UNITED STATES
SURFACE TRANSPORTATION BOARD

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ORAL ARGUMENTS

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ARIZONA ELECTRIC POWER :
COOPERATIVE, :
COMPLAINANT :

v. :
STB DOCKET No. :
42113

BURLINGTON NORTHERN & :
SANTA FE UNION PACIFIC, :
DEFENDANTS. :

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Tuesday,
September 28th, 2010
Washington, D.C.

The above-named proceeding
commenced at 9:30 a.m., at the U.S. Surface
Transportation Board, First Floor Hearing
Room, 395 E. Street, S.W., Washington, D.C.

before:

DANIEL R. ELLIOTT III CHAIRMAN
FRANCIS P. MULVEY, VICE CHAIRMAN
CHARLES D. NOTTINGHAM, COMMISSIONER

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CHAIRMAN ELLIOTT: Good morning, welcome. Today we will hear oral arguments in the matter of Arizona Electric Power Company Cooperative v BNSF and Union Pacific, STB Docket number 42113.

In an effort to move things along the Board members will not be making opening remarks this morning, but I wanted to cover a few procedural matters before we begin.

We have asked each party to make a short statement of their arguments, and counsel should be prepared to answer questions, from the Board, at any time during your allotted time.

Counsel for Complainant has been allotted 30 minutes total, and is requested to open with 25 minutes, and reserve five minutes for rebuttal.

Counsel for Defendant, BNSF and Union Pacific have been allotted a total of 30
minutes, and have agreed to allocate this time between the two.

Speakers please note that the timing lights are in front of me. You will see a yellow light when you have one minute remaining, and a red light when your time has expired.

The yellow one minute light will be accompanied by a single chime, and the red light, signifying that your time has expired, will be accompanied by two chimes.

Please keep to the time you have been allotted. When you see the red light, and hear the double chime, please finish your thought, and take a seat.

Counsel for BNSF and Union Pacific, please inform the Board before you begin your presentations, the amount of time you have opted for, as between the two of you, so that we may set the timer accordingly.

Additionally, just a reminder to everyone here, please turn off your cell
phones. Counsel for AEPCO, you may now begin.

As noted, you have requested 25 minutes, 20
for an opening, and 5 for rebuttal.

Please step up to the podium,
introduce yourself, for the record, and begin.

Before you get started, one of the issues that
I thought was really important, when I was
looking through the briefs, was the recession
issue, and how that is dealt with.

I noticed that you had used
certain numbers and that Defendants had used
different numbers. And then there didn't seem
like any of the current numbers, where the
traffic has spiked back up, had been used.

And I was just curious, also, to
hear how you thought we should address that,
in this proceeding. That, to me, was one of
the most important issues that I was looking
at going through. Thanks.

MR. ROSENBERG: Thank you, good
morning. I am Robert Rosenberg, of Slover &
Loftus, appearing on behalf of the
Complainant, Arizona Electric Power Cooperative, or AEPCO.

Let me note that, to my left, is Skip Whitley, who is AEPCO's corporate counsel, and is AEPCO's senior official that currently has direct responsibility for AEPCO's coal supply, and coal transportation matters.

By way of brief background, AEPCO is a relatively small, consumer-owned, non-profit rural electrical cooperative. It is directly responsible for supplying power to, roughly, 130,000 homes and businesses, primarily in rural Arizona.

To serve those customers, AEPCO burns roughly 1.2 to 1.5 million tons of coal per year, at its Apache Generating Station, located near Cochise, Arizona.

AEPCO is a classic captive shipper, as coal can be delivered to Apache only by Union Pacific. This rate case, AEPCO's third, marks the latest chapter in
AEPCO's ongoing efforts to obtain reasonable rates for moving coal to Apache.

Let me have projected on the screen, a PowerPoint -- there it is. And I have distributed copies, as well, in case the scale is too small in the screen.

That is a schematic of AEPCO's stand-alone railroad, which may make it easier to follow some of my comments.

AEPCO based its approach, in this rate case, directly on the Board's ruling in AEPCO's prior rate case, as well as other recent Board Orders.

In particular, AEPCO constructs the Vaughn-El Paso segment, and does not use the trackage rights approach, disallowed in AEPCO's earlier rate case.

Otherwise AEPCO utilizes the SAC approach that it proposed, and the Board approved, in AEPCO's prior rate case.

That specifically includes routing the New Mexico traffic via Vaughn-El Paso, and
having the reasonableness of the PRB rates
determined using a SAR that also handles the
New Mexico rates.

Neither aspect of AEPCO's presentation should be particularly exceptional. The coal rate guidelines specifically contemplate, and authorize, rerouting traffic over a longer route, to achieve a common use of density.

That is what AEPCO has done here. To require the stand-alone railroad to replicate the incumbent's operations violates the "least cost most efficient" essence to stand-alone costing.

It also constitutes an impermissible entry barrier. Furthermore, Congress specifies, in the Conference Report to the Staggers Act, that the rate standards for joint rates should be the same as for single line rates.

VICE-CHAIRMAN MULVEY: Let me ask you one question. You are adding this traffic
to Amarillo, which is pretty far to the east of the existing lines.

Is there any limit to how much you can reroute traffic to achieve your traffic densities, or to achieve lower costs? I mean, could you run the thing to South Carolina, for example, then run it back again?

Would that be permissible, theoretically?

MR. ROSENBERG: Well, first let me make clear that the New Mexico traffic does not go to Amarillo, it goes to Vaughn, and then it has --

VICE-CHAIRMAN MULVEY: You are running PRB traffic down there?

MR. ROSENBERG: Right, the PRB traffic does go, it is a modest extension, it reflects desirable densities, and there become, I think, practical limits, and also with limits with divisions, would add additional cost.

So we think that this extension,
here, is well within the realm of reasonableness. And I don't think the railroads have even attacked that element of PRB routing.

COMMISSIONER NOTTINGHAM: Mr. Rosenberg, if I could just follow-up on that point? What is it about Amarillo that is attractive, from your perspective? Is it that it is, also, a major east-west intermodal corridor, so you pick up a whole lot more density? Is that one of the features? What else can you tell us about the attractiveness of picking up Amarillo?

MR. ROSENBERG: It reflects desirable densities, there are higher densities there than along the other routing, and that it utilizes a higher density network, so it reflects least cost, most efficient principles, as contemplated in the coal rate guidelines.

COMMISSIONER NOTTINGHAM: Can you imagine a case where coal traffic is
interposed along a very congested, intermodal, primarily intermodal corridor, which to such an extent, would require the railroad involved to actually build out new capacity to accommodate the proposed coal traffic, having a high density coal corridor, and a high density intermodal corridor on limited track capacity, obviously could result in some situations and build out and expansion requirements.

How would those types of considerations, or how should they be factored into the economic analysis of a case like this?

MR. ROSENBERG: Well, the shipper is effectively required to conduct the simulation, the operation, the railroad, using the RTC program.

If the RTC program shows that the railroad doesn't provide reasonable equivalent service, then you need to start adding additional facilities in order for the service
to be equivalent, or you look at a different configuration.

And, you know, we submitted an RTC simulation, here, and it shows that our performance is, at least, as good and in most respects better than the incumbent's.

It is also the case here, and typically there is some traffic that the incumbents have that the stand-alone railroad, the shipper decides not to handle, and that is taken into account in the analysis as well.

COMMISSIONER NOTTINGHAM: Thank you.

MR. ROSENBERG: I will continue where I think I was.

The railroads are not allowed to split their joint through-rate into two parts, and require AEPCO to replicate each part separately.

Instead of moving freight from the origins to the Apache destination, in the least cost, most efficient manner, without
entry barriers.

