuel price changes prior to 2011. Several shippers nevertheless have used this proceeding as an opportunity to repeat their claims that rail fuel surcharges over-recover fuel costs. Two commenters – Allied Shippers and Highroad Consulting, Ltd. ("Highroad") – present analyses purporting to link their over-recovery claims to the use of the HDF index. Both analyses are flawed and unreliable.

Despite submitting evidence showing a stable (and declining) spread for BNSF over the period 2011-2013, Allied Shippers' experts (Crowley/Mulholland) nevertheless claim that "BNSF has collected well over half-a-billion dollars in additional revenues on unit coal train and carload traffic between 2011 and 2013 directly attributable to the Safe Harbor protection." Crowley/Mulholland Op. VS at 6. The calculations supporting this claim are presented in Crowley/Mulholland Exhibit CM-3. It is unnecessary to address all of the flaws in the calculations and assumptions underlying the Crowley/Mulholland analysis because there is a fundamental flaw with the analysis, clear from the exhibit itself, that invalidates the analysis altogether.

As noted in footnote 1 to the exhibit, the Crowley/Mulholland analysis for the years 2011-2013 is based on an assumption that BNSF was still using the fuel surcharge mechanism in place before 2011, which incorporated a "strike price," or a starting point for the fuel surcharge, of \$1.25 HDF. But in January 2011, BNSF increased the HDF strike price from \$1.25 to \$2.50 per gallon in its fuel surcharge mechanism. *See Cargill 8/12/13 Decision*, at 4 n.5. In effect, BNSF reallocated as of 2011 the amount of fuel costs that would be recovered going forward between the fuel surcharge and the base price, making the fuel surcharge a much smaller portion of the customer's total transportation bill. The Crowley/Mulholland calculations completely ignore the

2011 change in BNSF's fuel surcharge mechanism. Given the change in strike price in 2011, the important question is whether the spread changed from 2011 forward. The Crowley/Mulholland evidence shows that the spread did not change substantially during that period, fundamentally contradicting their claim of a massive over-recovery of fuel costs during that time period attributable to the spread.

Highroad took a different approach to assessing the supposed impact of changes in the spread over the period 2011-2013. Since the purpose of a fuel surcharge is to recover the incremental fuel costs produced when fuel prices increase (or decrease), Highroad looked at BNSF's increase in total fuel costs over the 2011-2013 time period and compared them to BNSF's increase in total fuel surcharge revenue. *See* Comments of Highroad Consulting, Ltd., at 10, STB Docket No. Ex Parte 661 (Sub-No. 2) (filed Aug. 4, 2014) ("Highroad Op."). The difference between BNSF's cost increases and the fuel surcharge increases in Highroad's analysis produces a purported "over recovery" amount that is approximately 5% of the half-billion dollar over-recovery claimed by Crowley/Mulholland for BNSF for the same time period.[7]

There are many flaws with the Highroad analysis and data, including the use of company-wide cost data and the use of HDF index values from individual quarters that do not correspond to the years 2011 and 2013. Moreover, Highroad's snapshot analysis fails to consider whether changes in fuel surcharge revenue relative to costs are attributable to factors such as changes in fuel surcharge participation rates or changes in BNSF's overall traffic mix.[8] Highroad's analysis is done at such a broad, aggregated level that the results are completely unreliable. Nevertheless, the difference between the results of the Highroad analysis and the

[7] $33,370,000 compared to $593,344,897 alleged by Crowley/Mulholland for years 2011-2013.

[8] Participation reflects the number of customers on a fuel surcharge program.

Crowley/Mulholland analysis shows how cautious the Board needs to be in reviewing shipper claims about fuel cost over-recovery, which can be easily distorted by flawed assumptions. The Board's focus in this proceeding should be on the spread between the HDF index and railroad internal fuel prices, which is the issue here, not on the many convoluted and flawed ways that shippers can attempt to create the appearance of an over-recovery of fuel costs.

