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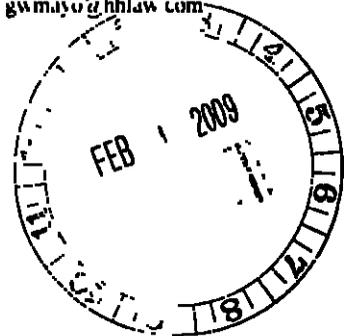
February 4, 2009

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BY HAND

The Honorable Anne K. Quinlan, Esq.
Acting Secretary
Surface Transportation Board
395 E Street, SW
Washington, DC 20423-0001

ENTERED
Office of Proceedings
FEB - 4 2009
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Re STB Ex Parte No 681
Class I Railroad Accounting and Financial Reporting
Transportation of Hazardous Materials

Dear Secretary Quinlan

Enclosed for filing in the above-referenced proceeding are an original and ten copies of the Comments of Arkansas Electric Cooperative Corporation on Proposed Rule-Making and three CD's containing the Comments

If you have any questions or I can be of any assistance, please let me know

Respectfully,

A handwritten signature in black ink that reads "George W. Mayo, Jr." with a stylized flourish at the end.

George W. Mayo, Jr

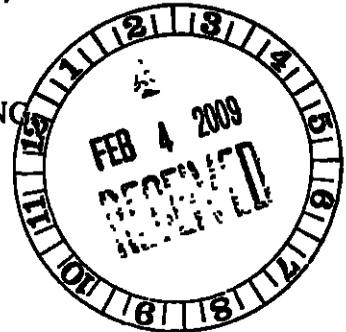
Enclosures

BEFORE THE
SURFACE TRANSPORTATION BOARD

EX PARTE NO 681

CLASS I RAILROAD ACCOUNTING AND FINANCIAL REPORTING
TRANSPORTATION OF HAZARDOUS MATERIALS

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COMMENTS OF ARKANSAS ELECTRIC COOPERATIVE CORPORATION
ON PROPOSED RULE-MAKING

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Dated. February 4, 2009

BEFORE THE
SURFACE TRANSPORTATION BOARD

EX PARTE NO. 681

CLASS I RAILROAD ACCOUNTING AND FINANCIAL REPORTING
TRANSPORTATION OF HAZARDOUS MATERIALS

**COMMENTS OF ARKANSAS ELECTRIC COOPERATIVE CORPORATION
ON PROPOSED RULE-MAKING**

Arkansas Electric Cooperative Corporation (AECC) respectfully submits these comments in response to the Advance Notice of Proposed Rulemaking served by the Board on January 5, 2009, which requests comments on whether and how the Board should update its accounting and financial reporting for Class I rail carriers and refine the Uniform Railroad Costing System (URCS) to better capture the operating cost of transporting hazardous materials (hazmat).

I. STATEMENT OF INTEREST

AECC is a membership-based generation and transmission cooperative that provides wholesale electric power to electric cooperatives, which in turn serve approximately 490,000 customers located in each of the 75 counties in Arkansas. In order to serve its member distribution cooperatives, AECC has entered into arrangements with other utilities within the state to share generation and transmission facilities. The largest of AECC's generation assets are its ownership interests in the White Bluff plant at Redfield, AR and the Independence plant at Newark, AR, each of which typically burns in excess of 6 million tons of Powder River Basin (PRB) coal annually. AECC holds a

35 percent interest in each of these plants (for which Entergy is the operator and majority owner). In addition, AECC holds a 50 percent interest (with American Electric Power) in the Flint Creek plant, which is located at Gentry, AR. This plant normally burns in excess of 2 million tons of PRB coal annually

As a result of the large volume of PRB coal used by these plants and the essential role of rail transportation for these movements, AECC has a direct interest in actions by the Board that affect its rail transportation options

II. COMMENTS

Pursuant to 49 U.S.C. § 10101 (13), the Board has an explicit mandate under the national transportation policy “to ensure the availability of accurate cost information in regulatory proceedings” In addition, 49 U.S.C. § 10101 (2) requires “fair regulatory decisions” and 49 U.S.C. § 10101 (5) guides the Board “to foster sound economic conditions in transportation” To achieve these objectives it is essential that the Board’s costing system provide accurate cost information

AECC supports fully the general proposition that the Board’s costing system should be maintained to the degree needed to ensure its validity in regulatory applications However, there are several aspects of the Board’s proposal and the current condition of URCS that warrant further consideration before the Board proceeds These include the following

- the focus on hazmat is unduly arbitrary, limited and inefficient,
- ensuring the accuracy of URCS variable costs in coal rate reasonableness cases is extremely important,
- unadjusted URCS produces biased results for large volumes of traffic that do not possess “system average” cost characteristics,

- the resulting cost misallocations are not a “zero-sum game”, and,
- available information indicates that the misallocations and their rate case effects are substantial.