While the railroads claim that AEPCO's SAR involve some sort of cross subsidy, they make no attempt to back up that claim with a PPL Montana, or other Ottertail type analyses, which is the Board's specified standard for determining if the SAR has an impermissible cross subsidy.

Furthermore, about two thirds of the SAR route miles that are used to handle the New Mexico traffic, are also used to handle the PRB traffic.

It is, thus, logical and efficient that SAR facilities, used to handle the New Mexico's traffic, are also used to handle the PRB issue traffic.

CHAIRMAN ELLIOTT: Quick question about the PRB traffic. Can the plant, at issue, burn the PRB coal, are you aware?

MR. ROSENBERG: Yes. Some years ago, around the time of AEPCO's earlier rate case, AEPCO invested a substantial sum in a
coal blending facility, at the plant, that enables it to burn a range of coals.

And it has received, it has burnt some PRB coal, it has burnt Colorado coal, it has burnt, you know, it is burning primarily New Mexico coal now.

You know, the coals each have some desirable characteristics, they have some undesirable characteristics, particularly coal, in certain cases.

And the blending facility lets AEPCO mix those coals to achieve an efficient and effective blend.

CHAIRMAN ELLIOTT: Thank you.

COMMISSIONER NOTTINGHAM: Mr. Rosenberg, if I could follow-up on that? Where does your client get its coal currently, or where is it, predominantly, purchase or source its coal over recent years?

MR. ROSENBERG: Well, it has been a mix. Since the most recent contract expired, and AEPCO has been looking at the
railroads' rates, and because of other factors, they have been getting coal from New Mexico.

Prior to that, under the contract, a good bit of the coal came from the Colorado and, also, from the Powder River Basin, as well as in New Mexico.

I think in years past they have taken coal even from Utah, I believe. So it is, you know, it is a function of the markets, and in large part the railroads are in a position to dictate where AEPCO's coal comes from.

AEPCO needs a blend that will work in its plants, and it wants the lowest delivered cost, consistent with that, and the railroad prices are a major input into that.

COMMISSIONER NOTTINGHAM: When AEPCO requested a tariff rate for the Powder River Basin coal, that triggered this complaint, what kind of volume are we talking about, and what was the source?
Was it a specific mine that was up and running, and open, or was it a mine that might have capacity of coal in the future?

The record is a little bit confusing on those points.

MR. ROSENBERG: Okay. My recollection may be a little bit off. But I think there was, initially, a request for Decker and Spring Creek, they are located in Montana, and I think also mines in what is called the Northern Wyoming basin, the mines that are captive to BNSF.

AEPCO also had a request for rates from the southern basin, and also from Colorado. And that is tied up into litigation in Tucson. And that is in New Mexico, one subdocket, so we are not able to prosecute a rate case, as to those rates, at this time.

AEPCO also requested rates from the Signal Peak mine, which is located further north. That mine is coming on-line, it is having some issues getting up to full
capacity.

But that coal has coal characteristics that are very similar to the Colorado coal, or also similar to the coal from the McKinley mine, which is located in New Mexico, and had a higher BTU content, and lower sulphur content and other desirable qualities.

And AEPCO hasn't yet taken coal from that mine. Again, there is not a lot of coal that is available for third party purchases, but there stands to be, over time. The way AEPCO designed its stand-alone cost presentation, it doesn't build out to that mine, to allow service to begin from there until 2012.

COMMISSIONER NOTTINGHAM: How does that work? You mentioned that the Signal Peak is not on-line, as having some "issues".

MR. ROSENBERG: Well, if I could -

COMMISSIONER NOTTINGHAM: I mean,
we are trying to work here, to resolve, hopefully, a very real and significant commercial dispute.

And I'm worried that part of the dispute might involve something somewhat hypothetical. Not the SARR, that is fine, that is the hypothetical part of the case that is, obviously, built into our process.

But a mine that is not actually ready to produce coal, to be delivered, you request a rate for that. What if the railroad had said, we can't give you a rate until we learn more about the mine's operating availability, and whether they are open for business?

Would, I mean, would you still be here complaining about that rate? It sounds somewhat a little bit speculative to me. And I know your client has to plan for the future, you can't just wait until you are a week away from running out of coal.

You have to be lining up new
sources in the future, I understand that. But help me understand and get a little more comfortable with the Signal Peak situation.

MR. ROSENBERG: Okay, well it is not -- I don't think the situation is nearly as speculative as your questions might indicate.

The mine is operating, BNSF is hauling coal from that mine. It hasn't hit, I think, the 10 million tons a year that is the -- that is what is projected.

But a lot of money has been invested, the mine is operating, I think there is coal that is going to First Energy in Ohio, who was the big investor in the mine.

We did request a rate, we did get a rate. You know, we would be able to, you know, if we entered into a contract we would be able to ship it now.

In part because of the arrangements we entered into, AEPCO entered into when the rate case was starting, based
upon the coal market conditions at this time.

And some of this is, you know, is frankly of a highly confidential nature, and I don't want to be disclosing all the details. It is explained in our evidence.

AEPCO doesn't anticipate, if things happen, if there are force majeure events, if production doesn't occur, AEPCO may take the coal before then.

But it becomes, you know, more and more of a material need, starting in 2012. And, again, we do have the rate, and there is coal that is moving, that BNSF is handling, that moves from that mine to other destinations.

COMMISSIONER NOTTINGHAM: Okay. And just to finish this line, and I want to let you get back to your time. But what type of volumes are we talking about?

Did you order a car load or two for a test burn, or was this a request for unit train service of coal over a long period
I'm trying to understand the type of transaction we are talking about here.

MR. ROSENBERG: Okay. AEPCO has had at least two trainloads, I believe, from the Decker Mine. Again, AEPCO has stockpiled, until the time that it is, from when this earlier contract was in effect, coal from McKinley and also coal from Colorado, that is very useful to AEPCO operationally.

So there have been trainloads. There may be more before its current New Mexico contract runs out, depending on production, depending on burn levels, and those factors.

COMMISSIONER NOTTINGHAM: So there have been two trainloads delivered from the Decker mine?

MR. ROSENBERG: I believe so, yes.

COMMISSIONER NOTTINGHAM: Any other trainloads delivered under this tariff from the Powder Basin mines?
MR. ROSENBERG: Not, I don't believe so. I could be off by a trainload or two, but I think that is correct.

COMMISSIONER NOTTINGHAM: These would be unit trainloads? I mean entire trains.

MR. ROSENBERG: Yes, it is a unit train that goes up there, it comes back, then it heads someplace else.

COMMISSIONER NOTTINGHAM: Thank you.

VICE-CHAIRMAN MULVEY: Commissioner Nottingham makes a point that SAR, after all, is a hypothetical railroad, we deal in hypotheticals.

But it strikes me that there should be some attempt to show that the railroad that you propose, the SAR, should have some semblance to a real world operation. I have a question as to whether the SAR that is proposed to be constructed has 24 interchanges and, yet, it doesn't have any
switches built into it.

You would expect the SAR to be interchanging traffic with connecting carriers. But the assumption is that there really aren't any, that it is basically a bridge carrier.

How are we supposed to look at the SAR that you have created it and consider it a kind of real world operation?

I mean you, for example, use the URCS cost of the Defendant, which is based upon coal traffic. And yet your SAR will carry mostly intermodal traffic, unless I'm mistaken.

So could you reconcile your SAR with real world operations, and why we should accept that SAR?

MR. ROSENBERG: Well, the SAR reflects the facilities that AEPCO utilizes, and AEPCO is a unit train shipper. It also reflects other traffic, grouped together, consistent with the coal rate guidelines.
You know, to serve AEPCO you don't need to switch individual car loads. The segments that AEPCO utilizes handle New Mexico Vaughn train loads, and AEPCO basically captures, in its SAR the facilities that are needed to handle its traffic, and other third party traffic that is efficient and cost effective.