All of the other fuel cost recovery analyses in the opening comments are irrelevant to the issue in this proceeding because they do not even purport to show whether the supposed over-recovery they present is attributable to any divergence between the HDF index and railroads' internal fuel price.[9] BNSF addresses the basic flaws in these analyses below in Section IV of these reply comments. However, the Board should give no weight to these analyses because they do not even purport to be relevant to the issue in this proceeding, which is whether the Board should modify its safe harbor for the use of the HDF index in a railroad's fuel surcharge mechanism.

III. Removing The Safe Harbor Would Create Uncertainty And Encourage Costly Litigation Without Offsetting Benefits.

The Board originally adopted the HDF safe harbor because, among other reasons, many shippers urged the Board to make fuel surcharge mechanisms more transparent through the use of a credible third-party index such as the HDF index.[10] As noted above, several commenting parties in this proceeding continue to acknowledge the benefits that come from the use of such a transparent index that is developed by a neutral government agency with no commercial interest in the application of the index. *See, e.g.* USDA Op. at 7 ("USDA believes the benefits of the safe

[9] Indeed, one commenter emphasizes that the over-recovery of fuel costs that it purports to identify is *not* attributable to the use of the HDF index at all but rather to some other aspects of rail fuel surcharge mechanisms that these parties urge the Board to investigate. *See* Comments from Consumers United for Rail Equity, at 10, STB Docket No. Ex Parte 661 (Sub-No. 2) (filed Aug. 4, 2014) ("CURE Op.").

[10] *See* BNSF Op. at 5-6 (summarizes some shipper comments supporting use of the HDF index in fuel surcharge mechanisms.)

harbor by way of continuing to use the HDF index to measure incremental fuel costs outweigh any drawbacks and advocates it be retained for the purposes of providing accuracy, transparency, and accountability in the marketplace."); AECC Op. at 2 ("AECC supports the concept of a 'safe harbor' provision for fuel prices, and is not aware of any index that would serve that purpose better than the HDF Index."); Highroad Op. at 20 ("if the Safe Harbor is eliminated, the railroads would not have an approved index on which to base their fuel surcharge programs and the result could be diminished transparency and credibility of the fuel surcharge programs. Therefore, at least for the present time, we recommend preservation of the HDF as a cost increase mechanism.").

A. The Benefits of the HDF Index Cannot Be Retained if Safe Harbor Immunity Is Removed.

At the same time that they acknowledge the benefits of the HDF index, some commenting parties urge the Board to eliminate prospectively any litigation immunity for the use of the HDF index in a fuel surcharge mechanism. *See, e.g.*, USDA Op. at 5, 6 ("If the Board chooses to modify the safe harbor instead of remove it, USDA believes eliminating immunity for over recovery is the best way in which to focus."); Highroad Op. at 13-14 ("the Board should redefine or modify the Safe Harbor to remove the immunity . . . and there should be a penalty if over-recovery occurs."); Comments of National Grain and Feed Association, at 7, STB Docket No. Ex Parte 661 (Sub-No. 2) (filed Aug. 4, 2014) ("NGFA Op.") ("The NGFA does not argue that the Board eliminate the use of the HDF index as a benchmark for measuring fuel costs. But we do strongly recommend that reliance on the HDF Index by granting it 'safe harbor status' should **not** immunize rail carriers from being challenged for setting fuel surcharges at levels that exceed the net incremental fuel costs actually incurred.") (emphasis in original). These commenting parties fail to explain why railroads would continue to have an incentive to use the HDF index if encouraged by the Board to do so when they could be subject to liability for over-recovery resulting from a divergence between the HDF index and their internal fuel costs.

Indeed, a number of other commenters recognize that the removal of safe harbor immunity for use of the HDF index in rail fuel surcharges would likely push railroads to abandon the HDF index altogether due to litigation concerns, and they urge the Board to preserve the benefits of the HDF index by maintaining the safe harbor, at least for the near future. *See, e.g.*, Comments Submitted by The National Industrial Transportation League, at 8, STB Docket No. Ex Parte 661 (Sub-No. 2) (filed Aug. 4, 2014) ("NITL Op.") ("[T]he League has concerns with elimination of the safe harbor altogether, since it is very possible that carriers would return to the use of opaque and unjustified procedures in their fuel surcharge programs that would have to be challenged on a case-by-case basis by members of the shipping public."); Mercury Op. at 21 ("We are concerned that an immediate elimination of the safe harbor provision may encourage conflict and further litigation. Rather, we recommend modifying the safe harbor rule in a staged manner.").

