224894

STEPTOE & JOHNSON LLP

ATTORNEYS AT LAW

Samuel M Sipe Jr
202 429 6486
ssipe@steptoe com

1330 Connecticut Avenue NW
Washington DC 20036 1795
Tel 202 429 3000
Fax 202 429 3902
steptoe com

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April 15, 2009

Via HAND DELIVERY

The Honorable Anne K Quinlan
Acting Secretary
Surface Transportation Board
395 E Street, S W
Washington, D C 20423-0001

Re: Docket No.42088, Western Fuels Association, Inc. and <u>Basin Electric Cooperative v. BNSF Railway Company</u>

Dear Secretary Quinlan

Enclosed for filing in the above-captioned matter are the original and ten copies of BNSF Railway Company's ("BNSF") Opposition to WFA/Basin's April 2, 2009, Request for Additional Rate Relief Also enclosed are three CDs containing an electronic version of the filing and three CDs, marked confidential, containing BNSF's workpapers

Respectfully submitted,

Samuel M Sipe, Jr
Counsel for BNSF Railway Company

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BEFORE THE
SURFACE TRANSPORTATION BOARD

WESTERN FUELS ASSOCIATION, INC. and BASIN ELECTRIC POWER COOPERATIVE, INC. Complainants, v. BNSF RAILWAY COMPANY Defendant.	Docket No. 42088

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BNSF'S OPPOSITION TO WFA/BASIN'S REQUEST FOR ADDITIONAL RATE RELIEF

Defendant BNSF Railway Company ("BNSF") hereby responds to the April 2, 2009 request for additional rate relief filed by complainants Western Fuels Association, Inc and Basin Electric Power Cooperative, Inc ("WFA/Basin"), which was styled as WFA/Basin's Reply to BNSF's Notice of Filing of Verified Notice of Compliance ("WFA/Basin's April 2, 2009 Request") In their April 2, 2009 Request, WFA/Basin ignore the plain terms of the Board's rate prescription and seek an order from the Board that would massively expand the relief that WFA/Basin have already received in this case For the reasons set out below, the Board should deny WFA/Basin's request for further relief [1]

[1] By styling their request for relief as a "reply" to BNSF's notice of compliance, WFA/Basin seek to foreclose a responsive filing by BNSF But WFA/Basin's April 2, 2009 Request is in fact a request for an order from the Board that would substantially expand the rate relief they have already obtained in this case The issues raised by WFA/Basin require careful scrutiny by the Board and BNSF is clearly entitled to file a response to WFA/Basin's arguments In any event, even if BNSF's response to WFA/Basin's pleading were considered a "reply to a (footnote continued)

INTRODUCTION

In its February 18, 2009 decision in this case, the Board used its newly adopted Maximum Markup Methodology ("MMM") to prescribe maximum revenue-to-variable cost ("R/VC") ratios for the 4th Quarter 2004 and for each year in the 2005-2024 period for the traffic moving to complainants' Laramie River Station The Board ordered BNSF to establish and maintain rates that do not exceed the maximum R/VC ratios prescribed by the Board The Board further instructed BNSF that "[f]or purposes of calculating reparations and setting the maximum rate for future movements, the variable cost of the issue movements must be calculated pursuant to unadjusted URCS, with indexing as appropriate " *Western Fuels Association, Inc and Basin Electric Cooperative v BNSF Railway Company*, STB Docket No 42088, slip op at 31 (served February 18, 2009) ("February 18, 2009 Decision")

In setting the current rates for WFA/Basin's traffic, set forth in BNSF's March 20, 2009 Notice of Filing of Verified Notice of Compliance ("Notice of Compliance"), BNSF complied with the express terms of the Board's February 18, 2009 Decision BNSF determined 2009 variable costs using 2007 unadjusted URCS costs – the most recent URCS costs available – and indexed those costs to current levels using URCS indexing procedures that have been standard practice before the ICC and the Board for almost 30 years

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reply," the Board regularly accepts such replies when they provide a response to arguments or evidence presented for the first time in the opposing party's reply *See, e g* , *Tulare Valley Railroad Company—Abandonment and Discontinuance Exemption—in Tulare and Kern Counties, Ca*, STB Docket No AB-397 (Sub-No 5X) at 2 (STB served Feb. 21, 1997), *Wyoming and Colorado Railroad Company, Inc —Abandonment Exemption—in Carbon County, WY*, STB Docket No AB-307 (Sub-No. 5X) at 1 (STB served Nov 10, 2004) WFA/Basin's entire April 2, 2009 pleading constitutes new evidence and argument If the Board considers BNSF's response to be a "reply to a reply," BNSF hereby requests leave to file this response in order to develop a complete record on which to address the issues raised by WFA/Basin in their April 2, 2009 Request

BNSF similarly intends to adhere to the express terms of the Board's February 18, 2009 Decision to determine the proper amount of reparations, using the appropriate URCS for the time period in question and the Board's standard indexing procedure WFA/Basin fail to mention in their April 2, 2009 Request that the relief they request would have an enormous impact on the amount of reparations As discussed below in Section II, when the Board issued the February 18, 2009 Decision, the Board announced that its order would generate about $100 million in reparations through 2008 But WFA/Basin's proposed approach to establishing maximum reasonable rates would produce over $145 million in reparations for that period, $45 million more than the Board estimated