You mentioned the 24 interchanges. I think a number of those are probably the coal mines, and that points where it interchanges with other carriers.

But it does have the interchanges where it takes trainloads intact, and moves them on. That is the portion of the system that AEPCO utilizes, to require the SAR to engage in individual trainloads, and other sorts of things, is to require AEPCO to have to cross-subsidize the Defendant's other traffic.

And the grouping principle is, the coal rate guidelines say that that is key to
contestable markets. And that is what a railroad is built around.

If you go down to, say, where the power plant is at Cochise, Arizona, and you look at UP's main line, you will see all of these large trains moving past it, and moving to or from El Paso, and then moving up to Vaughn.

That is the traffic in the area, that is the traffic that AEPCO incorporates, and that is what the coal rate guidelines say to do. That is what contestable markets say to do.

To require AEPCO to take on other things, is to impose an entry barrier, and to undermine the least cost, most efficient principle.

VICE-CHAIRMAN MULVEY: Thank you.

CHAIRMAN ELLIOTT: Would you mind -- I know you have been peppered with questions since you got out of the box.

But I'm still very curious about
how we are going to deal with the recession.
And my understanding is that you received some
data, pre-recession, you have done your
numbers, and then the railroad came along and
made some adjustments for the recession.

There are some arguments that
there might have been some cherry picking.
And then, also, there is another argument that
the recent uptick in numbers have not been
addressed.

And what I'm concerned about, you
know, if we keep going along, and along, that
this case could drag out farther.

And I was wondering, I mean,
obviously the recession occurred. What is
your idea of the best way to deal with those
numbers, the uptick and, obviously, the pre-
recession good numbers?

MR. ROSENBERG: Well, let me
contrast what AEPCO did with what the
railroads did. What AEPCO did is, of
necessity, we worked with the data and the
forecast that the railroads provided, as well
as other publicly available data.

The last complete set of data that
the railroads provided, went through the first
quarter of 2009. That is what we worked from
in devising our traffic route.

And then we used a combination of
railroad forecasts and other public
information, to forecast what would happen.

And, you know, that shows a
decline in 2Q through 4Q '09. And we reflect
that. And then we use the original forecast
that we put together, as adjusted for, you
know, certain technical errors, and certain
additional information provided, of a
different sort.

What the railroads purport to have
done, is to have selected their own traffic
route, including the earlier data, but also
data from 2Q '09 through 4Q '09, which is more
recent, except that they did not provide that
data in a complete manner, they didn't put it
in the record.

So they put together a traffic route but we, frankly, don't have the data to see what is in it, and what is not in it. However, from what we can discern, it is incomplete.

It was selected in a manner that truncated our traffic route selection, and it doesn't take into account when, you know, to a full extent when traffic moves, you know, it switches to move from a different origin to the same destination, or from the same origin to a different destination, or involves new origins, or destinations.

That is part of the flexibility, that reflects the operation of the market. And their analysis truncates that. And other examples, they tried to get something similar to our traffic route, but they say they have taken the case of the BNSF non-coal trains. They do it by the train symbol. But they include a train symbol only if 90
percent of a particular train symbol was included in AEPCO's traffic route.

So, for example, if AEPCO included 89.6 percent of trains with a certain symbol, they discard those trains altogether. So they end up with a different traffic route.

And, again, they didn't produce the data, so we can't tell what is in it. Again, AEPCO went on a train by train basis, deciding which trains to include, which trains not to include.

For example, if the train had an external reroute, AEPCO would exclude that train. You know, everything suggests that the railroads didn't engage in that process, they engaged in something more simple, more arbitrary, and that yields a more favorable answer to them.

But even if they had done it properly and, again, our position is that they didn't, they simply took the favorable data that was available to them, in this case data
showing 2009 decreases, but they ignored more recent data, and you can, you know any of the Wall Street analysts, things showing the increase in double digits, double digit increases in traffic, in 2010.

So they engaged in this selective updating, which is asymmetric, and unfair. And our point is that if they took all the evidence, into account, it would show our initial forecast as reasonable, and even conservative, particularly looking at how the railroad's volumes, revenues, and profits are recovering.

VICE-CHAIRMAN MULVEY: I have a procedural question. You mentioned the construction of your traffic group. And I gather that you were not happy with the discovery process, that you felt that BNSF was too slow, or didn't give you all the information you needed to build your traffic group.

Is that correct? And, if so, why
didn't you petition the Board for a motion to compel, so that they would have to give you the data, if you thought that their responses were insufficient?

MR. ROSENBERG: Okay. We got enough data to work from, from the 2Q '08 through 1Q '09 period.

What our objection is, primarily, in our evidence is to the railroads' effort to rely on the 2Q through 4Q '09 data, that hadn't been provided to us previously, and they did not provide it in their work papers.

As a consequence we could not work from it. Frankly, if they had done it, then in order to select, you know, to devise our traffic route, we would have had to have done what we did with the initial evidence, which was to go trainload by -- we would have to go car by car, train by train, and assemble a whole new traffic route.

That would take a number of additional months. We couldn't have done it.
in the initial procedural schedule, it entailed enormous expense.

And then after we did that, then the railroads would claim that it was a new traffic route, they would want to put in some sort of rebuttal, and then we would have to respond to that.

So we would be in this perpetual game of catch-up, and it would endanger our, or the Board's ability to comply with the three year deadline.

I will also say that discovery never goes as smoothly and as quickly as we would like in a rate case. But our objection here is to their, you know, selective use of data that was not even put into the record.

But it is clear that they didn't use the sort of process that the shipper is required to utilize.

VICE-CHAIRMAN MULVEY: Thank you.

Over the past six years, I have noticed that the discovery process doesn't always go
I want to point out that the members had some questions prepared by staff. I have seven pages of questions in front of me, and I was just wondering if the Chair would want to continue a little bit longer on this, because there is so much to ask.

CHAIRMAN ELLIOTT: Sure, I know.

Commissioner Nottingham has questions, also.

COMMISSIONER NOTTINGHAM: Is it fair to say that we will have the opportunity to ask questions as --

CHAIRMAN ELLIOTT: He is going to come back on rebuttal.

COMMISSIONER NOTTINGHAM: I have one follow-up on that point. We, obviously, take very seriously, here at the Board any assertion that a party has withheld information during discovery.

And I know, I assume that we have many practitioners observing this proceeding, and I want to make sure they all know that if
you are ever in a dispute, pending before the
STB, and you think another party is not being
forthcoming discovery, what you do is you
reach out to the Board and file the
appropriate motions to compel that
information, if you think it is actually
important to your client.

In this case I'm hearing that
maybe you felt it wasn't important because you
had already made up your mind that there was
one time period that you wanted to capture for
your base period, because, perhaps, it
reflected a peak, economic peak level of
traffic. And no matter what the other
parties, or the Defendants provided or didn't
provide in the way of more recent data, that
wasn't of use to you.

And so I guess what I'm asking you
is why are you complaining about that, if you
had no intention of using the contemporaneous,
more recent data that the railroads, at least
in part, provided?
MR. ROSENBERG: I'd like to -- I'm forced to take issue with your characterization. Once we had finally gotten a complete set of data that we could work with, that includes revenue tapes, it includes train movement, it includes car data.

And we need to take it apart, put it together, and assemble. We had gotten the data through 1Q '09. That gave us a complete set, and we started working with it.

It takes a considerable period of time, and we put our evidence in, and I think it was, I think it was January of 2009, and we worked, as quickly as we could, putting the data together.

Also doing the RTC simulation. That was timely with what we had at the time. It had taken us a good bit of time to get the complete data that we had, and we worked from it in a reasonable manner.

And we had complete data, and we were able to proceed with our case, that had
already been delayed. We are conscious of the three year limit.