B. Use of Internal Railroad Fuel Costs Instead of the HDF Index Would Eliminate the Benefits From Using A Transparent Third-Party Index.

As noted above, shippers seeking to preserve the safe harbor recognize that eliminating the safe harbor may induce railroads to use internal fuel prices to avoid litigation risk. The Allied Shippers directly seek this result, expressly asking the Board to "modify the safe harbor by eliminating it, and requiring carriers that utilize any permitted fuel surcharge programs to use actual railroad fuel price changes, not HDF or other surrogate price changes, in their fuel surcharge tables." Allied Shippers Op. at 44. The Allied Shippers claim that use of actual railroad fuel prices is feasible and can be independently verified because the railroads already provide quarterly reports of their fuel prices to the Securities and Exchange Commission ("SEC") as well as the Board. Allied Shippers Op. at 48.

The fact that railroads provide quarterly reports to the SEC and the Board does not address the transparency and objectivity concerns that led the Board to adopt the HDF safe harbor in the first place. The reason that a government-generated fuel cost index instills confidence and trust in users of the index is that the index is produced by a public body that has no interest in the commercial uses of the index. Even though the data and formulae used to create the index are not transparent to the public, the objectivity and lack of commercial interest of the government agency that produces the index creates a level of trust and confidence in the results that would be lost if the index was produced by the railroads themselves.

There would also be other potentially adverse collateral effects from using the railroad reports to government agencies rather than the HDF index. Most important, the railroad reports are generated on a quarterly basis, and the use of quarterly fuel cost data would create a potentially serious time-lag problem. One benefit of the HDF index is that it allows the fuel surcharge to be based on fuel prices that are relatively recent. Using the HDF index, the current month standard carload surcharges are based on the average monthly HDF fuel price from two months earlier.[11] But with a quarterly index, there would be a substantial lag between the time period covered by the quarterly index and the time period in which transportation occurs. Assuming that a quarterly index could be generated within 30 days after the close of the preceding quarter (the assumption used in the current quarterly fuel reports), and that the new index could then be applied at the beginning of the following month, there would be a lag of at least four months between the start of the quarter covered by the index and the beginning of the new fuel surcharge. Moreover, the new surcharge would be in effect for an entire quarter before changing again, so that movements occurring at the end of a quarter would be based on fuel prices that are an average of six months

[11] For example, the average monthly price of the HDF index in January is used in fuel surcharges applied in March, a lag of two months.

old.[12] The time lag associated with a quarterly index could therefore introduce substantial distortions in fuel cost recovery, especially at times when fuel markets are more volatile.

Allied Shippers appear to recognize this time-lag issue and thus seek to require the railroads to report monthly fuel price data and use those monthly data for the fuel surcharge. *See* Allied Shippers Op. at 49. But requiring railroads to undertake new burdens to produce new monthly fuel data reports runs counter to the premise on which Allied Shippers' proposal is based, namely that the use of internal railroad data is already feasible and verifiable. As to feasibility, the Board already recognized that requiring railroads to report monthly data would be burdensome and inappropriate. In *Rail Fuel Surcharges*, the Board determined that railroad fuel cost data reports should be quarterly to conform with railroads' quarterly financial reporting requirements. *Rail Fuel Surcharges*, STB Docket No. Ex Parte 661 (Sub-No. 1), at 4 (STB served Aug. 14, 2007). As to verifiability, any monthly reports required to be developed by the railroads for use in fuel surcharges would have to be developed through new internal procedures that are not concurrent with financial reports, which are only produced on a quarterly basis. The development of new procedures could well give rise to new concerns or complaints by shippers.[13]

C. AECC's True-Up Provision Would Unnecessarily Complicate Regulation of Fuel Surcharges.

While AECC supports the continuation of a safe harbor for use of the HDF index in fuel surcharges, it also recommends that the Board establish a true-up mechanism that would prospectively "compare and reconcile HDF Index results with prices actually paid by railroads." AECC Op. at 8. Any system of regular adjustments to the fuel surcharge would impose enormous

[12] For example, under a quarterly index, BNSF fuel prices for the January through March quarter would be used in fuel surcharges applied in May through July.