Based on these considerations, AECC urges the Board not to proceed with changes in URCS that address hazmat without also investigating and implementing broader refinements that are needed to ensure the validity of URCS in its statutory applications

Focus on Hazmat is Unduly Arbitrary, Limited and Inefficient

The Board’s notice infers a need to revise URCS with respect to hazmat costs from the observation that some costs incurred due to hazmat traffic are not fully ascribed to such traffic by URCS

AECC does not dispute the Board’s reasoning regarding potential inaccuracies in the URCS costing of hazmat movements. However, there are other types of traffic for which URCS also does not accurately ascribe the costs incurred. It would be unreasonably arbitrary for the Board to initiate URCS refinements for hazmat traffic without also providing an equivalent opportunity to develop and implement URCS refinements for such other types of traffic

As discussed in greater detail below, captive coal shippers have interests in the accuracy of URCS that go beyond hazmat, and this may be true of shippers of other commodities as well. If the Board were to open URCS separately for each area or issue that may require refinement, parties who are affected by URCS costs would need to participate in multiple proceedings, at least if they wished to ensure that changes requested by other parties did not have improper impacts on their own traffic. Also, the timing of needed refinements would be impeded, as a sequence of proceedings would

need to be completed before any of the stakeholders could have faith in the validity (and stability) of URCS results

To avoid such delay and waste of the resources of the parties and the Board, if URCS is to be opened up at all, it should be opened more broadly than the Board has proposed. Simple efficiency dictates that if changes are to be made in URCS regarding hazmat, other changes to the same costing system that ultimately are likely to affect the same parties should be made at the same time

URCS Variable Costs in Coal Rate Cases

AECC's interest in URCS refinements stems primarily from the role of URCS determinations of variable costs in coal rate reasonableness cases. As described succinctly by the Board

Variable costs, which are those railroad expenses that vary with the level of service provided by the carrier, are key components in the analysis of a rate reasonableness case for two reasons. First, we may consider the reasonableness of a challenged rail rate only if the carrier has "market dominance" over the traffic at issue, and the statute precludes a finding of market dominance where the railroad shows that the revenue produced by the movement is less than 180% of the carrier's variable cost of providing the service. Second, when we find that a carrier has market dominance and that its rate is unreasonably high, we may not prescribe a maximum rate that is less than 180% of the variable cost of providing the service at issue. ^{1/}

In the aftermath of the Board's findings in the WPL/Edgewater rate case ^{2/}, UP expressed surprise that the stand-alone cost (SAC) for the railroad designed by the shipper in a rate case could be lower than the 180 percent R/VC jurisdictional threshold

^{1/} See STB Ex Parte No. 589, Calculation of Variable Costs in Rate Complaint Proceedings Involving Non-Class I Railroads, decision served Mar. 28, 2003 at pages 1-2 (footnotes omitted)

^{2/} See STB Docket No. 42051, Wisconsin Power And Light Company v. Union Pacific Railroad Company, decisions served Sept. 13, 2001 and May 14, 2002

With the stipulations to that effect entered by the parties in the more recent KCPL/Montrose 3/ and OGE/Muskogee 4/ proceedings, it is becoming more generally recognized that, at least in the west, the regulatory rate relief available to coal plants located on or near Class I trunk lines is often likely to be governed directly by the jurisdictional threshold

Unadjusted URCS Produces Biased Results

Unfortunately, there is ample evidence that the current URCS treatment of some cost components is not only inaccurate, but also overlooks systematically at least a portion of the productivity advancements and traffic changes that have occurred since URCS was implemented. For example, while a large unit coal train in the early 1980's might have moved 11,000 tons, such a train today might move 18,000 tons due to increased car capacity and greater numbers of cars in individual trains. During the same time, there has been explosive growth in light-loading intermodal traffic that has fundamentally changed the mix of rail commodity flows.