The recession did not start in 2009, it started in 2008, and we reflected that data. We relied on things that reflected it. We believed then, and we still believe now, that we had made an accurate estimate of long-term trend.

You know --

COMMISSIONER NOTTINGHAM: Mr. Rosenberg, if I could -- thank you, I think you have responded. I just want to make sure I understand.

Your client got all the data it needed to bring the case that you felt you wanted to bring, is that correct?

MR. ROSENBERG: We got enough data that we could work with comfortably, yes.

COMMISSIONER NOTTINGHAM: Because if you hadn't, if your client was going to be disadvantaged, you would have obviously come to the Board.
You are no stranger to our
process. You would have come and asked for
relief, correct?

MR. ROSENBERG: Well, we try not
to come to the Board unnecessarily. We try to
work with opposing counsel, frankly. And in
most cases we are able to compromise and work
it out.

We have both been through this a
number of times. If we can come to a
reasonable accommodation, we do so. You know,
the objection here is that they put in their
reply evidence, and they don't provide the
data to back it up.

Plus the analysis that they do
does not comport with how a shipper would go
about selecting its traffic route. It is
defective data wise, it is also defective
analytically.

COMMISSIONER NOTTINGHAM: Do you
have that this purported lack of some data is
important enough for the Board to make sure
that we take action to correct and fill out
the record?

Or is this a non-issue? I'm just
trying to understand. You are sort of saying
on the one hand it is a non-issue, because you
were able to bring the case you wanted to
bring.

But then you are saying, on the
other hand, you are actually concerned that
the Defendants allegedly didn't provide all
the information that you might have wished
they had provided.

Do we need to -- what do you
suggest that the Board do about this?

MR. ROSENBERG: I suggest that the
Board look at the evidence that is presented,
and utilize the best evidence of record, which
is our evidence.

I'm certainly not suggesting that
we go through another year, or so, of delay to
have us reassemble a traffic route from more
recent data, and then have three more rounds
of evidence.

    AEPCO is a mid-sized shipper, it doesn't deserve a process like that.

    COMMISSIONER NOTTINGHAM: Thank you.

    CHAIRMAN ELLIOTT: Thank you, Mr. Rosenberg.

    Now counsel for BNSF and Union Pacific, please step up to the podium in the order you have agreed to, introduce yourself for the record, and state the amount of allocated time that you will be using.

    MR. ROSENTHAL: Good morning. My name is Michael Rosenthal, I represent Union Pacific Railroad Company, and I plan to use about 20 minutes of the Defendant's time.

    Mr. Sipe, who represents BNSF Railway Company will use the remaining time.

    I plan to focus on the issues presented by AEPCO's use of a hypothetical interchange point between BN and UP. Mr. Sipe will provide BN's perspective on that issue,
and he will also address the treatment of
Southwestern Railroad, and jurisdictional cost
calculations, and both of us will be happy to
answer your questions on other issues.

We think the central question in
this case is whether AEPCO can base its stand-
alone cost presentation on the premise that
the Defendant's interchange their traffic
somewhere other than the points that are part
of the challenged rates.

We think the answer is no, for two
reasons. First, the answer is no because the
interchange point is an essential part of a
joint rate, and the statute requires the Board
to determine the reasonableness of the actual
rates that carriers establish.

AEPCO's stand-alone cost
presentation is premised on different
interchange points than UP and BN established
for the issue traffic.

So the Board can't determine, from
AEPCO's evidence, whether the challenged rates
are reasonable.

Second, the answer is no because disregarding the actual participation of each Defendant, in the issue traffic, produces a meaningless stand-alone cost analysis.

Rather than address the cost associated with the Defendant's actual responsibilities for transporting the issue traffic, and the revenue available to cover those costs, AEPCO presumed that one Defendant displaces the other for significant portion of the routes.

And as a result its stand-alone cost presentation does not address whether the rates, for the services provided, are reasonable.

Let me try to explain how we get to these points. The tariff governing the New Mexico issue traffic, specifically identifies the interchange point between BN and UP, as Deming, New Mexico.

The tariffs governing the Wyoming
and Montana issue traffic identify the
interchange points as Pueblo, Colorado.

In the real world BN moves the New
Mexico issue traffic east to Belen, New
Mexico, and south to Rincon, and the
Southwestern Railroad, which interchanges the
traffic at Deming with UP.

UP then carries the traffic to the
Atlas Plant and Cochise.

VICE-CHAIRMAN MULVEY:  Excuse me,
doesn't the Board's policies allow the
Complainant to reroute the traffic to create
the most efficient line?

And isn't that what they have
done?  I mean, in their rerouting of traffic,
one would presume it could cause a change in
the interchange points?

MR. ROSENTHAL:  The Board's rules
allow the rerouting of traffic.  But that is
not just what has happened here.

What has happened is the
Complainant, AEPCO, has presumed a change in
the Defendant's responsibilities for handling
the issue traffic. And that brings, with it,
a change in the traffic that can be part of
the issue traffic group.

And that causes a major distortion
in the stand-alone cost analysis. This isn't
simply a question of rerouting the issue
traffic, it is a change in the Defendant's
responsibilities, it is a change in the rate,
and it is a change in the traffic group.

VICE-CHAIRMAN MULVEY: Do you
think the Board needs to be more specific as
to what it is going to call permissible
reroutings, and changes, in creating a SAR?

Or do you think the Board's rules
and regulations right now are fine, and it is
just that you feel that the Complainant has
abused them?

MR. ROSENTHAL: Well, I think the
Board's precedent is clear that rerouting is
one thing, and assuming that the traffic and
revenues of one carrier are available to the
other carrier, when in the absence of some
sort of cost-sharing, or revenue-sharing
arrangement.

I think the Board has
been clear in its precedent where the line is,
and what makes for a sensible cost test. This
case presents the problem in a slightly
different light than in prior cases.

But I think the lines were drawn
by the prior cases, and the precedent is out
there.

VICE-CHAIRMAN MULVEY: Thank you,
that is fine.

MR. ROSENTHAL: I was showing the
routes, and I don't have to go through them.
But what is happening is that we have the real
world interchanges, again, at Deming and at
Pueblo.

And the problem, the reason we are
where we are in this case is because AEPCO
knows what would have happened if it had based
its stand-alone cost presentation on the
actual service provided by the Defendants.

We did the analysis, and AEPCO essentially concedes that if you had done the stand-alone cost analysis, based on the actual routes, the Board would have to dismiss the case.

So essentially AEPCO tries to avoid the result by disregarding the challenged rates. And it is easier to see and understand what AEPCO has done, by looking at a simplified schematic of the routes, which we have prepared.

Essentially, AEPCO developed its stand-alone cost presentation, as though BN and UP interchange all of the issue traffic at Vaughn, New Mexico.

So for the Wyoming and Montana traffic, AEPCO presumed a change in the end point of BN's responsibility from Pueblo to Vaughn. And it used that new end point to justify taking BN's non-issue traffic, moving south of Pueblo, and using that revenue to
offset what are, actually, UP's costs to move
the traffic from Pueblo to Vaughn.

And this BN's non-issue traffic
includes huge volumes of intra-modal traffic,
moving over BN's transcon line, through Vaughn
and Amarillo.

The answer to Commissioner
Nottingham's question about what was so
attractive about Amarillo? But this is
traffic, it is transcon traffic, it is traffic
that in the real world shares no facilities
with the issue traffic.

And it is not actually available
to cover UP's costs to handle the traffic
south of Pueblo. You see, essentially, the
same thing with the New Mexico route.

AEPCO presumed the change, in the
end point of the end responsibility for the
New Mexico issue traffic to Vaughn, and used
the new endpoint to justify taking revenue
from UP's non-issue traffic, moving between
Vaughn and Deming, and using that revenue to
offset what are actually BN's costs to
transport the issue traffic between Billing
and Deming.