[13] Indeed, Allied Shippers' ultimate objective appears to be to create so much litigation risk and burdensome regulation that railroads will be induced to eliminate fuel surcharges altogether. Allied Shippers Op. at 75.

procedural burdens on railroads and shippers to adjust internal accounting and pricing systems with every adjustment in the mechanism, and could lead to additional regulatory oversight and litigation when the required adjustments are implemented. Moreover, AECC's proposal is superficial and contradictory in many ways.

While AECC suggests that the true-up adjustment would be prospective only, it explains that the supposedly prospective adjustment would have to carry forward the historical deviation between the HDF index result and actual fuel prices, "us[ing] it prospectively to adjust permissible recovery of fuel price fluctuations in the following year." AECC Op. at 8-9. In other words, future purchasers of transportation would pay rates not based on the fuel price in effect at the time but rather based on adjusted fuel prices that reflected historical fuel prices. Such an approach would create more problems for shippers and concerns about fairness and transparency than it would solve, and would create winners and losers among shippers who have shipped different volumes and mixes of traffic subject to fuel surcharge programs in different years. Moreover, AECC's proposed true-up mechanism would be based on railroad industry-level fuel price data. AECC Op. at 9. Such an approach would not even achieve AECC's purported objective that the fuel surcharge mechanism reflect an individual rail carrier's actual fuel prices. AECC's (and the other shippers) concerns about the HDF index is that it does not accurately reflect a particular rail carrier's fuel prices but a railroad industry index will not likely precisely reflect an individual rail carrier's fuel prices either.

D. Expanded Fuel Cost Reporting Requirements Would Not Be Justified.

A number of commenters urge the Board to establish new and much expanded fuel surcharge reporting requirements in the quarterly report filed at the Board. *See, e.g.* USDA Op. at 6 (requests the STB to require railroads to provide, among other things, "total revenue allocated to fuel costs collected through the base rate");[14] NGFA Op. at 8 (requests the STB to require reporting of more granular, specific information by rail carriers by major commodity group); Allied Shippers Op. at 76 (seeks annual certifications from railroads regarding, among other things, whether fuel surcharge programs over-recover incremental fuel costs and whether a railroad has engaged in any prohibited double-dipping practices). The apparent objective of these new data reports is to make it easier for shippers and their counsel to assess their litigation prospects in challenges to rail fuel surcharges. Indeed, some commenters specifically describe the type of data to be reported as data that shippers would need to determine whether to bring a challenge to a fuel surcharge. *See* USDA Op. at 6; NGFA Op. at 8.

It would be inappropriate for the Board to establish reporting requirements that are designed solely to allow shippers to evaluate their litigation prospects. The Board already requires railroads to report data quarterly on their internal fuel costs, and those quarterly data reports can be used to determine whether a railroad's internal fuel price is reasonably tracking the HDF index and to monitor railroads' fuel cost recovery. There is no need or justification for imposing new and onerous reporting burdens on the railroads, particularly where the data reports are being requested simply to facilitate litigation. For example, the Allied Shippers' request for annual certifications and supporting data studies regarding whether a rail carrier has over-recovered its incremental fuel costs or engaged in double-dipping in effect puts the burden on a railroad to prove the