In their April 2, 2009 Request, WFA/Basin purport to "correct" BNSF's calculations of the prescribed rates They do so without ever citing or acknowledging the Board's actual instructions to BNSF in the February 18, 2009 Decision regarding the establishment of maximum reasonable rates WFA/Basin argue that BNSF did not comply with the Board's order, claiming that the Board ordered BNSF to calculate variable costs using "4Q2004 BNSF variable costs employing Phase III procedures, indexed forward to the involved year using the RCAF-A " WFA/Basin's April 2, 2009 Request at 9 But there is no such order in the Board's February 18, 2009 Decision. In setting the current rates, BNSF did exactly what the Board instructed it to do and what has been done in every prior stand-alone cost ("SAC") case where prescribed rates have been based on R/VC ratios

WFA/Basin's criticism of BNSF's rates is actually a challenge to a central feature of MMM, which is to express a rate prescription as an R/VC ratio rather than as a set of predetermined rates that remain set in stone throughout the prescription period The key aspect of R/VC ratios is that the actual rates they produce in the real world will change from year to year to reflect the defendant carrier's real world cost changes over the course of the prescription period This feature of MMM is particularly important in this case where the prescription period will extend for a full 20 years. Railroad variable costs are subject to substantial change over time as input prices, traffic levels, and other determinants of cost change Recent experience with the volatility of fuel prices shows how railroad variable costs can change dramatically over time. Rate prescriptions set as R/VC ratios can accommodate such changes, whereas prescriptions of fixed rates cannot The Board's decision to express the rate prescription under MMM as an R/VC ratio rather than as a rate per ton based on outdated assumptions baked into the SAC calculations was a core holding in *Major Issues in Rail Rate Cases*, Ex Parte No 657 (Sub-No.1), (served October 30, 2006) ("Ex Parte 657 Decision"), that should not be subject to challenge here

With minor exceptions, there is no dispute that the variable costs BNSF used to implement the prescribed R/VC ratios are the most accurate reflection of BNSF's current variable costs But for WFA/Basin, BNSF's actual costs are irrelevant WFA/Basin in effect argue that the calculations in the Board's MMM workpapers take precedence over the agency's actual rate prescription. In doing so, they seek to substitute the variable cost calculations used to establish the prescribed R/VC levels for the actual variable costs needed to implement the prescribed R/VC levels in the real world.

MMM establishes R/VC ratios in the SAC world based on calculations that are necessarily based on time-bound record evidence and assumptions about the future But once the R/VC ratios have been prescribed through the MMM calculations, they are applied to the defendant carrier in the real world It would be both irrational and contrary to the Board's prior practice of implementing R/VC rate prescriptions to use MMM to prescribe R/VC ratios over a

20-year period and then to ignore the actual changes in variable costs that the defendant railroad incurs over the lengthy prescription period when the R/VC ratios are translated into specific rates Under WFA/Basin's approach, BNSF would be required to establish maximum rates in 2024 based on BNSF's URCS variable costs for the year *2004*, indexed by a *2006* RCAF-A forecast Such an approach would make no sense

The fatal flaw in WFA/Basin's approach is underscored by the fact that implementing the prescribed R/VC ratios with outdated URCS costs would result in rates for certain periods that are below the jurisdictional threshold and which the Board therefore has no authority to prescribe As BNSF demonstrates below, for the entire year 2008 and for the first quarter 2009, the revenues generated by WFA/Basin's proposed rates, which are produced using understated variable costs, are less than 180 percent of BNSF's actual variable costs for those periods If BNSF's variable costs increase again in the future, the same result could obtain in future periods An approach to setting maximum reasonable rates that produces rates that are impermissible under the statute is untenable

BNSF has complied fully with the express terms of the Board's rate prescription order in this case WFA/Basin's effort to obtain lower rates and additional tens of millions of dollars in reparations based on outdated costs is a clear overreach and should be denied.

BACKGROUND

The Board adopted the MMM rate reduction methodology in its October 30, 2006 Ex Parte 657 Decision Under the prior methodology, the percent reduction methodology, the Board reduced the challenged rates per ton by the percentage that SAC revenues in a particular year exceeded SAC costs Under the new MMM methodology, the Board abandoned its focus on rates per ton and instead decided to express its rate prescription as an R/VC ratio The defendant would be required in each year of the rate prescription period to limit the revenues generated by the issue traffic to a prescribed R/VC level for each year The Board noted that "Congress regarded R/VC ratios as an appropriate measure for allocating joint and common costs among rail shippers, as reflected in the 180% R/VC jurisdictional floor for rate relief" *Ex Parte 657 Decision*, slip op at 14

The Board's Ex Parte 657 Decision also changed the existing procedures for calculating URCS variable costs. The Board decided that it would no longer consider movement-specific evidence modifying the URCS costs that are developed by the Board in its annual URCS determinations The parties to SAC cases were instructed to use the Board's URCS Phase III program to calculate unadjusted URCS costs using nine specified categories of input information *Id* at 60, *see also id* at 52, note 166, specifying the nine inputs to be used