And AEPCO tries to defend this by
saying that what it is doing is that it has
just rerouted the issue traffic as permitted
by coal rate guidelines, but as I addressed
this with Vice-Chairman Mulvey, it didn't
simply reroute the traffic.

It presumed the change in BN's and
UP's responsibilities for transporting the
traffic and, therefore, a change in the
traffic and revenue that are available to
offset the costs of the issue traffic.

And so what you ultimately have is
AEPCO's stand-alone cost presentation, that is
based on service the Defendants don't provide,
it relies on traffic and revenue that do not
pay, and cannot be expected to pay for the
costs of the service that are actually being
provided.

And the result is that AEPCO's
stand-alone cost analysis can't be used to address the critical issue in a stand-alone cost case, which is whether the issue traffic is cost subsidizing portions of the Defendants' network that it doesn't use.

And this approach conflicts with the statute, and with the purpose of the stand-alone cost test. The statute recognizes that an interchange point is an essential part of the joint rate.

Section 10703 expressly recognizes that the rate established by the carriers, for intra-line transportation, is applicable to a specific through-out, that the carries established.

And the establishment of the through-out necessarily entails the specification of an interchange point.

So by presuming different interchange points, and the carriers established, AEPCCO is, essentially, asking the Board to regulate non-existent rates.
And under section 10751, the Board's rate -- reasonableness jurisdiction extends only to a rate established by a rail carrier.

Under Section 10704(a), the Board may prescribe a maximum rate, only after it determined that a rate charged, or collected, by a carrier is unreasonable.

And that is not what AEPCO is challenging.

COMMISSIONER NOTTINGHAM: Mr. Rosenthal, if I could ask -- you are arguing about the cross subsidy and the importance of cross subsidy in our analysis.

Are you, basically, arguing that as long as there is no cross subsidy any rate would be valid?

MR. ROSENTHAL: Well, what we are arguing, there are different ways that tests of carriers rates can be constructed within constrained market pricing.

The test that AEPCO chose to
proceed under, in this proceeding, the stand-alone cost test, requires AEPCO to show that Defendants are using its rates to cross subsidize portions of the network that AEPCO isn't using.

So what we are saying is that under the test that AEPCO chose to proceed with, they haven't proven their case.

COMMISSIONER NOTTINGHAM: If I could just follow-up? We get different types of cases, obviously. One recent hearing we had that resulted in actually a settlement, recently, involved the possibility of barge alternative.

How would your analysis on the interchange argument, and maintaining the existing interchange, work if the shipper proposed a barge operation as an alternative to the joint, the joint line rail service?

MR. ROSENTHAL: That is a good question. And it highlights that there are, really, two different issues going on here.
It highlights what the key issue is in this case.

And the key issue is traffic selection, in a stand-alone cost case, and traffic grouping.

And one of AEPCO's points is the Board's rules might allow barge, the Board's rules might allow a Complainant to build a coal slurry pipe line.

But even in that case you would still have the question of what traffic do you include in the traffic group, what traffic is part of this, what revenue should we include?

And just, you know, to take a wild example. If it was a coal slurry pipeline, AEPCO wouldn't be carrying a lot of the intermodal traffic, in this case, that is having a major effect on the rates.

So I think the issue is still there, it is still the one that we are focused on, which is which traffic is part of this case? And what we are saying is that AEPCO,
by rerouting, can't circumvent the Board's usual rule that you can't use traffic and revenues of one carrier, to offset the costs of another, absent some sort of revenue sharing arrangement.

VICE-CHAIRMAN MULVEY: On this interchange point, again, couldn't UP and BNSF simply have offered individual rates to the interchange? So that from A to B is the BNSF rate, and B to C the UP rate?

If the rates are the rule 11 rates, rather than joint rates, could the rates have been separately challenged, and the argument to move the interchange could not be made, is that correct?

You had the option was to have separate rates to the interchange, did you not?

MR. ROSENTHAL: I think that is right. I mean, if you talk about how carriers could react, there are different ways of setting rates under the Board's rules, under
1  10701(c), carriers generally have the
2  initiative to establish any rate that is
3  lawful.
4
5  And, presumably, they could have
6  structured something different that would
7  have, you know, perhaps established, even more
8  firmly.
9
10  Although the tariffs, here,
11  specify the interchange point. And the
12  Board's rules say you have to challenge from
13  origin to destination. So I'm not sure that
14  the practical result would have been
15  different.
16
17  But if what you are saying is the
18  carriers could have made this even clearer,
19  and --
20
21  VICE-CHAIRMAN MULVEY: Had you
22  done that they could not have moved the
23  interchange point, because the rate was to the
24  interchange point, and from the interchange
25  point to the mine.
26
27  MR. ROSENTHAL: I don't think they
can move the interchange point in this case, either. I think the Board's rules are pretty clear, and the statute is pretty clear, that you've got, that the interchange point is part of the rate, and you have to challenge the rate.

And anything else is -- it just gets you into a manipulation of revenues and costs. And, as I have said, the Board has addressed it, it addressed it in the first AEPCO case.

It said that you can't pretend that the revenues of one carrier are available to the other. It goes beyond the creativity that parties are allowed in designing the stand-alone cost railroads, and it distorts the SAC analysis.

It doesn't tell you whether the rate that Union Pacific and BNSF established for this traffic is reasonable. And that is, ultimately, the purpose of this test.

VICE-CHAIRMAN MULVEY: Thank you.
MR. ROSENTHAL: So you know --

yes?

CHAIRMAN ELLIOTT: Mr. Rosenthal,
sorry. Just so that you don't run out of
time, I would be interested in what you are
thinking. I assume that you think, with
respect to the recession, we heard Mr.
Rosenberg's piece, that we assume that you
think that your evidence is the best evidence
of record.

And I did notice, assuming that we
accept it, we take into consideration
recession, in the way you suggest, that there
has been this uptick.

And I'm also very aware of Mr.
Rosenberg's concerns that we don't want to go
through this all again.

Is there any there other
information, out there, possibly that we can
use, to maybe take some of this into
consideration?

MR. ROSENTHAL: Let me just try to
go through this a little more systematically.

CHAIRMAN ELLIOTT: Thank you.

MR. ROSENTHAL: I want to address your concerns. First, both parties recognized that there was a recession, and that the traffic levels in 2009 were less than some early forecasts that were produced, by the parties, in discovery predicted.

Both parties recognized that we were starting with a traffic base that was based primarily in 2008, with the first quarter of 2009.

So both parties tried to make an adjustment. What AEPCO did, and I'm characterizing it, and you can try to follow it in their evidence, it is a bit difficult.

But they looked at what the projections were, this sort of pre-recession projections were. Then they looked at the overall traffic result in 2009, and tried to make an assumption that if the carriers had predicted something pre-recession, you could
apply essentially the same presumptions in reverse to what the traffic would have done given the recession.

And what we said is, we think there is an easier way. We think you can focus on the traffic that actually moved in 2009, look at the actual lanes involved, and see how traffic changed.

So we both tried to make an adjustment. AEPCO seems to have a misunderstanding of what the railroad's tried to do.

We didn't try to select a new traffic route. What we tried to look at were origin and destination pairs that had traffic moving in both periods and say, what happened to the traffic?

We tried to develop an index and scale it up or scale it down. And Mr. Rosenberg says, well, we wouldn't have accounted for new traffic, traffic that wasn't in the first period, but suddenly appeared in
the second.

And in our response is, well that
is true, but we also took out of our analysis
traffic that existed in the first period, and
completely disappeared in the second period.

This isn't perfect. But what we
ended up focusing on were changes in volume
for lanes where there was traffic in both
periods.