[14] The Board already has concluded that it will not attempt to analyze the fuel costs recovered by a rail carrier in its base rates. As the Board explained when it rejected Cargill's double-dipping claim, "[w]e also have practical concerns about trying to deconstruct a base rate. Costs – including fuel costs – can be among the factors that carriers consider in setting their base rates. But there are many other factors as well ... all of which could influence how a carrier structures its pricing. The Board does not attempt to attribute values to each component of rail pricing actions or rule on a carrier's rate on a component-by-component basis." *Cargill, Inc. v. BNSF Ry. Co.*, STB Docket No. NOR 42120, at 6 (STB served Jan. 4, 2011) ("*Cargill 1/4/11 Decision*").

reasonableness of its fuel surcharge before any claim challenging it has been filed. Such a request is unprecedented and would be extremely burdensome to comply with. As long as the HDF index works as a reasonable proxy for changes in railroad fuel costs, as it does today, there is nothing to be gained by eliminating the HDF safe harbor, imposing new reporting burdens and injecting more uncertainty and potential for litigation into fuel surcharge practices.

IV. Comments That Are Unrelated To The Safe Harbor Provision Are Outside The Scope Of This Proceeding And Should Not Be Considered.

Several commenters have used this proceeding as an opportunity to assert complaints about fuel surcharges that are unrelated to the safe harbor issue that is the subject of this proceeding.[15] The issues raised by these commenters are wide-ranging and completely unrelated to the HDF safe harbor. For example, some commenters have asked the Board to reopen Ex Parte 661, *Dairyland*, and *Cargill* to reconsider various aspects of those decisions that have nothing to do with the safe harbor provision.[16] Other commenters have asked the Board to initiate new rulemakings to address aspects of fuel surcharges unrelated to the fuel price index mechanism or to consider additional reporting requirements unrelated to the fuel price index.[17] Some commenters

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[15] *See, e.g.,* Allied Shippers Op. at 51 (acknowledging that this proceeding is focused on the safe harbor provision, but arguing that "[o]ther changes in the Board's current rail fuel surcharge policies must be made as well").

[16] *See, e.g.,* Highroad Op. at 14-15 (the Board should reopen Ex Parte 661 and consider whether the Board's fuel surcharge rules "should apply to exempt traffic"); Highroad Op. at 5 (arguing the Board should "re-open STB Ex Parte 661, *Rail Fuel Surcharge*s, so the railroads' fuel surcharge programs and the Board's fuel surcharge rules … should be reviewed for potential change or termination"); Allied Shippers Op. at 59-60 (the Board should reopen *Dairyland* to reconsider its holding that a shipper may not challenge the level of a fuel surcharge as applied to itself and must challenge the general formula); Allied Shippers Op. at 54-55 (the Board should reconsider its decision in *Cargill* that a shipper may not allege that a railroad is "double recovering" fuel cost increases both in its fuel surcharge and in the base rate).

[17] *See, e.g.,* Opening Comments of the Dow Chemical Co., at 16, STB Docket No. Ex Parte 661 (Sub-No. 2) (filed Aug. 4, 2014) ("Dow Op.") (asking the Board to initiate a rulemaking to conduct a "more searching review of fuel surcharge programs"); AECC Op. at 9-16, 19 (asking the Board to adopt various proposals relating to "fuel use" factors); Opening Comments of Colorado

have even asked the Board to order railroads to abolish fuel surcharge programs for regulated traffic.[18]

The Board's notice initiating this proceeding provided a clear and well-defined scope of the proceeding. The Board should not consider comments on issues that fall outside of the defined scope. If shippers want the Board to reopen prior proceedings or to initiate new rulemaking proceedings on other issues relating to fuel surcharges, they must follow the procedural rules for such requests and satisfy the applicable legal standards for such requests. They cannot use this proceeding as a back door way to initiate a broad review of other fuel surcharge practices or launch collateral attacks on the Board's decisions in prior proceedings.[19]

In any event, there is no credible evidence to support the premise of the shippers' various requests to undertake a broader review of fuel surcharges, namely that railroad fuel surcharges are generating revenues substantially in excess of incremental fuel costs. Indeed, as to BNSF's fuel surcharge, the Board's *Cargill* decision found precisely the opposite. Apart from desiring to further investigate the divergence between the HDF index and BNSF's internal fuel costs, the Board found that BNSF's fuel surcharge revenues closely corresponded to changes in BNSF's actual fuel costs and that the various elements of BNSF's fuel surcharge were reasonably designed to recover costs. *See Cargill 8/12/13 Decision,* at 17.

