

20 MR. LOFTUS: Thank you, Chairman Nober.  
21 Good morning, Vice-chairman Mulvey. Good morning,  
22 assembled staff.

1 I am appearing this morning on behalf of  
2 Complainants Arizona Public Service Company and  
3 Pacificorp.

4 I want to advise the Board that  
5 representatives of both of those companies are here  
6 this morning to observe these proceedings.

7 With me at counsel table is Peter Pfohl of  
8 our firm who has assisted in the development of this  
9 case.

10 I have advised that we would like to  
11 reserve five minutes of our time for rebuttal.

12 In this reopened proceeding, each of the  
13 parties, the Complainants and BNSF went back to the  
14 Board's 1998 DCF analysis and they made revisions to  
15 that analysis in the limited areas that the Board  
16 allowed the parties to address in this reopened  
17 proceeding. The most consequential issue by far in  
18 the case is the question of BNSF's proposed revenue  
19 adjustment to the DCF analysis.

20 BNSF claims that there is a conceptual  
21 flaw in the analysis submitted by Complainants. They  
22 identify that flaw as a failure to take account of the

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1 prescribed rate levels during the elapsed portion of  
2 the DCF period. Now when I refer to the elapsed  
3 portion or the historical period, I'm referring to the  
4 period January 1, 1994 until the date of reopening,  
5 which was in May of 2003.

6 The supposed flaw, I want to point out, is  
7 not in the revenues that the Complainants used in the  
8 DCF analysis. In fact, both Complainants and BNSF  
9 assumed the same revenues in the analysis for purposes  
10 of determining whether stand alone revenues exceed  
11 stand alone costs. For the traffic moving from  
12 McKinley to Cholia and to the Coronado station.

13 The supposed flaw doesn't relate then to  
14 the revenues, nor does it relate to the costs i.e.,  
15 not to the inputs of the DCF analysis. Rather, it  
16 relates to the application of the percentage reduction  
17 methodology through which the Board in its  
18 prescription in 1998 and since has determined how the  
19 excess revenues for the stand alone system are spread  
20 over the stand alone traffic group to generate the  
21 maximum rates. That is where the supposed flaw  
22 occurs.

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1           BN says that because the new maximum rate  
2           levels under the Board's percent reduction methodology  
3           for the elapsed period are higher than the maximum  
4           rates prescribed by the Board in 1998, an adjustment  
5           must be made. That adjustment is made by first  
6           calculating the present value difference between the  
7           new maximum rate levels and the old maximum rate  
8           levels for the tons that move during the elapsed  
9           period. In other words, the first step is to  
10          calculate the value of the additional monies BNSF  
11          would have earned from the traffic moving during the  
12          elapsed period if the Board had prescribed the rates  
13          that are generated by the DCF analyses now in  
14          evidence.

15                 In short, it is a calculation of  
16          reparations. The next step in BNSF's adjustment is to  
17          calculate the additional amount that should be added  
18          to prescribed rate levels for traffic moving from May  
19          2003 through the future period ending with closure of  
20          the McKinley mine.

21                 This adjustment, we believe, must be  
22          rejected by the Board for multiple reasons. But

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1 before I address those, I want to make one point at  
2 the outset and that is that we believe the only reason  
3 that the new maximum rates are higher than the  
4 original maximum rates is because the Board improperly  
5 limited the evidence with regard to the impacts of  
6 changed circumstances on the stand alone cost  
7 analysis. We've made that point before. I just make  
8 it for the record now. We believe if all relevant  
9 change circumstances had been considered, the new  
10 maximum rates would be below the old maximum rates.

11 Turning to the reasons why this adjustment  
12 must be rejected, we first start with the fact that it  
13 is well established law this agency may not order  
14 payment of amounts beyond the original prescribed  
15 rates for traffic that moved before May 2003. In the  
16 Arizona Grocery case, the Supreme Court ruled that the  
17 ICC could not retroactively change a prescribed rate.  
18 As you know, the fact pattern there was the ICC had  
19 prescribed a rate level, a few years later, it  
20 prescribed a lower maximum rate level and it awarded  
21 reparations on the difference between the higher  
22 original prescription and the subsequent lower

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1 prescription. And the Supreme Court ruled, and I  
2 quote, that the ICC did not have the power to  
3 "retroactively repeal its own enactment as to the  
4 reasonableness of the rate it prescribed."