It may not be a perfect
adjustment, neither was perfect. But we think
that by focusing on the traffic, and the
lanes, rather than using pre-recession
forecasts, and system average traffic, we
think we got a better estimate.

With regard to post 2009 data, you
know, it is a separate issue. There were
separate data used to project what would
happen in 2009, and what would happen after
2009.

After 2009, again, there were
projections, there were forecasts in the
record produced by the railroads. AEPCO chose one, I don't want to get into highly confidential information, but there were different forecasts with different predictions about the pace of economic recovery.

AEPCO chose one, the railroads agreed with the choice, and we moved on with the case. And whether that forecast, which projected things out a number of years, not just to 2010, but I believe, it may be highly confidential, but for a number of years.

Whether that forecast will prove true, or false, it is much too early to say, it is much too early to say.

CHAIRMAN ELLIOTT: So the railroads actually agreed with AEPCO's approach to the uptick?

MR. ROSENTHAL: The railroads produced several forecasts of what traffic would do. The forecasts were based on post-recession assumptions, when the recession would end, how quickly traffic would recover.
AEPCO picked one, the railroad said fine. So for future projections there was, really, no disagreement about the source of the data.

And for the 2009, both parties recognized that there needed to be an adjustment. The question was, the methodology of making the adjustment.

CHAIRMAN ELLIOTT: But the basis of the assumption, and the basis of the traffic both differ. In other words, BNSF, UP's base, and AEPCO's base, from which the growth and traffic would take place differ, is that not true?

MR. ROSENTHAL: There is a slight, there is a difference in base. There were sort of two separate issues. One had to do with coal traffic, one had to do with non-coal traffic.

For the coal traffic what AEPCO actually did, in rebuttal, was we had criticized their use of April 2009 data, April
2009 projection.

In the rebuttal they switched to a 2010 data source that actually took into account the effects of the recession.

So for coal there is, actually, much less of a difference between the parties than there was at the beginning. For non-coal, it really is a different methodology of how to account for what happened in 2009.

We didn't try to construct a new traffic group. We tried, like AEPCO did, to index it. We just used a different data indexing process.

CHAIRMAN ELLIOTT: Thank you, Mr. Rosenthal. Mr. Sipe?

MR. SIPE: Good morning, Chairman Elliott, Vice-Chairman Mulvey, and Commissioner Nottingham.

My name is Sam Sipe, I'm here today on behalf of BNSF Railway. I have three points I would like to make this morning, in the ten minutes allotted to me.
First, BNSF emphatically concurs that the interchange issue that Mr. Rosenthal has addressed in some detail, is the key to this case.

It will determine the outcome.

Some of the other issues that you have identified here this morning are important and, of course, should be properly resolved for purposes of not only getting it right this time, but for purposes of guiding the parties in future cases.

But this interchange issue is going to determine the outcome of the SAC test in this case. Because, as Mr. Rosenthal noted, if you do it right, and do the analysis based on the actual interchanges that the Defendants used to provide the service to AEPCO, they don't get over the hump on the stand-alone cost test.

This issue, to speak to Vice-Chairman Mulvey's question about the clarity of the Board's precedent, this issue regarding
the interchange, and how the Board's rerouting precedent applies, is an issue of first impression in this case, because it is a multi-carrier case.

It is because there are two defendants in the route that we need some clarification to the facts here regarding the prior precedent that talks about rerouting in the context of a single carrier case.

AEPCO tries to downplay the interchange issue by characterizing its SAR configuration, as involving an internal reroute, and contending that AEPCO internally reroutes both the New Mexico and PRB traffic, consistent with established Board precedent.

And, yes, the Board says you can do internal reroutes of issue traffic. But there is no internal reroute here with respect to the real world service provided by each Defendant.

In the real world the interchange points agreed to by the carriers, define the
boundaries of their responsibility for providing service.

Thus the interchange point, in an inter-line rate case is the equivalent of an origin or destination in a single carrier case. And it is axiomatic that the stand-alone railroad must serve both the origin and the destination.

So, too, in an inter-line case, the design of the stand-alone railroad must respect the interchange point, because it defines the boundary of the participating carrier's responsibility for transporting the traffic.

In addition to defining their respective geographic boundaries responsibilities, by their specification of an interchange point, BNSF and UP have distinct corporate boundaries.

They are not responsible for paying one another costs, and they don't have access to one another's revenues. AEPCO's
shifting of the interchange points away from
those agreed to by the carriers, not only
results in a meaningless cross subsidy
analysis, as Mr. Rosenthal explained, it also
represents an impermissible blurring of
corporate boundaries, by using BNSF revenues
to offset UP costs, and vice versa.

The Board recognized, in the prior
AEPCO case, that it would not be appropriate
to claim a carrier's revenues to offset costs
for which it is not responsible.

The Board should respect the
carriers specification of interchange points,
because doing so will respect the corporate
boundaries of the two Defendants.

And I would note there is
precedent on this issue of, if you will, the
boundaries of a Defendant's responsibility,
and it is a little bit different, a little bit
different subject from the rerouting.

And the principle, which we have
addressed in our brief, was reiterated by the

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Board in TMPA, when it said the analysis of
the reasonableness of a Defendant carrier's
rate should be based on the extent of the
Defendant carrier's participation in the
movement.

COMMISSIONER NOTTINGHAM: Mr. Sipe, if I could ask? On your point about the sanctity of the interchange points, as determined by the railroads, what can railroad customers, shippers, do if they are concerned about the routing, they think the routing that the railroads have determined and set up disadvantaged them?

Should they petition the Board for alternative routing, and in this case, possibly through Amarillo, and then make certain showings to have the routing determined?

Because, surely, railroads understandably are in the business of producing the highest value possible to their shareholders and not necessarily always
providing the lowest possible rate to their
customers.

You know, I think we are all
concerned that the interchange points
determined by the railroads might not always
be determined purely on efficiency, and rail
operational grounds, but could this be for
economic gain, and real customers might want
to petition for an alternative routing?

MR. SIPE: It is a good question,
Commissioner Nottingham, and it is a question
that, I believe, has a very straightforward
answer.

There is a statutory provision,
section 10705, and there is Board rules,
competitive access rules implementing that
statute that says: If a shipper can
demonstrate the railroad routing is
inefficient, the shipper is entitled to have
the traffic rerouted.

Here, in this case, if you focus
for example on the New Mexico traffic, there
is no way in the world that the Board would ever find that AEPCO's proposed rerouting of the traffic is more efficient than the actual real world routing.

AEPCO increases the length of haul by a very substantial amount, the variable costs of handling this traffic over AEPCO's proposed reroute would be far higher than they are on the actual issue traffic movement.

So, you know, we would say fine if their problem is that we haven't given them an inefficient routing, you know, bring it on under the competitive access rules in section 10705.

VICE-CHAIRMAN MULVEY: You are basically saying that it is a reasonableness issue, and that the creation of the SAR by AEPCO is unreasonable, it goes too far, and that it overcapitalizing the SAR in order to justify it, or in terms of relying on it.

The problem, of course, a point that was raised before. What if it was a
water carrier that was going to be part of the joint movement, instead of two railroads, and that might require a different interchange point to get to where the water carrier is located.

Wouldn't you be able to justify changing the interchange points in those cases?

MR. SIPE: As Mr. Rosenthal said, in responding to a similar question, the issue here is what traffic is available to offset the costs of the stand-alone facility.

And we think the traffic has to be the traffic associated with a Defendant carrier's participating in the movement. It doesn't make sense for AEPCO to be claiming revenues from BNSF on those movements from Amarillo to Vaughn, for example, which have nothing to do with New Mexico issue traffic.

So how that would all play out in the hypothetical situation of a water carrier movement with a different interchange point,
I can't tell you what the mechanism would be,
Vice-Chairman Mulvey.

