



ASSOCIATION
OF AMERICAN
RAILROADS

John T. Gray
Vice President - Policy & Economics

March 28, 2008

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

Re: Ex Parte No. 290 (Quarterly Rail Cost Adjustment Factor)

Dear Ms. Quinlan:

This amended submission is the AAR calculation of the Rail Cost Adjustment Factor using the newly available revised productivity information served by the Surface Transportation Board (STB) in the above proceeding served on March 28, 2008 ("Decision"). The AAR originally filed its forecast of the second quarter 2008 All-Inclusive Index and Rail Cost Adjustment Factor in this proceeding on March 5, 2008. The Decision affects only two numbers in the AAR's original filing, the Productivity Adjustment Factor and the RCAF (Adjusted). The RCAF (Adjusted) still rounds to the same number as filed before, so the only changes involve productivity factors.

	<u>2008Q1</u>	<u>2008Q2</u>	<u>% Change</u>
All-Inclusive Index	103.5	106.1	2.5
Preliminary RCAF	1.035	1.061	2.5
Forecast Error Adjustment	0.015	0.016	
RCAF (Unadjusted)	1.050	1.077	2.6
Productivity Adjustment Factor	2.1618	2.1683	
RCAF (Adjusted)	0.486	0.497	2.3
PAF-5	2.2763	2.2859	
RCAF-5	0.461	0.471	2.2

The Decision contains a different Output Index for 2006 compared to the original decision served February 22, 2008, which causes a different five-year moving average to be calculated. The Decision also states "... the cost recovery procedures have required that the quarterly rail cost adjustment factor (RCAF) be adjusted for long-run changes in railroad productivity. The ICC Termination Act of 1995 continues this requirement (49 U.S. C. 10708, as revised). The long-run measure of productivity is computed using a 5-year moving geometric average." Since the Decision states that the productivity adjustment is to be based on a geometric average, the calculations herein use the STB's five-year moving geometric average as found on the second page of the Decision, and also found under Table B of the Decision.

It should be noted that the Decision explicitly states that the productivity adjustment is to be based on a geometric average. However, the Decision twice refers to an "average" that is arithmetic. (The arithmetic average in ratio format is 1.013, while the geometric average is 1.012.) The fourth paragraph of the Decision states that the STB "will adopt 1.013 (1.3% per year) as the measure of average change in railroad productivity." The fifth paragraph of the appendix states that the "growth in productivity over the period 2002-2006 is 1.013 (1.3% per year)."

AAR is concerned that use of the arithmetic average in these two places of the decision could inadvertently create confusion as to the proper measure to be used. While the use of either average in the present instance will result in the same RCAF-Adjusted, AAR is concerned that the reference to the arithmetic average in the two places in the Decision could create confusion as to the proper average to be used in subsequent RCAF calculations. Accordingly, it is suggested that the Board clarify that an arithmetic average should not be used for RCAF calculations.

AAR's submission herein consists of this two-page letter, AAR's Productivity calculation, and AAR's Rail Cost Adjustment Factor calculation. AAR's original filing is not otherwise affected by the Decision or the present submission. Questions should be directed to the undersigned or Clyde Crimmel (202 639-2309) of this office.

Sincerely,

A handwritten signature in black ink, appearing to read "John T. Gray", with a long horizontal flourish extending to the right.

John T. Gray

Attachments

Productivity

Amended 3-28-08

Since 1989, the cost recovery procedures have required that the quarterly rail cost adjustment factor (RCAF) be adjusted for long-run changes in railroad productivity. The long-run measure of the change in productivity is computed using a five-year moving geometric average. On February 22, 2008, the Surface Transportation Board (STB) served a decision in Ex Parte 290 (Sub-No. 4) which added the year 2006 to the Productivity Adjustment Factor (PAF) and deleted the year 2001. However, after a postponement of the effective date, and review of their source data, the STB served another productivity decision on March 28, 2008. The decision calculates a geometric average annual productivity change for 2002 through 2006 of 1.2 percent – a 0.5 percentage point decrease from the 2001 through 2005 average of 1.7 percent. The components of this average annual value are shown on the following table in ratio format – therefore, 1.012 is the same as an increase of 1.2 percent. Productivity changes are calculated by dividing the output index by the input index. The average annual rate is calculated by multiplying each of the five productivity changes together and taking the result to the one fifth power. The quarterly productivity adjustment factors (PAF) are calculated by increasing the previous quarter's PAF by quarterly versions of the annual rate which are the fourth root of the average annual growth rate. The difference between the PAF and the PAF-5 is the timing of the 5-year productivity trend.

Comparison of Output, Input, & Productivity			
2002 - 2006			
Year	Output Index (1)	Input Index (2)	Productivity ¹ Changes (3)
2002	1.012	1.006	1.006
2003	1.039	1.020	1.019
2004	1.033	1.057	0.977
2005	1.021	0.956	1.068
2006	1.018	1.024	0.994
Average			1.012
Previous Average (2001-2005)			1.017

¹ The values shown in Column 3 are based on full float calculations and may not exactly match numbers calculated using the rounded numbers displayed in Columns 1 and 2.

Calculation of PAF and PAF-5			
For 2002-2006, use fourth root of avg. productivity change = 1.0030			
For 2001-2005, use fourth root of avg. productivity change = 1.0042			
Quarter	Year	PAF	PAF-5
Q1	2008	2.1618	2.2763
Q2	2008	2.1683	2.2859
Q3	2008	2.1748	2.2955
Q4	2008	2.1813	2.3051
Q1	2009	2.1878	2.3120

2001-2005

2002-2006

Rail Cost Adjustment Factor Second Quarter 2008

Amended 3-28-08

Four RCAF values are presented in this filing. Two are not modified for productivity (Preliminary RCAF and RCAF Unadjusted), and two incorporate a productivity calculation (RCAF Adjusted and RCAF-5). The All-Inclusive Index and all four RCAF values, plus the percent change for each, are shown below. Note that the All-Inclusive Index is on a 2007Q4=100 basis.

	Previous 2008Q1	Current 2008Q2	Percent Change
All-Inclusive Index ¹	103.5	106.1	2.5
Preliminary RCAF ²	1.035	1.061	2.5
Forecast Error Adjustment ³	0.015	0.016	
RCAF (Unadjusted) ⁴	1.050	1.077	2.6
Productivity Adjustment Factor ⁵	2.1618	2.1683	
RCAF (Adjusted) ⁶	0.486	0.497	2.3
PAF-5 ⁷	2.2763	2.2859	
RCAF-5 ⁸	0.461	0.471	2.2

¹ See All-Inclusive Index on page 3 of original March 5, 2008 filing.

² All-Inclusive Index divided by the All-Inclusive Index in the base period (100.0).

³ The current figure is from Forecast vs. Actual All-Inclusive Index in this filing (page 4). The previous quarter figure is shown in a similar section of the previous quarter's filing.

⁴ Preliminary RCAF plus the forecast error adjustment.

⁵ See amended Productivity from March 28, 2008 filing.

⁶ RCAF (Unadjusted) divided by the Productivity Adjustment Factor (PAF).

⁷ See amended Productivity from March 28, 2008 filing.

⁸ RCAF (Unadjusted) divided by the PAF-5.