Shortly after issuing its Ex Parte 657 Decision, the Board issued a decision jointly in the present rate reasonableness case involving WFA/Basin and in the pending case *AEP Texas North Company v BNSF Railway Company*, Docket No 41911 (Sub-No 1), instructing the parties in both cases to provide the data necessary to implement the newly adopted procedures For purposes of implementing both the new methodology for allocating through revenues on cross-over traffic and the new MMM methodology, the parties were instructed to submit URCS variable costs for the base year, which in the WFA/Basin case was 2004 *Western Fuels Association, Inc and Basin Electric Cooperative v BNSF Railway Company*, STB Docket No. 42088, slip op. at 3-4 (served November 8, 2006) (issued jointly in Docket Nos 42088 and 41911 (Sub-No 1)) In the Ex Parte 657 Decision, the Board had explained that the maximum R/VC levels prescribed for each year of the prescription period would be determined by "project[ing] the initial (base year) URCS variable costs forward, using the hybrid approach discussed infra for projecting the SARR's operating expenses." *Ex Parte 657 Decision* slip op at 14. note 19

On September 10. 2007, the Board issued a decision in this case finding that WFA/Basin had failed to show that the challenged rates exceeded a reasonable maximum rate Based on a SARR that largely replicated BNSF's real world traffic patterns, the Board found that WFA/Basin "was not being forced to cross-subsidize other parts of BNSF's broader rail network " *Western Fuels Association, Inc and Basin Electric Cooperative v BNSF Railway Company*, STB Docket No 42088. slip op at 2 (served September 10, 2007) The Board observed that the challenged rates were already among the "lowest transportation rates any utility pays to acquire PRB coal " *Id* Nevertheless, the Board concluded that WFA/Basin should have the opportunity to reopen the record and present modified evidence in light of the Board's adoption of a new revenue allocation methodology for cross-over traffic *Id* at 3 In response, WFA/Basin presented new SAC evidence based on a hypothetical SARR that handled only a small portion of BNSF's real world PRB coal traffic and that relied heavily on traffic that had been rerouted from the real world route of movement

On February 18, 2009, the Board issued a decision finding that under WFA/Basin's new SAC assumptions the challenged rates exceeded reasonable maximum rates. The Board rejected BNSF's arguments that WFA/Basin's new SARR configuration exceeded the scope of the limited reopening the Board had ordered and that WFA/Basin's rerouting assumptions had been made to game the new MMM methodology and to produce an artificially low R/VC rate prescription The Board used its MMM methodology to identify the maximum R/VC ratios that BNSF could charge over the 20-year prescription period *See February 18, 2009 Decision*, slip op. at 31, Table 4 The Board ordered BNSF to establish and maintain rates that do not exceed the maximum R/VC ratios prescribed by the Board The Board further instructed BNSF that "[f]or purposes of calculating reparations and setting the maximum rate for future movements, the variable cost of the issue movements must be calculated pursuant to unadjusted URCS, with indexing as appropriate " *Id*, slip op at 31

BNSF complied with the Board's February 18, 2009 order and established new rates on March 20, 2009 Pursuant to 49 C F R §1111 9, BNSF filed a verified notice that it had complied with the Board's order The Board did not order BNSF to establish the maximum rates applicable to prior historical periods or to provide calculations of the amount of reparations that would be due under the February 18, 2009 Decision Under the Board's regulations, where the amount of damages cannot be determined from the record, the complainant is required to prepare a statement of damages and forward that statement to the carrier for confirmation of its accuracy 49 C F R §1133 2 As of the date of this filing, WFA/Basin have not yet sent their statement of reparations to BNSF Moreover, their April 2, 2009 Request was silent on the impact of their proposed approach on reparations To show the effect of WFA/Basin's proposed approach on reparations, BNSF has determined the maximum rates that would apply under the February 18, 2009 Decision and has made an estimate of reparations that will be due to WFA/Basin based on those rates The rates and reparations are set out below in Table 1 Table 1 also presents the rates calculated using WFA/Basin's approach and the corresponding reparations that would be due under that approach Details are included in the electronic workpapers submitted with this pleading

TABLE 1

RATE AND REPARATION COMPARISON

	BNSF Rates 1/	Estimated Reparations under BNSF Rates ($M) 2/	WFA Rates 3/	Estimated Reparations under WFA Rates ($M) 2/
2004 Q4	$3 24 - $4 04	$7 2	$3 11 - $3 91	$7 4
2005	$3 67 - $4 61	$23 7	$3 20 - $4 11	$26 7
2006	$2 94 - $4 46	$30 1	$2 61 - $3 87	$34 7
2007	$3 53 - $5 34	$27 4	$2 71 - $4 02	$37 3
2008	$4 78 - $6 24	$24 1	$3 24 - $4 16	$39 1
Total		**$112.5**		**$145.2**

1/ BNSF rates based on most current URCS costs, indexed as necessary
2/ Including estimated interest
3/ WFA work paper "MMM Model Linked to III-H-3 Reb (S1B final corrected revenue xls", Differences between BNSF's and WFA/Basin's 4Q04 rates are due to WFA/Basin s use of URCS costs excluding loop track miles and its purported implementation of technical corrections See Section VI below

ARGUMENT

I. As Instructed By The Board, BNSF Set Rates Using Standard Variable Costing Procedures.

In rate reasonableness cases, maximum rates have often been prescribed based on a specified R/VC ratio to ensure that the prescribed rate does not fall below the statutory jurisdictional threshold The Board in its Ex Parte 657 Decision referred explicitly to that practice in justifying its adoption of MMM, noting that the Board's decision to express the rate prescription as an R/VC ratio was consistent with Congress' decision to express the jurisdictional threshold as an R/VC ratio *Ex Parte 657 Decision*, slip op at 14. There is a longstanding and established practice for determining maximum reasonable rates in cases where the rate is expressed as an R/VC ratio, and BNSF followed that practice here