Springs Utils., at 2, STB Docket No. Ex Parte 661 (Sub-No. 2) (filed Aug. 4, 2014) ("Colorado Springs Utils. Op.") (asking the Board to "separately consider the reasonableness of other aspects of fuel surcharge programs," including "implied fuel usage"); CURE Op. at 12 (requesting the Board's "oversight" on other aspects of fuel surcharge mechanisms); NGFA Op. at 8 (asking the Board to require railroads to report information, such as fuel costs recovered through their base rates).

[18] *See* Allied Shippers Op. at 78; Highroad Op. at 19.

[19] Given that this proceeding was initiated as an ANPRM, the Board could not adopt a rule on issues outside the scope of the notice without going through further rulemaking proceedings. Moreover, the Board should not expect parties to have to address the merits of issues that are raised by other parties that are outside the scope of the ANPRM, many of which are little more than off-the-cuff suggestions of issues that the Board could or should investigate.

The analyses presented by the commenters in this proceeding supposedly showing an over-recovery of incremental fuel costs by the railroad industry are simplistic, flawed and completely unreliable. For example, the USDA submitted an analysis comparing the growth in railroad grain fuel surcharges to railroad fuel costs from 2001 through 2012. Half of the period covered by the USDA analysis pertains, mysteriously, to a time period before most railroads even established a mileage-based surcharge. If USDA is trying to evaluate fuel cost recovery under current fuel surcharge mechanisms, it makes no sense to look at a period before those mechanisms even existed. The sketchy information supporting the analysis provides no indication of how the USDA is accounting for the growth in fuel surcharge participation over the time period or how annual, company-wide data were used to identify costs and revenues for grain transportation. Moreover, there appear to be obvious errors or anomalies in the data, such as the apparent growth in fuel costs per car from 1Q 2011 to 4Q 2012 (from about $240 to $250, or about 4%) which bears no resemblance to the actual growth in fuel costs during that time period (the RCAF-Fuel index increased 26% during that time period, from $324.6 to $410.6). *See Quarterly Rail Cost Adjustment Factor,* STB Docket No. Ex Parte 290 (Sub-No. 5) (2011-3), at 5 (STB served June 20, 2011) (1Q 2011 Actual); *Quarterly Rail Cost Adjustment Factor*, STB Docket No. Ex Parte 290 (Sub-No. 5) (2013-2), at 5 (STB served Mar. 20, 2013) (4Q 2012 Actual).[20]

Other commenters submitted analyses purporting to show an over-recovery by comparing the percentage increase in fuel surcharge revenues to the percentage increase in total fuel costs. For example, Dow's Table 1 purports to show that the percent change in fuel surcharge revenues

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[20] USDA's Figure 2 is also completely without supporting data or explanation. It appears to be derived from the data in Figure 1 and simply reflects the percentage difference between the blue "fuel surcharges" line and the yellow "fuel costs" line for each quarter from Figure 1. Since it is impossible to tell how either number was derived, Figure 2 also provides no basis for assessing USDA's claim of an over-recovery of fuel costs. Other shippers included the identical figure in their comments. *See* NGFA Op. at 6.

for railroads other than NS from 4Q 2007 to 1Q 2014 exceeded by 15%-58% the percentage change in fuel costs over that time period. Other shipper commenters presented similar percentage-based analysis. *See* NITL Op. at 7; CURE Op. at 6. These apples-to-oranges comparisons are flawed and highly misleading. Fuel surcharges are intended only to recover a portion of total fuel costs. Since fuel surcharge revenues are less than total fuel costs for a given time period, the percentage change in fuel surcharge revenues from period-to-period will inevitably be higher on a percentage basis than the percentage change in total fuel costs even if the fuel surcharge is recovering exactly the incremental change in costs. A simple example illustrates the flaw in these shipper commenters' percentage-based comparisons.