But I will say to you that it would be inappropriate to allow the
complaining shipper to rely on traffic that has nothing to do with the issue traffic.

And that is a sort of first principle of SAC. You know, grouping of SAC traffic which is, frankly, what allows shippers to win the cases, when they win.

Grouping is supposed to involve sharing of facilities with the issue traffic. And they are not doing that here.

There is one other point I would like to make. Mr. Rosenthal mentioned that I would say something about the Southwestern Railway variable costs.

And I'm going to take a pass on that, unless you want to ask me about it, because we have addressed it thoroughly in the brief.

But there is another point that I
would like to mention to the Board. And that involves the methodology for allocating revenues on cross-over traffic.

If I may, I will be very brief.

The Board's use of modified ATC, instead of original ATC to allocate revenue on cross-over traffic, has been remanded, by the DC Circuit to the Board, in the pending Western Fuels case.

In the present case Defendants argued, in their reply evidence, which was submitted before the DC Circuit's remand, that original ATC is the proper approach to apply.

And the DC Circuit's remand reinforced that position. Defendants submitted evidence on original ATC revenues, in their electronic work papers in this case.

BNSF believes that the Board should refrain from addressing the proper approach to revenue allocation, in this case, while the issue is pending in Western Fuels.

Before issuing a decision in this
case, the Board should determine whether the choice of revenue allocation methodology makes any difference in the results here.

We don't think it will make any difference. But if you decide that it does, then we would request that the Board hold this case in abeyance, until it decides the revenue allocation issue in the Western Fuels case.

Thank you.

CHAIRMAN ELLIOTT: Thank you, Mr. Sipe. Mr. Rosenberg, you have five minutes on rebuttal.

MR. ROSENBERG: Thank you. Let me address a few points in rebuttal, very quickly.

CHAIRMAN ELLIOTT: And, by the way, you should keep your answers to Vice-Chairman Mulvey's questions short, because he has seven pages of questions.

MR. ROSENBERG: I'm aware of that, I will do my best. First, the Railroad Counsel said that the answer about rerouting
the traffic, and using a different interchange was important. And they said that it was pretty clear.

We agree that it is important, and it is pretty clear. In fact the Board addressed it in AEPCO's prior rate case. And when the Board said that AEPCO could reroute the New Mexico traffic through Vaughn-El Paso.

The railroads, while they claim that you should stick to the present, they are actually asking you to jettison it. And you shouldn't.

Let's see, I want to clarify my comments on the updated evidence as to volumes. When I said that AEPCO had the best evidence of record, I should say that AEPCO has the only evidence of record that you can utilize, because the railroads did not submit complete data.

Also, the idea of filing a, you know, a Motion to Compel, or other discovery request, when the evidence has already gone in
is, you know, would be problematic, because
discovery has already closed.

Discovery is supposed to happen
before the evidence comes in, not afterwards.

With respect to not updating the projections
for the recession, about the non-coal values,
I think Mr. Rosenthal described it properly.

But what happens is that the
railroads previously had a forecast that AEPCO
utilized, that showed volumes going down, and
then recovering and trending upwards.

What the railroads are trying to
do is to lock in a greater than projected
decrease, and keep that intact throughout the
remainder of the DCF period, so the volumes
are always below the projections.

Our point is that with the
recovery, so far, with the data that is
available, it shows that the original
projections are reasonable, if not
conservative.

It has also been indicated, or
implied that the UP's Vaughn-El Paso traffic
shares no facilities with the traffic moving
to AEPCO.

And, in fact, with our stand-alone
railroad, 85.7 percent of the traffic that we
depict, as moving over the Vaughn-El Paso
segment, actually moves west on UP, past
Cochise to points further west.

So it is traffic that is logically
and reasonably available. With that I would
be glad to respond to as many of the pages
that Vice-Chairman Mulvey has, as I can, in
the time available.

VICE-CHAIRMAN MULVEY: I think, in
the interest of time, I would ask the Chairman
to keep the record open, as we usually do, and
we will submit some of these questions to be
responded to for the record to both AEPCO and
the two railroads.

COMMISSIONER NOTTINGHAM: Mr.
Chairman, if I could, Mr. Rosenberg, I'm
trying to figure out a way to harmonize
section 10705 regarding competitive access
with the stand-alone rail cost model.

    Should -- do you believe that
shippers should make some type of efficiency
argument, or showing, if they are going to
adjust interchange points, and reroute traffic
in their SARR?

    Or does efficiency have absolutely
nothing to do with the stand-alone railroad
model?

MR. ROSENBERG: What AEPCO did is
AEPCO filed a rate case. What we are saying
is that the rate is too high, that we pay too
much, that we end up cross-subsidizing other
traffic.

    And enriching the carriers
excessively. That is what the stand-alone
cost analysis does. That is what we
demonstrated.

The Board's earlier reasoning is
that if the railroads have the capability to
adopt a different routing, then the stand-
alone railroad has that same routing, has that same flexibility, and applies it in the stand-alone world.

And that is exactly what we did. Frankly, we think that the railroad position is a little bit contrived. And if I can belabor an example?

Suppose with the New Mexico traffic that we had filed a 10705 case, and we are saying that the way the traffic should be handled is that BNSF should take it, and handle it, as far as it can go, which would be to handle it going first to Vaughn, and then to EL Paso, using the track price that we tried to use in the earlier case, and we are not allowed.

Then El Paso would be handed off to UP. That is consistent with the preferences given the originating carrier.

Even if we had done that we would not be able, based upon the earlier rate case, to use the trackage rights. What the
railroads are trying to do is to make it more
difficult to bring a rate case where there is
a joint line, a joint through-rate movement
involved.

That is inconsistent with AEPCO's
prior rate cases, and inconsistent with the
coal rate guidelines. It is also inconsistent
with the Staggers Act Conference Report, where
it says the same rate standard, for other
rates, should apply to joint line rates.

It is unnecessary --

COMMISSIONER NOTTINGHAM: Mr.
Rosenberg, if I could get you to try to answer
the question a little more precisely.

How does efficiency, how should
efficiency play into our consideration of a
case like this? Does it have absolutely no
bearing, whatsoever, on the case? Or should
we be keeping some sense of the efficient
operation of the national interstate rail
system in mind, as we try to reach an
equitable outcome in this case?
MR. ROSENBERG: I think efficiency
is being used in two different senses. And it
is the nature of the analysis.

It is one thing when you are
looking at the world as it currently stands,
you know, the railroads legacy, what they have
inherited.

If you are looking at the
railroads as they stand today, you have the
line that runs from Belen to Deming. It is
logical for the railroads to use it.

In the stand-alone world you start
with a clean sheet of paper, where you need to
recoup all of your investments. You know, a
different routing makes sense.

The railroads get to have the
higher of the stand-alone costs, or the
jurisdictional threshold. That protects them
more than adequately under these
circumstances.

COMMISSIONER NOTTINGHAM: So did I
hear you say that in the real world
efficiency, of course, should matter. But that in case such as this, it should not matter?

MR. ROSENBERG: No, I'm saying that efficiency is applied differently in the two contexts, and the railroads are the beneficiary of having the rate determined as the higher of the jurisdictional threshold, or the stand-alone cost.

In this case our stand-alone cost analysis shows that the railroads, at the jurisdictional threshold, receive more than they need to be able to handle the traffic.

Yet the rate is going to be set at the jurisdictional threshold instead. That is a cross subsidy, it is what the statute, as applied by the Board calls for.

And that is sufficient under these circumstances.

COMMISSIONER NOTTINGHAM: Mr. Rosenberg, just one follow-up. Regarding, changing topics a little bit.
Regarding AEPCO's hypothetical railroad operating plan, if I understand the hypothetical railroad proposed, it would be about 3,310 track miles that would carry a substantial amount of intermodal and general freight traffic, but it would have no classification yards, nor intermediate switching anywhere on its system?