First, the Board uses URCS costs to determine the variable costs for a particular period based on the URCS Phase III costs developed by the Board for that period or, if the URCS costs for the period in question are not yet available, on the Board's most recently issued URCS For example, in *Wisconsin Power & Light Co v Union Pacific Railroad Co*, STB Docket No 42051, (served Sept 13, 2001) ("WPL"), the Board prescribed "the maximum reasonable rate level at 180% of the variable costs of providing service" *WPL*, slip op at 33 In their evidentiary filings, the parties developed variable costs for the first two quarters of 2000 However, at the time the evidence was filed, the Board had not yet established UP's 1999 URCS costs, so the parties used preliminary data for 1999, the most recent annual period When the Board issued UP's 1999 URCS costs, the Board substituted the final 1999 URCS cost calculations for the parties' preliminary calculations *Id*, slip op at 39 [2]

Second, where URCS costs must be indexed to current levels, the Board uses indexing procedures that it has adhered to for almost 30 years *See WPL*, slip op at 59, note 117 (citing relevant authority) The procedure involves the use of historic price indices developed by the Association of American Railroads ("AAR") for the relevant region (here, the western region) to index crew wages, wage supplements, materials and supplies, and fuel expenses All other indexable expenses are adjusted using the Producer Price Index – All Commodities This procedure is consistent with the indexing approach referenced in the governing statute. 49

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[2] *See also Carolina Power & Light Co v Norfolk Southern Railway Co*, STB Docket No 42072, slip op at 114 (served Dec. 23, 2003) ("Here, the parties relied upon preliminary 2001 data, because final 2001 URCS numbers were not available in time to be incorporated into the parties' evidence The Board has restated the preliminary 2001 URCS data where appropriate to reflect the final numbers"), *Kansas City Power & Light Company v Union Pacific Railroad Company*, STB Docket No 42095, slip op at 8 (Served May 19, 2008) ("Because the Board had not released its 2006 URCS data before the parties submitted their evidence, both parties developed their own versions of UP and Western Regional 2006 URCS costs We have since released 2006 URCS data, which employs our most recent 2006 cost-of-capital finding We will use these data in this case "), *Consolidated Rail Corporation –Abandonment – Between Warsaw and Valparaiso in Kosciusko, Marshall, Starke, La Porte and Porter Counties*, Docket No. AB-167 (Sub-No 1125) *1993 ICC LEXIS 303* (Served January 14, 1994) ("Conrail's use of the 1991 figures is acceptable because such data were the most recent available to applicant at the time it prepared and filed its evidence ")

U S C §10707(d)(1)(B) The Board recently invited parties to comment on the possibility of revising the current indexing approach "used in individual proceedings" to an approach that uses "the Rail Cost Adjustment Factor indexes published by the Board " Ex Parte No 431 (Sub-No 3), *Review of Surface Transportation Board's General Costing System*, slip op at 3 (served April 6, 2009) ("Ex Parte No 431") Unless and until the Board issues a rule adopting a different indexing approach, it is appropriate to adhere to the indexing approach long followed by the Board in individual proceedings

The Board's February 18, 2009 Decision prescribed R/VC ratios for each year 2004-2024 and ordered BNSF to establish and maintain rates that did not exceed those R/VC levels The Board did not instruct BNSF to abandon the existing practice for translating R/VC ratios into maximum rates To the contrary, the Board ordered BNSF to use the standard practice – "unadjusted URCS, with indexing as appropriate " The Board did not instruct BNSF to ignore the unadjusted URCS costs that the Board has issued for BNSF for 2005, 2006 and 2007 and to apply instead an indexed version of 2004 URCS costs for those years Nothing in the Board's February 18, 2009 decision indicates that BNSF was supposed to implement the prescribed R/VC ratios in a way that defied 30 years of practice and ignored actual URCS costs that have been calculated by the Board through 2007 and the most recent URCS costs where current URCS costs have not yet been published

BNSF used the standard practice to establish a rate for 2009 that reflects a 240% R/VC ratio, which is the R/VC ratio prescribed by the Board for that year Since the most recent available URCS was for 2007, BNSF used unadjusted 2007 URCS costs and indexed those costs forward using the Board's standard indexing procedure and the most recent quarterly AAR

Railroad Cost Indexes for the Western Region BNSF properly implemented the Board's instructions in the February 18, 2009 Decision in setting the maximum 2009 rates

II. There Is No Dispute That The Rates Set by BNSF Reflect BNSF's Current Costs, Including Recent Variable Cost Increases.

