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August 13, 2007

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By Courier

Honorable Vernon A. Williams
Secretary
Surface Transportation Board
395 E Street, S W
Washington, D.C. 20423-0001



Re: Ex Parte No. 558 (Sub-No. 10), "Railroad Cost of Capital -- 2006"

Dear Secretary Williams:

Enclosed for filing in the above-referenced proceeding are the original and ten copies of the Rebuttal Comments of the Association of American Railroads ("AAR") and Its Member Railroads. These Rebuttal Comments were due to be filed last Thursday, August 9, 2007, but due to an inadvertent communications problem among counsel, the fact that the filing wasn't made on that date did not come to the attention of the undersigned counsel until after the close of business on Friday, August 10. Because we are filing the Rebuttal Comments on the first business day following that discovery, and because the comments contain no new evidence but rather only limited legal arguments, AAR respectfully requests that the Board grant leave for this late filing.

Counsel for the only party to file Reply Comments in this proceeding, Western Coal Traffic League, has indicated that they have no objection to AAR's request

Sincerely,

G Paul Moates

**BEFORE THE
SURFACE TRANSPORTATION BOARD**



_____))
RAILROAD COST OF CAPITAL – 2006)
_____))

EX PARTE NO. 558 (Sub-No. 10)

**REBUTTAL COMMENTS OF THE ASSOCIATION OF AMERICAN RAILROADS
AND ITS MEMBER RAILROADS**

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**Counsel for the Association of American Railroads
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August 9, 2007

**BEFORE THE
SURFACE TRANSPORTATION BOARD**

RAILROAD COST OF CAPITAL – 2006

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) EX PARTE NO. 558 (Sub-No. 10)
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**REBUTTAL COMMENTS OF ASSOCIATION OF AMERICAN RAILROADS
AND ITS MEMBER RAILROADS**

Pursuant to the schedule adopted by the Board in its May 16, 2007 Decision instituting the above-referenced proceeding, the Association of American Railroads ("AAR"), on behalf of its member railroads, hereby submits its Rebuttal Comments.

Only one party, the Western Coal Traffic League ("WCTL"), filed a reply to AAR's June 25, 2007 opening Comments. However, WCTL's reply comments exceed the scope of the issues in the Board's notice in this proceeding, and with one modest exception, do not address whether the AAR submission properly applies the established methodology. The Board should proceed with the stated purpose of this proceeding and determine the railroad cost of capital for 2006 in accordance with its established methodology.

COMMENTS

The preponderance of WCTL's Reply Comments is devoted to rearguing matters that it has raised in Ex Parte No. 664, "Methodology To Be Employed In Determining the Railroad Industry Cost of Capital" That approach, however, is fundamentally inconsistent with the directive of the Board in its May 16 Decision that "Comments should focus on the various cost

of capital components [used in prior annual cost of capital determinations] using the same methodology followed in the 2005 decision.” Moreover, the Board expressly noted that if it proposed to change the existing methodology, “it may (as needed) seek supplemental evidence to implement the new alternative approach” but “[a]t this time we seek the information needed to calculate the 2006 cost of capital under the existing methodology.” Decision at 2. But unequivocally declaring that it “disagrees with these limitations”, WCTL proceeds to offer further argument regarding what it characterizes as “the unreasonableness of utilizing the market-based capital structure in conjunction with the DCF methodology.” WCTL Reply Comments at 2-3.

AAR does not believe that it would be consistent with the Board’s Decision to respond to the repetitive and expanded arguments and evidence offered by WCTL on issues that are before the Board in Ex Parte No. 664, nor would it be appropriate to do so given the requirement that the Board proceed to make a 2006 cost of capital determination for the railroad industry in timely fashion. Indeed, AAR has already expressed its disagreement with many of those arguments in filings which it has made in Ex Parte No. 664.