5 Now, in the Arizona Grocery decision,  
6 the Supreme Court actually addressed specifically the  
7 claim that BNSF presents here. It said, "If that  
8 body," then the ICC, "sets too low a rate, the carrier  
9 has no redress saving new hearing and the fixing of a  
10 more adequate rate for the future. It cannot have  
11 reparation from the shippers for a rate collected  
12 under the order upon the ground that it was too low."  
13 That is precisely what BN is attempting to do here.

14 We believe that not only does Arizona  
15 Grocery directly preclude the adjustment that BN seeks  
16 to make, the Board's own decision reopening the case  
17 also does so. In that decision, the Board said that  
18 the lawfulness of the rates approved and prescribed in  
19 our 1998 reopening cannot be challenged with respect  
20 to traffic that moved from 1997 until now. There is  
21 no question that that is what the BN's adjustment is  
22 focused on. I quote from BN's brief. "APS

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1 Pacificorp's payment of the originally prescribed  
2 rates in the elapsed years of the DCF period resulted  
3 in a revenue shortfall for those elapsed years." That  
4 is what they're seeking to recover through this  
5 adjustment.

6 Now, they claim that this is not a  
7 recovery of reparations, and the reason why, which  
8 they explain at page 8 of their brief, is that if this  
9 were a reparations award, it would be an amount  
10 certain, including interest, that would be paid to  
11 them. But what they propose is different. The  
12 amount, which depends on the actual amount of traffic  
13 that moves from the date of reopening forward, may be  
14 different from the amount of reparations. And this  
15 they say is a sufficient distinction to make Arizona  
16 Grocery inapplicable.

17 We have three responses to that argument.  
18 First, this adjustment is a prohibited recovery of  
19 reparations for past shipments. It is precluded  
20 regardless of its precision. There cannot again be  
21 any question about the fact that these monies are for  
22 the historic shipments.

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1           Second, this reopening is designed to  
2 achieve the most accurate calculation of future  
3 tonnage possible within the confines of the limited  
4 areas the Board has allowed to be addressed in  
5 evidence.

6           Third, the payment of reparations by check  
7 now would be less expensive, in all likelihood, to  
8 Complainants than recovery over future time periods as  
9 proposed by BNSF, and that is because of the interest  
10 rates that would apply to the reparations amount when  
11 contrasted to the impact of the cost of capital  
12 discount rates that are utilized in the DCF formula in  
13 determining how much needs to be recovered in future  
14 years to make up for the shortfall they posit in the  
15 elapsed period. In other words, we think BN's  
16 reparations recovery will be greater under this  
17 adjustment than they would be if you just forced us to  
18 write a check today.

19           BN's adjustment also violates contractual  
20 arrangements between the parties. In January of 1999,  
21 Complainants and BNSF entered into a memorandum of  
22 understanding concerning rail transportation to

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1 Cholla. Pursuant to that MOU, they subsequently  
2 entered into a rail transportation contract. Each of  
3 those documents has been submitted into evidence and  
4 we have provided each Board member a copy of those two  
5 documents for convenient reference at this time.

6 And if I could ask you to look under tab A where we  
7 have -- I should add for the? Chairman Nober and Vice-  
8 chairman Mulvey, the BN was aware that we were  
9 presenting these in this fashion and we're dealing  
10 with highly confidential documents. I can't read them,  
11 so what we've done is to box the language we're  
12 referring to in connection with a specific point and  
13 direct your attention to it.

14 At page 4 of the MOU with the red tab  
15 designated with an "A" and at page 5 of the contract  
16 at the red tab where we have designated with an "A,"  
17 we believe it is very clear these documents resolve  
18 all issues relating to the rates that would be paid  
19 for the transportation rendered under the contract  
20 from January 1, 1999 through December 31st, 2002, a  
21 four-year period. And we believe those pieces of  
22 these documents make that very clear.