Apart from the relatively minor methodological issues addressed below in Section VI, WFA/Basin do not dispute that the variable costs used by BNSF to establish the 2009 rates most accurately reflect BNSF's current variable costs Moreover, WFA/Basin expressly acknowledge that BNSF's current variable costs are substantially higher than the costs that WFA/Basin would have the Board use in translating the prescribed R/VC ratio into a rate per ton for 2009 *See* WFA/Basin's April 2, 2009 Request at 17 Set out below in Table 2 is a comparison of the variable costs that BNSF calculated for 2009 using the most current data available and the much lower costs that WFA/Basin claim should be used based on data available at the time the SAC evidence was submitted As shown in the Table, WFA/Basin's outdated variable costs are approximately 30% lower than BNSF's current variable costs

TABLE 2

VARIABLE COST COMPARISON FOR 2009

	BNSF 1/	WFA 2/	Percent Difference
Antelope	$1 62	$1 14	-30%
Caballo Rojo	$2 12	$1 50	-29%
Caballo	$2 16	$1 52	-30%
Dry Fork	$2 39	$1 70	-29%

1/ Based on BNSF 2007 URCS indexed using standard indexing procedures

2/ Based on BNSF 2004 URCS indexed to 2009 using a 2006 forecast of RCAF-A.

Even BNSF's calculations likely understate the extent to which BNSF's variable costs have actually increased since 2004, the base year for URCS variable cost calculations used to determine the Board's R/VC prescription URCS variable unit costs are a function of both input price changes and changes in traffic volumes As traffic volumes drop, a railroad's variable costs per unit increase, all other things being equal As described above, BNSF's variable cost calculations are based on the most recent available URCS for the year 2007, indexed using the Board's standard indexing procedures Use of the AAR/PPI indices to adjust the 2007 URCS costs produces current variable costs that reflect actual changes in input price However, there has been a substantial drop in BNSF traffic volumes over the past several months as the U.S. economy has slid into a deep recession [3] These declines in traffic volume suggest that BNSF's variable costs *per unit* have probably increased The extent of the actual unit cost increases will not be known until the Board issues URCS calculations for 2008 and 2009 Nevertheless, the costs determined by BNSF are the most accurate current costs that are available using the Board's standard costing practices

The Board's recent notice in Ex Parte No 431 indicates an intention to refine URCS costing and reflects the Board's ongoing interest in ensuring that regulatory decisions are based on the most accurate variable cost evidence possible But WFA/Basin would have the Board ignore altogether evidence of BNSF's actual variable costs and use variable cost assumptions that are admittedly outdated and hence no longer accurate By using outdated variable costs that are substantially lower than BNSF's actual 2009 variable costs, WFA/Basin's approach would produce significantly less contribution for BNSF from the issue traffic under the prescribed rates than the Board expected when it established the rate prescription In fact, WFA/Basin's approach would have the perverse effect of *reducing* the contribution received by BNSF just at the time that cost increases require *higher* contribution Such an approach makes no sense

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[3] *See* http //www bnsf com/investors/weeklyunits/20090404 (reporting a year-to-date decrease of 13 56% in intermodal and carload units over 2008)

For example, the Board prescribed an R/VC ratio of 240% for 2009, thus allowing a contribution to BNSF's joint and common costs from the issue traffic of 140% of BNSF's variable costs The Board's SAC calculations assumed that the variable costs for movements from the Dry Fork mine were $1.70/ton. Thus, BNSF's contribution from Dry Fork movements was assumed to be $2 37/ton – 140% of the assumed variable costs But BNSF's actual 2009 variable costs for movements from Dry Fork are $2 39/ton, based on the most recent available data Under WFA/Basin's approach, the maximum 2009 rate for Dry Fork movements would be $4 07/ton Subtracting the actual BNSF variable costs of $2 39/ton from this rate would result in a contribution of only $1.68/ton, which is 30% lower than the $2 33 contribution that the Board expected that BNSF would earn on the Dry Fork movement when the SAC calculations were made Far from producing a "windfall" for BNSF, as WFA/Basin assert,[4] BNSF's calculations maintain the contribution percentage prescribed by the Board while WFA/Basin's approach would reduce both the contribution percentage and the actual dollar amount of contribution

The fundamental idea of a rate prescription based on R/VC ratios is to achieve a certain percentage contribution to defray joint and common costs. It would be inconsistent with this concept to require *reduced* levels of contribution in periods of cost *increases* When rates are set by reference to an R/VC ratio, the dollar amount of contribution increases with cost increases and declines with cost reductions Congress endorsed this approach when it set the Board's jurisdictional threshold as a function of R/VC ratios and the Board adopted this approach when it decided to set rate prescriptions under MMM as an R/VC ratio WFA/Basin's approach turns the logic of R/VC ratios on its head

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[4] *See* WFA/Basin's April 2, 2009 Request at 19

WFA/Basin's approach would also be inconsistent with the statutory revenue adequacy mandate The Board is required to "promote a safe and efficient rail transportation system" by "allowing rail carriers to earn adequate revenues" 49 U S C §10101(3) The Board is expressly instructed to "make an adequate and continuing effort to assist those carriers in attaining [the] revenue levels prescribed" 49 U S C §10704(a)(2) The Board "shall" apply its rate reasonableness standards "recognizing the policy of this part that rail carriers shall earn adequate revenues" 49 U S C §10701(d)(2). BNSF has never earned adequate revenues on a sustained basis under the Board's revenue adequacy standard Before the current economic downturn, BNSF was approaching revenue adequacy, but the dramatic changes in economic conditions have driven BNSF farther from revenue adequacy WFA/Basin's approach would make it even harder to achieve revenue adequacy by reducing contribution just at the time that BNSF needs additional contribution to offset higher costs