As a result of such changes in the industry, assumptions regarding the distributions of costs that once may have been reasonable may now be unreasonable. Consider, for example, expenses for diesel fuel. This cost component, which is far larger than the insurance cost issue cited by the Board for hazmat, is distributed by URCS on the basis of system average usage rates 5/. However, even a casual inspection of readily

3/ STB Docket No. 42095

4/ STB Docket No. 42111

5/ In URCS, it is understood that fuel expenses are apportioned on the basis of both gross ton-miles and locomotive unit-miles, with system averages used for each.

available information indicates that different commodity flows differ substantially from the system average in their actual fuel usage rates

As an illustration, UP in 2007 moved 1,052 billion gross ton-miles with a total of 1,326 million gallons of fuel, for an overall system average of 793.4 gross ton-miles per gallon of fuel used ^{6/} However, a unit coal train cycling on UP between the PRB and Kansas City – the corridor that accounts for the preponderance of PRB coal traffic – moves approximately 1,178.3 gross ton-miles per gallon of fuel, ^{7/} almost 50% above the UP system average. Put another way, using the example of a PRB-Kansas City movement via UP, almost 1/3 of the fuel expense ascribed on the basis of system average fuel use rates (as in URCS) will be fictitious. In this example, each ton would bear the cost of 0.46 gallons of diesel fuel that it does not use, solely as a result of the failure of the methodology to reflect the true productivity achieved by the movement

Of course, when significant volumes of traffic move at fuel efficiency levels that are higher than the system average, there necessarily is corresponding traffic that moves at comparatively low levels of fuel efficiency. While a full assessment of rail fuel efficiency by commodity is well beyond the scope of these comments, it is reasonable to

^{6/} See page 6 of UP's 2007 Analyst Fact Book, as presented at <http://www.up.com/investors/factbooks/2007/disclosure.shtml>

^{7/} Calculations based on the fuel use estimates presented in Table 2 of the report "Rail Fuel Use and Surcharges for White Bluff and Independence Plants" (May 15, 2006), which was submitted to the Board at the request of then-Chairman Buttrey in Ex Parte No. 661, Rail Fuel Surcharges. See STB Document ID 216548 at <http://www.stb.dot.gov/filings/all.nsf/WEBUNID/516F975178588A6D8525716F00709A16?OpenDocument>. Calculations assume a train containing 132 cars, each weighing 23 tons and carrying 120 tons of coal, pulled by 3 locomotives, each weighing 210 tons, moving over the 767 miles of loaded segments and 760 mile empty return between the PRB and Kansas City as shown in Table 2. The direct fuel use estimate of 14,345 gallons of fuel is increased by an allowance of 5 percent for unplanned operational problems and delays, as discussed on page 8 of the report

anticipate that such an analysis would find intermodal traffic to be a disproportionate user of rail diesel fuel. As explained in a recent comprehensive analysis authored in part by BNSF personnel,

Because of constraints imposed by the design and diversity of equipment, intermodal trains incur greater aerodynamic penalties and increased fuel consumption compared to their general freight counterparts. In order to compete effectively with highway transport, intermodal trains are typically the fastest freight trains operated thereby amplifying the effect of their poor aerodynamics. ^{8/}

Overall, since the time the URCS methodology was originally developed, many developments have transformed the mix of rail traffic, and the productivity and cost of its movement. In this light, it should not be surprising that URCS results are systematically inaccurate for some flows.

In the past, if URCS produced inaccurate results in the context of a rate case, coal shippers had a remedy in the form of "movement-specific adjustments" to URCS. However, in Ex Parte Nos. 657 ^{9/} and 646, ^{10/} the Board eliminated such adjustments. While the Board has acknowledged freely that changes in URCS may be needed to compensate for the resulting loss of accuracy, its prohibition of movement-specific adjustments to URCS in rate reasonableness proceedings has left coal shippers unable to obtain rate constraints that correspond to the actual cost characteristics of their movements, at least until a comprehensive update and refinement of URCS is undertaken.

^{8/} See Lai, Yung-Cheng et al., "Machine Vision Analysis of the Energy Efficiency of Intermodal Freight Trains", Journal of Rail and Rapid Transit (Volume 221, Number 3, 2007) at pages 353-364.

^{9/} STB Ex Parte No. 657 (Sub-No. 1), Major Issues in Rail Rate Cases, decision served Oct. 30, 2006.

^{10/} STB Ex Parte No. 646 (Sub-No. 1), Simplified Standards for Rail Rate Cases, decision served Sept. 5, 2007.