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1           As contract rates, the Board has no  
2 jurisdiction over those rates that were paid on that  
3 traffic that moved during that period. And yet,  
4 having agreed to accept those monies for that traffic,  
5 the BN is here today asking for more money for that  
6 very same traffic in the form of its adjustment that  
7 it proposes be added to the prescribed rates for the  
8 future.

9           A separate point: BN waived its right to  
10 seek any reopening of this case before 2003. In the  
11 first place, after the Board's decision on reopening,  
12 BN chose not to file a judicial appeal. They then  
13 agreed to enter into this contract that we have  
14 directed your attention to. We have marked with the  
15 blue tab at page 4 of the MOU the language box where  
16 we put the letter "B", and we believe that language  
17 confirms that the BN waived any right to seek  
18 reopening prior to 2003.

19           And here is a very important point. BN  
20 made that waiver despite the fact that it very clearly  
21 understood two things. First, the effect of errors in  
22 the traffic volumes and the out years of the DCF would

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1 cause lower prescribed rates in the early years of the  
2 DCF. They understood that perfectly well. They  
3 explained that in their petition to reopen in 1997.  
4 And they further explained that if the Board  
5 subsequently discovered this error, that they wouldn't  
6 be able to remedy it, and I quote from their petition  
7 to reopen: "Even if the Board at some future time  
8 sought to reopen this proceeding to correct an actual  
9 shortfall in the SARS predicted traffic volumes, it  
10 likely would have no ability to remedy its error."  
11 Arizona Grocery.

12 Now, BN has actually received in the real  
13 word revenues greater than the new higher maximum  
14 reasonable rates under Complainant's percent reduction  
15 methodology. They say on their brief, "You must  
16 disregard that fact." They say, "You must disregard  
17 it because that's real world." The reason they  
18 receive greater revenues is that the traffic moving to  
19 Coronado did not actually pay the rates that were set  
20 by the Board. Instead, they paid higher contract  
21 rates. They were not issue traffic in the case. But  
22 if you look at the stand alone traffic group as a

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1 whole, they earned revenues greater than the revenues  
2 that result from these new maximum rates for the stand  
3 alone traffic group. They say, "Can't consider that.  
4 That's real world." And yet, they entire premise for  
5 their adjustment is in the real world they earn less  
6 than the maximum rates that are generated by the  
7 percent reduction methodology. They meet themselves  
8 coming around the corner on that argument.

9 In summary on this issue, Arizona Grocery  
10 and the Board's May 2003 decision directly preclude  
11 BN's proposed adjustment. Second, the adjustment  
12 would violate the parties' contract. Third, BN knew  
13 before entering the contracts that it could not  
14 recover in a subsequent reopening if it turned out  
15 that the prescribed rates were set too low.  
16 Notwithstanding that knowledge, it waived the right to  
17 seek reopening prior to January of 2003. In the real  
18 world, BN's revenues from the stand alone railroad  
19 traffic have exceeded the new maximum rates for the  
20 historic period.

21 I'd now like to turn to another issue,  
22 which is the minimum volume obligation that BN

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1 purports to establish in its common carrier or pricing  
2 authority 90069. That is a minimum volume commitment  
3 of 3.5 million tons per year from the McKinley mine to  
4 Cholia, and that's important. It's not all deliveries  
5 to Cholia. It's from the McKinley mine to Cholia.  
6 They say "must be 3.5 million tons a year." If it is  
7 not, they purport to impose a penalty equal to 100  
8 percent of the rate for every shortfall ton. This  
9 volume obligation we submit is clearly improper.

10 In the first place, in the original case  
11 the rates challenged by the Complainants were subject  
12 to an annual volume of 1.5 million tons. That was the  
13 common carrier tariff that was challenged, 1.5 million  
14 ton annual volume. The Board did not in its '97 or  
15 '98 decisions direct any change in that volume. For  
16 that reason, this 3.5 million that BN purports to have  
17 imposed today is in violation of the Board's  
18 decisions. In addition, the change to the annual  
19 volume is beyond the limited scope of this reopening.  
20 It has not been justified by any evidence that has  
21 been submitted by BN in this case. Even though 2003  
22 volumes were less than 3.5 million tons, if you look

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1 at BN's DCF analysis, you won't see any revenue in  
2 there for shortfall tons. So apparently they did not  
3 even consider it sufficiently realistic that they even  
4 took that into account.

