

**SURFACE TRANSPORTATION BOARD
OPEN VOTING CONFERENCE
MARCH 21, 2003**

*Texas Municipal Power Agency v.
The Burlington Northern and Santa Fe Railway Company, STB Docket No.
42056*

**STATEMENT OF
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SLIDE 1

Good morning Chairman Nober, Commissioner Morgan.

Five of the cases on the docket today involve challenges to rail rates or the procedures used by the Board to evaluate the reasonableness of a challenged rate.

To set the stage for a discussion of these cases, I thought it would be helpful to first briefly discuss the two main parts of a rail rate proceeding.

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Before the Board can examine the level of a challenged rail rate, the statute requires the agency to find that the railroad has market dominance over the challenged transportation.

The statute defines market dominance as an absence of effective competition from other transportation alternatives.

There are two parts to a market dominance analysis.

In the qualitative assessment, the Board examines whether there are transportation alternatives available to the complaining shipper and whether those alternatives are effective in placing competitive pressure on the railroad's pricing.

In the quantitative assessment, the Board computes the railroad's variable cost of providing service to determine whether the rate being challenged generates revenues that are more than 180% of the railroad's variable cost.

Only when the Board finds that there are no feasible transportation alternatives and that revenues generated by the transportation exceed the variable cost of providing service by 180% can the agency evaluate the reasonableness of the rate.

SLIDE 3

The Board's constrained market pricing principles provide the framework for evaluating rates. C-M-P- seeks to determine what a railroad would need to charge to cover its costs under "honest, economical and efficient management." To ensure that rates reflect this statutory requirement, C-M-P- allows the shipper challenging a rate to identify costs associated with operational inefficiencies and cross-subsidies so that it will not have to pay for such inefficiencies or subsidies.

Under C-M-P- a shipper can focus on the financial health and requirements of the existing railroad to show that the rate the shipper is being assessed is not justified.

Alternatively, the shipper has the option of showing that a hypothetical railroad (designed specifically to serve the shipper) could offer lower rates to the that shipper while still covering all its costs. This procedure is the stand-alone cost test, which most shippers have opted to use when challenging a rail rate.

In S-A-C- cases, the revenues that would be earned by the S-A-R-R- from all of the traffic it would transport over a 20-year period are compared to the costs the S-A-R-R- would incur over that same period. If the revenues projected exceed the costs that are calculated, then the rate is too high, and a rate reduction and reparations are ordered. In making these calculations, there are hundreds of subsidiary issues that arise between the parties on all sorts of matters: issues about how you figure out the costs of the movements, how the S-A-R-R ought to operate, how much it would cost to build the S-A-R-R, and how much revenue the S-A-R-R could get. These issues are highly contested by the parties, and individual issues can have a ripple effect through the whole analysis.

With that introduction, I'll turn the presentation over to Rachel Campbell, who will discuss the first rate case on the agenda.

SLIDE 6

This is a rate complaint brought by the Texas Municipal Power Agency (TMPA) challenging the rate charged by the Burlington Northern and Santa Fe Railway Company (BN) for moving unit trains of coal in railroad-owned cars from mines in the Powder River Basin to a TMPA power plant at Iola, TX. In addition to challenging the level of the existing rate in railroad-owned cars, TMPA asks that BN be required to established a second rate for movements of coal in shipper-supplied cars.

The draft decision finds that under existing case law BN is not required to provide service in shipper-owned cars, so long as it can meet its common carriage obligation by moving TMPA's coal in railroad-supplied cars. Because BN is not required to use shipper-owned cars, it is not required to provide a rate for that service.

The draft decision also finds that BN has market dominance over TMPA's traffic and that, based on the S-A-C- test, the challenged rate is unreasonably high.

SLIDE 7

As discussed in great detail in Appendix A, the draft decision concludes that the challenged rate generates revenues for BN that exceed 180% of BN's variable cost of providing service to TMPA with respect to 2 mines. For 2 other mines, from which TMPA seeks a rate prescription but from which no traffic has moved, there simply was no data available to make a quantitative determination.

In addition, the draft discusses why the evidence did not support a conclusion that TMPA has any effective transportation alternatives to BN. Specifically, based on the facts here, it rejects a potential build-out option as an effective competitive constraint on BN's pricing in this case.