Is that -- that sounds remarkable to me. Is that a fair characterization of the hypothetical railroad you are proposing?

MR. ROSENBERG: AEPCO's traffic route consists of unit coal trains, and it consists of overhead traffic plus a limited number of intermodal trains that it originates at El Paso.

That is traffic that the Defendants handle, and that is the traffic that AEPCO has included, proceeding on the least cost, most efficient basis, which is what the coal rate guidelines contemplate.

To require AEPCO to -- AEPCO's SAR
to engage in other activities is to force AEPCO to pay for other traffic, to construct facilities that are not needed, to handle its traffic, or the other traffic that it has selected for its traffic route.

COMMISSIONER NOTTINGHAM: But in the real world of railroading, a 3,310 track mile system, carrying a great diversity of traffic would, in fact, have intermediate switching at multiple locations, it would seem to me.

And it would probably have classification yard facilities as well. Those things cost money, and how do you account for that in your hypothetical railroad?

MR. ROSENBERG: The hypothetical railroad does not need those facilities in order to be able to handle AEPCO's traffic. To force AEPCO, and the other shippers, to pay for those facilities that they don't need, constitutes cross-subsidy of costs, it constitutes an inefficiency that is
inconsistent with the coal rate guidelines,

contestable market theory, and stand-alone
costing.

VICE-CHAIRMAN MULVEY: This case,

this hearing is a good example of no good deed
goes unpunished.

The Board, over the past few

years, has made a lot of effort to try and

simplify the whole rate case process,

including opening up processes to small

shipments.

But, obviously, we still have

very, very complex cases. And this particular
case is especially complex.

I wanted to ask a question about

some of the Board's changes. We have adopted

the average total cost approach, and the

maximum markup methodology recently.

And I was wondering to what extent

those changes in our processes affected

AEPCO's approach to building its traffic
group, and its operating plans?
And if those changes had an effect, what was the effect in constructing the traffic group and operating plans, the maximum markup methodology and the average total cost approach?

Or is that a question better submitted for the record?

MR. ROSENBERG: It is probably better submitted for the record. But if I can venture, it made it more complicated. But, I mean, --

VICE-CHAIRMAN MULVEY: But I'm not surprised.

MR. ROSENBERG: Let's see, originally, when we submitted our opening evidence, we had to run it on the beta version of Office10, because the spreadsheets were just too large to run otherwise.

So, you know, so this is a good sized railroad, it makes it more complicated. I would have to, you know, check with our consultants as to whether or not we would have
done anything differently as a consequence.

One of the things is that in trying to put a rate case together, a lot of the stuff comes together at the end, because everything cannot be fully contemplated, in advance, particularly with demands of the RTC analysis.

So you anticipate, you know, the Board sets up rules, and we try to work with it. And in this case we believe that we have.

VICE-CHAIRMAN MULVEY: Thank you.

CHAIRMAN ELLIOTT: Thank you, Mr. Rosenberg. Thank you, Counsel, very much for appearing today, and for your excellent arguments, and we will take the matter under advisement, and the meeting of the Board is now adjourned.

(Whereupon, at 10:50 a.m., the above-entitled matter was concluded.)
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Neal R. Gross & Co., Inc.
202-234-4433
CERTIFICATE

This is to certify that the foregoing transcript

In the matter of: STB Docket No. 42113

Before: United States Surface Transportation Board

Date: September 28th, 2010

Place: Washington, DC

was duly recorded and accurately transcribed under my direction; further, that said transcript is a true and accurate record of the proceedings.

[Signature]

Court Reporter
September 28, 2010

STB Docket No. 42113

AEP Co. v. BNST & UP

ARGUMENT EXHIBITS

DEFENDANTS' ORAL
actual weight of coal per ton load whichever is greater.

Preflight charges will be assessed on the basis of the applicable minimum weight per ton load of the

<table>
<thead>
<tr>
<th>Route</th>
<th>Minimum Weight Provided Shipper</th>
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<tbody>
<tr>
<td>North Tipple, NM</td>
<td>$1.59</td>
</tr>
<tr>
<td>El Segundo, NM</td>
<td>$1.39</td>
</tr>
<tr>
<td>Lee Ranch, NM</td>
<td>$1.39</td>
</tr>
<tr>
<td>Outlaw</td>
<td>$1.16</td>
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</tbody>
</table>

Rates shall be in U.S. Dollars per Net Ton Coal;

Through Rates and Minimum Weights:

Weights shall be in Net Tons Coal;

<table>
<thead>
<tr>
<th>Route</th>
<th>Destination</th>
<th>Origin</th>
<th>Commodity</th>
<th>Effective Date</th>
</tr>
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</tbody>
</table>

considered „enhanced” or „beneficial” and addressed used exclusively for dust control to reduce breathing shall not be provided however, Coal Issued with

No Subbituminous Coal, STCC 1.1-2 Series. Not applicable for transportation

Common Carrier Rating Authority BNSF 57966

The Burlington Northern and Santa Fe Railway Company („BNSF„)
The following table outlines the specific rates and minimum weights for coal transportation on the specified routes:

<table>
<thead>
<tr>
<th>Route</th>
<th>Minimum Weight</th>
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<tbody>
<tr>
<td>Eagle Bluff - Decoy, MT</td>
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</tr>
<tr>
<td>Challenger, AR Co., MT</td>
<td>118</td>
</tr>
<tr>
<td>Spring Creek - Neco, MT</td>
<td>118</td>
</tr>
<tr>
<td>Challenger, AR Co., MT</td>
<td>118</td>
</tr>
</tbody>
</table>

Additional information and notes can be found below:

- **Effective Date:** February 19, 2009
- **Commodities:** Raw Subbituminous Coal, STC 11-21 Series, Not applicable for transportation
- **Fuel:** Considered "enhanced" or "enriched" as described exclusive of those products or to reduce heating requirements of enriched coal or synthetic coal, provided however, coal received with
- **Rates:** Shipped in U.S. Dollars on ton coal
- **Weight:** Shipped in net tons coal
- **Designation:** Arizona Electric Power Cooperative, Inc. Apache Generating Plant near Coolidge, AZ
- **Options:**
  - **Flex:**
  - **Common Carrier Rates Authority BNSF 57988**

The Burlington Northern and Santa Fe Railway Company ("BNSF")
Pretax Charges will be assessed on the basis of the applicable Minimum Weight per Trainload or the actual Weight of Coal per Trainload whichever is greater.

<table>
<thead>
<tr>
<th>Commodity</th>
<th>Signal Peak - Mine</th>
<th>MT</th>
<th>Origin:</th>
<th>Destination:</th>
</tr>
</thead>
<tbody>
<tr>
<td>Raw Subbituminous Coal</td>
<td>STC 11-2</td>
<td>118</td>
<td>BNSF - Peabody, CO - Union Pacific Railroad Company (&quot;UP&quot;)</td>
<td>Arizona Electric Power Cooperative, Inc. Apache General Plant near Coolidge, AZ.</td>
</tr>
<tr>
<td></td>
<td></td>
<td>4423</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

*Rails spirited in U.S. Dollars per Ton Coal: Weights spirited in Net Tons Coal: Through Rates and Minimum Weights:
- BNSF - Peabody, CO - Union Pacific Railroad Company ("UP")
- Arizona Electric Power Cooperative, Inc. Apache General Plant near Coolidge, AZ.*
Schematic Of The Arizona and Northern Stand-Alone Railroad

- Defiance to Vaughn: 263.1 miles
- Vaughn to El Paso: 230.6 miles
- El Paso to Cochise: 239.5 miles