5 Even if a change in the minimum volume  
6 were not improper, the tonnage level they set, 3.5  
7 million tons from McKinley is clearly unreasonable  
8 given the facts relating to this traffic movement to  
9 Cholia. That's particularly true as it applies to  
10 2003 volumes. We've explained in length in the  
11 evidence the circumstances affecting 2003.

12 Finally, it has to be improper to charge  
13 100 percent of the rate if there is to be any sort of  
14 penalty for not meeting a reasonable annual volume  
15 commitment. Charging 100 percent of the rate is  
16 clearly unreasonable and penal, and should not be  
17 permitted.

18 I'd like to turn finally to two relatively  
19 minor issues in the scheme of things, and they relate  
20 first to non-McKinley tons delivered to the Cholla  
21 facility prior to 2007. We have included such tons  
22 because we believe they are proper under the Board's

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1       October decision and May decision on reopening. BN  
2       has taken the position that the only tons moving from  
3       other origins are tons that are moved after closure of  
4       the McKinley mine.

5                       Now the Board in its October 2003 decision  
6       said that the decline in traffic moving over the SAR  
7       from the McKinley mine can be made up for by including  
8       in the SAR replacement coal from the Lee Ranch mine or  
9       even other origins. So a decline to us means a  
10      gradual reduction and that it does not require that  
11      you put off consideration of other tons until the mine  
12      actually closes.

13                      The October decision also says that both  
14      parties may update the record regarding any forecasts  
15      used in the original SAC analysis that have since  
16      proved to be inaccurate. We have explained in the  
17      evidence that one of the reasons additional coal was  
18      used is that there were increases in electricity  
19      demand beyond that forecast in 1997 and 1998 by the  
20      parties or the Board. In short, we think it's proper  
21      to include these non-McKinley tons that moved prior to  
22      1997 in the stand alone cost analysis as crossover

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1 traffic and to consider the revenues associated with  
2 those tons.

3 On non-McKinley tons after 2007, BN raises  
4 two arguments. First, it challenges APS Pacificorp's  
5 projected coal burns on the grounds that they would  
6 exceed an 85 percent capacity factor. We have  
7 explained to you in evidence that their calculations  
8 are incorrect. When you use the correct heat rates,  
9 the capacity factors do not exceed 85 percent at the  
10 tonnage levels we have posited. But even if they did,  
11 achieving those capacity factors would not be  
12 unprecedented or even unusual for Cholia or for other  
13 plants. The Complainant's projections in this regard  
14 are numbers developed in the ordinary course of  
15 business for purposes not related to this case and  
16 should clearly be accepted.

17 BN also challenges certain of Salt River's  
18 coal volume projections. Salt River is not a party.  
19 They provided information pursuant to requests for  
20 discovery subpoenas served upon them and BN took issue  
21 with some of their projections as being speculative.  
22 There is no evidence to support BN's position in that

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1 regard. In fact, Salt River's fuels department  
2 manager testified that the projections were not  
3 speculative, but are its best attempt to model its  
4 future needs.

5 I'd like to make another comment with  
6 regard to the idea of lifting the rate prescription.  
7 BN is the moving party in this case. It seeks the  
8 relief. As such, it has the burden of proving that  
9 that is appropriate. Now, the Board in its decision  
10 on reopening said that because the Complainants were  
11 likely to have better access to information about how  
12 the Complainants might resource their coal  
13 requirements in the face of dwindling supplies from  
14 McKinley, that we should go first and close, and so we  
15 did. But, 49 C.F.R. 1153 and 1154 clearly impose the  
16 burden of proof on BN and that does not change because  
17 of the manner in which the Board directed the parties  
18 to proceed with their evidence.

19 I will stop with my prepared remarks at  
20 this point and be happy to respond to any questions  
21 from the Board.

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