AAR also notes that the schedule established by the Board in Ex Parte No. 664 specified a deadline of December 8, 2006 for interested parties to file their comments, and further specified that the written testimony of parties participating in the hearing held in that proceeding on February 15, 2007, be filed by February 12, 2007. WCTL made extensive written submissions on both of those dates, and no provision was made for reply comments and the issues raised there have been under consideration by the Board since that time. Yet WCTL’s Reply Comments here indicate that it sought to submit them in Ex Parte No. 664 as well – apparently without even a perfunctory motion for leave to do so – and further that “these

comments respond in part to assertions made by the AAR for the first time at the hearing and in its post-hearing filing¹, and its comments include some responsive materials that were not available at the time of the hearing.” (WCTL Reply Comments at 3, fn. 2) WCTL has not sought leave to reopen the record in Ex Parte No. 664, and AAR notes that the Board’s website does not reflect the inclusion of WCTL’s Reply Comments in that docket. If the Board were to decide that it desires supplemental evidence regarding an alternative methodology for calculating the industry’s cost of capital, AAR is prepared to address whatever matters might be the subject of such a decision. At this juncture, however, no useful purpose would be served by going beyond the scope of the Board’s order establishing this proceeding – to determine the 2006 railroad industry cost of capital using the only approved methodology -- to respond further to WCTL’s Reply Comments on what it considers to be a superior methodology.

WCTL’s Reply Comments offer only limited criticism of the AAR’s application of the Board-directed methodology, primarily in several pages addressing one issue that was a subject of AAR’s opening Comments, namely financial analysts’ forecasts for the cost of capital and growth rates for the Class I railroads which are included in AAR’s calculations. (WCTL Reply Comments at 18-22) But WCTL’s comments in this regard amount to little more than quibbling over the number of such forecasts included in the IBES sample average² WCTL also refers to S&P calculations of capital costs for the Class I’s that WCTL itself concedes are the result of a DCF model, “discounted by the weighted average cost of capital, typically calculated using a CAPM (beta) approach” (Id at 21), but does not explain the methodology used to derive

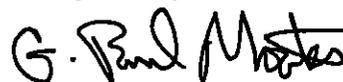
¹ AAR’s February 22, 2007 “post-hearing filing” consisted of literature critical of the CAPM methodology that had been expressly requested by Commissioner Mulvey during the February 15 hearing in Ex Parte No. 664

² Use of the Thomson/IBES data is consistent with the Board’s past practice in its annual cost of capital determinations. Moreover, although the minimum number of forecasts upon which the IBES sample average was based was four (and not three, as stated at p. 11 of Mr. Rockey’s statement attached to AAR’s opening Comments), in 90% of the cases, the number ranged from five to six

those values or propose alternative earnings estimates to be used in the calculation directed in the Board's order establishing this proceeding. In other words, WCTL suggests that cost of capital and growth rate calculations made using the differing methodologies of the type it has advocated in Ex Parte No 664 generate different results from those using the approved methodology employed to generate the results in AAR's opening Comments -- not that the calculations performed by AAR in accordance with the Board's approved DCF methodology were incorrect. In the meantime, WCTL offers nothing with respect to AAR's opening Comments in the instant proceeding, including the calculations made pursuant to the procedures specified by the Board's May 16, 2006 Decision, that warrants any further response.

As explained in AAR's opening Comments, the Board should determine that the railroads' cost of capital for 2006 is 13.6 percent

Respectfully submitted,



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Counsel for the Association of American Railroads
and Member Railroads

August 9, 2007

CERTIFICATE OF SERVICE

I hereby certify that on this 13th day of August, 2007, I caused a copy of the foregoing Rebuttal Comments of the Association of American Railroads and Its Member Railroads in Ex Parte No. 558 (Sub-No. 10), "Railroad Cost of Capital – 2006" to be served on all parties of record in this proceeding by first class mail, postage prepaid or more expeditious method of delivery.

Matthew Wolfe

Matthew Wolfe