In light of these findings on market dominance, the draft goes on to evaluate the reasonableness of the rate using the S-A-C- test proposed by TMPA.

MAP

In this case, TMPA designed a hypothetical 1,600 mile S-A-R-R stretching from the Powder River Basin of Wyoming to Iola, TX, where TMPA's power plant is located. The route of the S-A-R-R is shown on the screen in blue and would, for purposes of the S-A-C- test, replace the existing BN line.

The line in red on the screen is another BN line that the S-A-R-R would not replace.

In its S-A-C- presentation, TMPA would hypothetically reroute some BN coal traffic that currently moves over the red line so that the S-A-R-R- could move that traffic over the blue line.

BN objects to the rerouting, arguing that the S-A-R-R could not use a different route from that specified in contracts governing the movement of the traffic.

The draft finds that the language of a contract by itself is not an impediment to the rerouting proposal. Indeed, it is well established by prior cases that the existence of a contract does not bar the S-A-R-R- from assuming that it would handle the traffic.

Thus, for traffic for which the S-A-R-R- would fully replace the service provided by BN, the draft concludes that rerouting is permissible. That would be the case for the movement to the Big Brown power plant, which now moves from the P-R-B down the red line and back over to the blue line at Dallas/Ft. Worth. Because the S-A-R-R could handle that traffic from origin to destination, the draft would accept TMPA's rerouting.

However, for traffic for which the S-A-R-R- would only replace a portion of the transportation service provided by BN, the draft concludes that a rerouting which would necessarily change how the traffic is handled beyond the S-A-R-R has not been supported.

In this case, the draft rejects TMPA's proposal to reroute traffic from the red route to the blue route where that rerouted traffic would have to be interchanged at Iola for movement to various plants at the southern end of the red route.

The draft explains that TMPA failed to account for many of the costs and operational problems that BN would encounter by moving the interchanged traffic through Houston, a very busy rail area that BN now largely avoids by moving much of the traffic over the red route.

SAME MAP

ISSUE: Cross-Subsidy

As in the PPL case just discussed, here BN questions whether the portion of the S-A-R-R south of Madill, which is just north of the Texas/Oklahoma border on the map, would have sufficient traffic to pay for the cost of constructing that segment of the line.

The draft explains that even after rejecting some of TMPA's rerouting assumptions, the line south of Madill would have enough traffic to justify construction of that portion of the line and, therefore, that BN has failed to show that there is a cross-subsidy inherent in TMPA's S-A-C presentation.

SAC ANALYSIS

In addition to the rerouting and cross-subsidy matters, the draft discusses a multitude of the more typical sorts of issues concerning what it would cost to build, operate and maintain the hypothetical rail system that TMPA has designed and what revenues would be available to the S-A-R-R from the traffic that it is designed to serve.

As in other S-A-C cases, the draft decision uses TMPA's evidence on some issues, BN's evidence on some issues, and a blend of the two on yet other issues.

The design of the S-A-R-R- is discussed in Appendix B while the costs to build and operate the system are discussed in the rather lengthy Appendices C and D. In addition, the decision discusses the revenues that would likely be available to the S-A-R-R- for the years 2001-2020.

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After all of the costs and revenues have been quantified, the draft concludes that, over the full 20-year period, there would be a net over-recovery of \$208 million, in present-value terms. The way the analysis works out, the S-A-R-R would need to reduce its rates for the traffic it would carry by varying amounts in the years 2001 through 2011— by 4.4% in 2001, by 5.5% in 2002, and then by lessening amounts, until the rate reduction is phased out by 2012. And BN would be required to reduce its rate to TMPA by these same percentages and to pay reparations on traffic that has already moved under the challenged rate.

From the record, we know only the amount of traffic that moved under the challenged rate for the last 9 months of 2001. On this traffic, BN would owe about \$1.2 million in reparations. The draft also directs the parties to compute the amount of additional reparations due on traffic that moved since the beginning of 2002 as the information becomes available.

Finally, I'll point out that while the draft would reduce the challenged rate, it does not require BN to reduce its rate all the way to the statutory floor of 180% of the variable cost of providing service.

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That completes my presentation. We will be happy to answer any questions that you may have.