In particular, WFA/Basin's approach would substantially increase reparations, a fact that WFA/Basin failed to mention in their April 2, 2009 Request As noted above in Table 1, by ignoring BNSF's actual cost increases, WFA/Basin's approach would produce reparations through 2008 of over $145 million, $45 million more than the Board announced when it issued its February 18, 2009 decision *See* STB News Release, February 18, 2009 (noting that the Board was ordering BNSF to "reimburse the Utilities for approximately $100 million in overcharges from 2004 through 2008") As it turns out, the Board's estimate was $12 million too low. BNSF estimates that actual reparations for the period 2004 through 2008 will be about $112 million, with interest [5] WFA/Basin would add tens of millions of dollars to what is already

[5] Reparations will be even greater when movements from January 1, 2009 to March 20, 2009 are included in the reparations calculations

the largest award of rate relief ever ordered by the Board Under WFA/Basin's proposed approach, the Board's estimate of $100 million in reparations for 2004-2008 would balloon to a reparations award of $145 million for that period, including interest

III. An Essential Feature Of MMM Is That It Expresses The Rate Prescription As An R/VC Ratio That Can Reflect Changes In Costs Over Time.

WFA/Basin argue that the Board, in the Ex Parte 657 Decision, specifically ordered the parties in rate cases to use the same variable cost assumptions used in the MMM calculations to set maximum rates per ton WFA/Basin's April 2, 2009 Request at 14 They misread the Board's discussion of MMM in that decision In describing the new MMM methodology, the Board stated that "to calculate rate prescriptions, the parties should project the initial (base year) URCS variable costs forward " *Ex Parte 657 Decision*, slip op at 14, note 19 The "rate prescriptions" referred to by the Board were R/VC ratios and not rates expressed in dollars per ton The Board expressly stated that "[t]he SAC rate will be expressed as an R/VC ratio " *Id.* at 14 In other words, the Board was instructing the parties in rate cases to establish the R/VC ratios – the "rate prescriptions" – using the base year URCS Contrary to WFA/Basin's claim, the Board did *not* say that the rates per ton to be charged based on the prescribed R/VC levels should be calculated using the base year URCS

The "rate prescription" expressed as an R/VC level necessarily must be determined using the data and forecasts available in the record at the time the Board makes its SAC determinations The Board decided that the R/VC rate prescriptions would be determined using a single year's URCS, the base year URCS, indexed using the RCAF-A and a forecast of the

RCAF-A[6] But while the R/VC prescription must necessarily be made based on the data available in the record at the time the calculations are made, there is no reason to use outdated data in calculating maximum rates based on the prescribed R/VC ratios The latter calculations can, and should, be made using the most recent cost data to produce rates per ton that accurately reflect the prescribed R/VC level

Indeed, by expressing the rate prescription as an R/VC ratio, the Board's MMM methodology allows the rates per ton charged for the issue traffic to adjust over time as actual costs change This was an innovation introduced with MMM that addresses a problem that has long troubled the Board in SAC cases, namely that rate prescriptions that will be in effect for years into the future must be made based on time-bound evidence and forecasts of future events An essential feature of MMM is that it expresses the rate prescription as an R/VC ratio rather than as predetermined rates per ton that remain set in stone throughout the prescription period This feature of MMM makes it a flexible rate prescription mechanism that allows the actual rates charged for the issue traffic to yield the same percentage contribution prescribed by the Board as costs change Recent experience with fuel price volatility shows how rail costs can change dramatically and unpredictably. The flexibility provided by MMM's R/VC-based rate prescription and its responsiveness to real-world cost changes is particularly important in a rate prescription, like the prescription in this case, that is supposed to last for 20 years

[6] The Board originally instructed the parties to escalate the base year URCS using the hybrid cost escalation methodology also adopted in the Ex Parte 657 Decision In the February 18, 2009 Decision in this case, the Board concluded that the RCAF-A would produce a better forecast of the incumbent's variable costs for purposes of calculating the prescribed R/VC ratios *February 18, 2009 Decision*, slip op at 30

If the Board had intended the rates for future periods to be determined using only the data and forecasts included in the SAC calculations, as WFA/Basin suggest, there would have been no reason to express the rate prescription as an R/VC ratio All of the data necessary to calculate rates per ton for every year of the rate prescription period would have been available when the SAC calculations were made The expression of the rate prescription as an R/VC ratio would have been superfluous and misleading But the Board did not adopt such an approach with MMM and chose instead to express the rate prescription as an R/VC ratio that reflects cost changes over time WFA/Basin's argument challenges this central feature of MMM

WFA/Basin claim that the rates per ton *must* be calculated using the same assumptions used to produce the maximum R/VC levels to preserve the "integrity of the Board's SAC analysis " WFA/Basin's April 2, 2009 Request at 10. But the object of the SAC analysis is not to import the operations and performance of the hypothetical SARR into the real world Because the SARR is hypothetical, that cannot happen Once the SAC analysis is completed, there will always be a disconnect between the SAC world, based on assumptions that often turn out to be inconsistent with reality, and the real world where the SAC results are applied Traffic patterns will always differ to some extent from the assumptions used in the SAC calculations; revenues and costs will always diverge from the assumptions underlying the SAC calculations In this case, WFA/Basin's extensive use of rerouted traffic make it certain that SAC assumptions cannot be replicated in the real world

The SAC test is a tool used to identify maximum rates that are intended to be assessed in the real world Assumptions and estimates must be made to carry out the SAC calculations and to establish appropriate rate prescriptions, and it is important that the most accurate evidence available at the time be used to make those calculations But it would represent a triumph of form over substance to establish SAC rate prescriptions as a function of variable costs, and then ignore the defendant's real world variable costs to preserve the "integrity of the SAC analysis"

IV. WFA/Basin's Proposed Approach Produces Results That Are Inconsistent With The Plain Language Of The Decision And In Some Cases Are Unlawful.