Assume that total fuel costs in Period A are $100 and that the fuel surcharge recovers half of the fuel costs, or $50. If total fuel costs increase in Period B by 10%, the total fuel costs go from $100 to $110. The fuel surcharge is designed to recover the incremental $10 of fuel costs in addition to the $50 already recovered in the fuel surcharge. Therefore, the fuel surcharge revenues will go from $50 to $60. While the fuel surcharge has done exactly what it is supposed to do – recover incremental fuel costs – the percentage increase in the fuel surcharge revenues is 20% ($10/$50) while the percentage increase in the total fuel costs is only 10% ($10/$100). The percentage-based comparisons presented by Dow and other commenters are meaningless.[21]

Moreover, all of the shipper analyses fail to account for substantial capital costs incurred by railroads to improve fuel efficiency. In its opening comments, BNSF explained that it has invested considerable capital and management resources into improving fuel efficiency. *See* BNSF Op. at 11-12. The parties alleging an over-recovery of fuel costs do not even attempt to

[21] In addition to this flaw in their arithmetic, their analyses fail to consider a whole range of other issues, such as changes in participation and traffic mix and, as to BNSF, changes in the structure of the fuel surcharge program.

consider the costs incurred to achieve improvements in fuel efficiency. Indeed, not only do the commenters ignore the costs to achieve fuel efficiency in their fuel cost recovery analyses, they claim that any benefits from those expenditures should flow directly through to shippers through adjustments to the fuel surcharge that reflect any fuel efficiency cost savings. *See* Dow Op. at 14, 16; Allied Shippers Op. at 25-26 & Verified Statement of Thomas Johnson at 4; Colorado Springs Utils. Op. at 7. These shippers fail to explain why railroads would have an incentive to make large expenditures to achieve fuel efficiency gains if all of the improvements would directly flow through to the shippers.

The parties seeking a broad review of fuel surcharge practices also misconstrue the Board's limited role in regulating fuel surcharges. The Board has described its regulatory authority as focused on determining whether a fuel surcharge mechanism constitutes a misrepresentation by being designed to recover more than incremental fuel costs. *See Cargill 1/4/11 Decision*, at 2. Consistent with this limited role, when presented with a challenge to a railroad fuel surcharge, the Board asks only if the fuel surcharge has a "reasonable nexus to fuel consumption." *Rail Fuel Surcharges 1/26/07 Decision*, at 9. Exact precision is not required, and the Board does not micromanage fuel surcharges. *Cargill 8/12/13 Decision*, at 17 n. 23. Indeed, the Board has recognized the importance of allowing carriers flexibility in the design of their fuel surcharges. *Rail Fuel Surcharges 1/26/07 Decision*, at 10.

Last, the parties seeking more aggressive Board oversight of fuel surcharge practices would like the Board to convert its regulation of fuel surcharges into a species of rate regulation. But it has been long established that the Board's authority in the area of fuel surcharges does not extend to regulating the level of a railroad's fuel surcharge. *See Union Pac. R.R. Co. v. ICC*, 867 F.2d 646, 649 (D.C. Cir. 1989) (holding that the agency's authority to consider whether a railroad has committed an "unreasonable practice" does not include conduct that is "manifested *exclusively* in the level of rates that customers are charged" because such a claim may only be considered in a rate reasonableness case) (emphasis in original). The Board must let the market determine whether the level of a fuel surcharge is excessive, or address a challenge to the level of a fuel surcharge in a rate reasonableness proceeding. Otherwise, the Board's role is limited to ensuring that a railroad has not engaged in a misrepresentation by designing a "fuel surcharge" that is intended to recover more than incremental fuel costs.

V. Conclusion

For the reasons explained above, BNSF believes that the safe harbor established in 2007 in *Rail Fuel Surcharges* for the use of the HDF index in a fuel surcharge program provides important benefits to railroads and shippers, and it should be retained without modification.

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