Cost Misallocations Are Not a “Zero-Sum Game”

While it might be contended that imprecision in the apportionment of costs between two commodity groups is a “zero-sum game”, that is not the case. From the earlier example, fuel costs incurred by intermodal that are shifted to coal through inaccurate cost allocation inflate artificially the URCS determination of variable costs in a coal rate case, and as a result, the jurisdictional threshold for captive coal shippers. However, if URCS cost distributions were changed to reflect cost causality, an increased distribution of fuel cost to intermodal would have little, if any, adverse effect on intermodal shippers. Intermodal moves under a class exemption that presumes the existence of effective competition – in other words, unlike coal, there basically are no captive intermodal shippers who would be affected by an increase in the distribution of URCS costs. However, even if there arose instances where the impacts of change would create trade-offs among captive shippers, for the Board to fulfill its statutory obligations, it must ensure that the traffic of such shippers is not burdened with phantom costs.

The Misallocations Are Substantial

The Board should be well aware from its own data that URCS currently produces variable cost estimates that are materially inflated relative to their likely true values for many coal movements. This can be seen, for example, in a comparison between the variable costs found by URCS in the recent KCPL/Montrose rate case and the variable costs found by the Board in older rate cases that allowed movement-specific adjustments. WPL/Edgewater, in particular, is arguably comparable to the Montrose movement in that it is a long-haul PRB movement using a similar-size consist handled on UP’s trunk lines for most of the distance to the plant. In the Edgewater case, the Board found variable

costs of \$0 0060/net ton-mile (as of Q2 of 2000 for the movement from the Black Thunder mine) 11/

This value is not directly comparable to the value of \$0 0093/net ton-mile (as of Q1 of 2006 for the movement from Black Thunder) 12/ found in the Montrose case using the unadjusted URCS methodology because of changes in factor prices and, potentially, differences in productivity between the two movements. However, assuming that the productivity benefits associated with the somewhat longer haul of the Edgewater movement are offset by the effects of the weight restriction applied to that movement, the unadjusted RCAF (which reflects factor price changes without productivity change) increased by a little less than 25 percent between Q2 of 2000 and Q1 of 2006 13/. Based on the variable cost of 0 0060/net ton-mile found in the Edgewater case, all else equal, a variable cost finding of no more than \$0 0075/net ton-mile would have been expected for Montrose. This implies that URCS overstated costs for the Montrose movement by \$0 0018/net ton-mile.

After application of the 180% R/VC ratio, the \$0.0018/net ton-mile overstatement of costs in the current URCS methodology translates to an apparent "premium" of nearly \$3 00/ton paid by the Montrose movement. In other words, where KCPL is paying

11/ Calculated as Linked Variable Cost of \$7.62/ton (from Revised Table A-5 in May 14, 2002 decision) divided by 1,270.24 loaded miles (from Table A-2 in September 13, 2001 decision)

12/ See STB Docket No. 42095, Kansas City Power & Light Company v Union Pacific Railroad Company, decision served May 19, 2008. Calculated as Total Variable Cost of \$8.52/ton (from Appendix B) divided by 915 miles (from Table 2).

13/ See http://www.aar.org/~/media/AAR/RailCostIndexes/Index_RCAFIhistory.ashx

\$15.32/ton (= \$0.0093 x 1.80 x 915 miles), this comparison suggests that they should be paying about \$12.35/ton (= \$0.0075 x 1.80 x 915 miles)

It must be noted, however, that this difference of nearly \$3.00/ton does not include or account for the fuel efficiency differential described previously. Even though the parties in the Edgewater case submitted movement-specific fuel use estimates, the Board's decision declined to utilize such estimates, and defaulted to unadjusted URCS estimates based on system averages ^{14/} Including the estimate (derived above) that under system average costing each ton moving in the PRB-Kansas City corridor via UP improperly bears the cost of 0.46 gallons of fuel that it does not use, and applying an approximate rail diesel price of \$1.85/gallon in Q1 2006, the total differential between the Montrose rate prescribed from unadjusted URCS and the rate that likely would result from actual costs is on the order of \$4.50/ton ^{15/}

Summary

In light of the foregoing considerations, it would not be accurate, fair or sound for the Board to limit its refinement of URCS to hazmat issues. The objective of having URCS better reflect actual costs is as meritorious for coal movements (and other traffic affected by URCS) as it is for hazmat, and pursuit of separate reforms would only introduce unnecessary delay and expense.

The Board therefore should not proceed with changes in URCS that address hazmat without also investigating and implementing the broader refinements that are

^{14/} See STB Docket No. 42051, Wisconsin Power And Light Company v. Union Pacific Railroad Company, decision served Sept. 13, 2001 at Appendix A, Section C 5 c

^{15/} Calculated as (((\$0.0018/ton-mile) x 1.80 x 915 miles) + ((0.46 gallons/ton) x \$1.85/gallon x 1.80)

needed to ensure the validity of URCS in its statutory applications, including coal rate cases.

Respectfully submitted,



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