In the February 18, 2009 Decision, the Board set out the maximum R/VC ratios that BNSF can generate from transportation of the issue traffic for each year 2004-2024 *See February 18, 2009 Decision*, slip op. at 31, Table 4 Under WFA/Basin's proposed approach, the actual R/VC ratios for the issue traffic would bear no resemblance to the R/VC ratios prescribed by the Board Under the Board's decision, BNSF is entitled to charge rates that yield 240% of its variable costs in 2009, but WFA/Basin's approach would result in rates that generate only 170% of BNSF's variable costs in 2009 By relying on outdated variable costs that are far lower than BNSF's current variable costs, WFA/Basin's approach dramatically reduces the actual R/VC ratio on the issue traffic Table 3 below compares the R/VC ratios that the Board prescribed for 2004-2009 with the actual R/VC ratios that WFA/Basin seek to impose

TABLE 3

COMPARISON OF PRESCRIBED R/VC RATIO TO R/VC RATIO USING WFA/BASIN APPROACH

	STB Prescribed R/VC Ratio 1/	WFA R/VC Ratio 2/
2004 Q4	241%	237%
2005	244%	225%
2006	229%	204%
2007	236%	183%
2008	243%	167%
2009	240%	170%

1/ Decision at 31
2/ WFA rates divided by most current URCS costs, indexed as necessary

Since the Board prescribed maximum R/VC ratios over a 20-year period, the divergence between the R/VC ratios prescribed in the Board's decision and those R/VC ratios that would actually be generated under WFA/Basin's approach could well become more pronounced over time

It would be arbitrary and misleading for the Board to announce a decision that prescribed rates at one R/VC level only to implement that decision in a way that generated R/VC ratios at a different level Moreover, as shown in Table 3, WFA/Basin's approach would produce rates that are unlawful The statute makes it clear that a railroad's actual costs, as measured by URCS, must be the basis for determining whether the Board has jurisdiction over a particular rate 49 U S C §10707(d) (costs should reflect "current wage and price levels"). Thus, the best estimate of BNSF's actual variable costs in a particular year must be used to determine whether the Board has jurisdiction

The fatal flaw in WFA/Basin's approach to setting maximum rates is illustrated by dividing the rates that WFA/Basin propose for 2008 and 2009 by BNSF's actual variable costs for those time periods calculated using the most recent URCS and the Board's standard indexing approach The resulting R/VC ratios are below the jurisdictional threshold as shown in Table 3 above The Board may not prescribe rates that yield R/VC ratios below the jurisdictional threshold, and it may not order reparations on rates that fall below the threshold If BNSF's variable costs continue to increase over the prescription period, future rates may also fall below the jurisdictional threshold The Board cannot impose a rate prescription methodology that yields rate levels that are impermissible under the statute

When the Board adopted MMM, it specifically linked the new R/VC rate prescription methodology to Congress' use of R/VC ratios to determine the Board's jurisdiction *See Ex Parte 657 Decision*, slip op at 14 The jurisdictional threshold rate level must be determined on the basis of a railroad's current costs, and the maximum rates determined in accordance with the Board's R/VC-based rate prescription under MMM should be calculated in the same manner

V. WFA/Basin's Heavy Reliance On The Board's Workpapers Is Misplaced.

WFA/Basin place great weight on the Board's estimate in the February 18, 2009 Decision that a rate prescription set at 240% of BNSF's variable costs in 2009 would "translate[] to a roughly 60% reduction in the transportation rate" *February 18, 2009 Decision*, slip op at 2 The Board's workpapers contain the rate per ton assumptions that appear to be the basis for this statement in the decision The rates per ton contained in the workpapers were based on BNSF's estimated 2009 variable costs for the issue traffic and those estimates were based on the only data in the record relating to BNSF's 2009 variable costs - *i e* , 2004 URCS costs indexed using the RCAF-A

There was no need for the Board to estimate the impact of its decision on the rates charged The Board's estimate was not an operative element of its decision – it was not a holding or an order The Board prescribed the maximum R/VC levels and instructed BNSF to implement those R/VC levels But having decided to make an estimate of the impact of its decision, the Board used the only data available to it to make the estimate – *i e* , the data in the record that were used to produce the SAC calculations In making its estimate of a 60% rate reduction, the Board was simply extrapolating from the data in the record If BNSF's actual 2009 variable costs had turned out to be closer to the estimated 2009 variable costs in the workpapers, the rate reduction would have been approximately 60% Since the data in the record were outdated and turned out to understate substantially BNSF's actual 2009 variable costs, the actual reduction in the rates for 2009 was less than 60% There is nothing remarkable in the fact that BNSF's actual 2009 costs differ from costs forecast based on outdated data

Regardless of its accuracy, the Board's estimate of the magnitude of BNSF's rate reduction should not be confused with the Board's rate prescription The Board did not order BNSF to reduce its rates by 60%, and it did not prescribe the rates included in its workpapers on which WFA/Basin relies If the Board had wanted to prescribe specific rates, it could have done so based on the calculations in the workpapers Since the workpapers contained rate calculations, the Board could have simply ordered BNSF to establish the rates set out in the workpapers But the Board did not prescribe specific rates It ordered BNSF to establish rates that reflected the prescribed R/VC ratio and BNSF fully complied with that order

VI. WFA/Basin's Proposed Adjustments To BNSF's Variable Cost Calculations Using Standard Costing Procedures Are Wrong or Insignificant.

WFA/Basin also raise a number of relatively minor issues regarding BNSF's use of the Board's standard URCS costing procedures to implement the prescribed R/VC ratios First, WFA/Basin claim that BNSF should have used the RCAF-A to index BNSF's 2007 URCS costs to current levels WFA/Basin's April 2, 2009 Request at 20 In its Notice in Ex Parte No 431, the Board indicated that it was considering the adoption of the RCAF as the index to be used to adjust URCS costs to current levels *Ex Parte No 431*, slip op at 3 Unless or until the Board concludes that use of the RCAF produces a more accurate calculation of a railroad's current variable costs, the Board should continue to use the standard indices

Second, WFA/Basin claim that BNSF mistakenly included index items that do not apply in cases where the shipper supplies its own railcars and they propose an alternative approach WFA/Basin's April 2, 2009 Request at 20 WFA/Basin's proposed indexing approach has a de minimus effect on the rate calculations If the Board concludes that WFA/Basin's approach is an appropriate way to index costs in cases where a shipper supplies its own railcars, BNSF would have no objection to implementing it in this case

Third, WFA/Basin complain that BNSF failed to use "the most recently available 1Q09 index data" WFA/Basin's April 2, 2009 Request at 20, note 17 But the recent data referred to by WFA/Basin were published *after* BNSF established the maximum rates pursuant to the Board's February 18, 2009 order BNSF used the most recent data available at the time it complied with the Board's order As WFA/Basin correctly point out, the index level in the data issued after BNSF established the rates is lower than the index level in data available at the time BNSF established the rates Use of the now current quarterly index data would produce lower rates for the second quarter 2009 But the Board did not instruct BNSF to establish rates that change on a quarterly basis BNSF acknowledges that rates that are adjusted on a quarterly basis are most responsive to cost changes, both up and down If the Board orders the establishment of quarterly rates, BNSF will adjust the rates accordingly.

Fourth, while WFA/Basin's pleading is silent on the issue, their recalculation of URCS costs for the issue traffic also includes a change in the movement characteristics used to produce the URCS costs Specifically, WFA/Basin eliminated the loop track miles at the various mine origins This is directly contrary to the Board's instructions in the Ex Parte No 657 Decision that the calculation of unadjusted URCS costs must include loop track miles *See Ex Parte 657 Decision,* slip op at 52, note 166

Finally, WFA/Basin note that BNSF's rates do not include the impact of the technical correction that the parties asked the Board to make in a joint petition filed on March 10, 2009 But the Board has not yet issued a decision on the technical correction petition WFA/Basin submitted workpapers purporting to show how the proposed technical correction should be implemented, but those calculations are erroneous in several areas WFA/Basin's workpapers are not complete, so it is not possible to determine the basis for WFA/Basin's errors But there are a number of anomalies in the WFA/Basin calculations that make it clear the WFA/Basin calculations are not to be relied upon[7] In any event, the instructions provided by the parties for implementing the technical correction are clear and the Board can and should implement those instructions without regard to WFA/Basin's workpapers.

VII. CONCLUSION

BNSF complied with the Board's order to establish rates that reflect the maximum prescribed R/VC ratio set out in the February 18, 2009 Decision The Board should deny WFA/Basin's request for an order requiring BNSF to establish rates that would generate revenues that are inconsistent with the R/VC ratios prescribed by the Board and that would add tens of millions of dollars in reparations to what is already the largest award of rate relief in the agency's history

Respectfully submitted,

Samuel M Sipe, Jr
Anthony J LaRocca
Frederick J. Horne
STEPTOE & JOHNSON LLP
1330 Connecticut Ave, N W
Washington, D C 20036
(202) 429-3000
ATTORNEYS FOR DEFENDANT

Richard E Weicher
Jill K Mulligan
BNSF RAILWAY COMPANY
2500 Lou Menk Drive
Fort Worth, TX 76131
(817) 352-2353

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[7] For example, WFA/Basin's summary workpaper shows that the revenues on one movement originating on the Campbell Subdivision would increase while the revenues on another movement on the Campbell Subdivision would decrease *See* "MMM Model Linked to III-H-3 Reb (STB final corrected revenue xls" Since the shift to real world mileages and densities should have had a similar effect on those movements, it makes no sense that the revenue changes would go in different directions

CERTIFICATE OF SERVICE

I, Anthony J LaRocca, hereby certify that on April 15, 2009, I caused a true and correct copy of BNSF's Opposition to WFA/Basin's Request for Additional Rate Relief to be served by hand on the following·

John H LeSeur
Slover & Loftus
1224 Seventeenth Street, N W
Washington, D C 20036

Anthony J LaRocca