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VIA E-FILING

Cynthia T. Brown
Chief of the Section of Administration
Office of Proceedings
Surface Transportation Board
395 E Street, SW
Washington DC 20423-0001

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October 7, 2024
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Public Record

Re: BNSF Railway Company – Terminal Trackage Rights – The Kansas City Southern Railway Company And Union Pacific Railroad Company, FD 32760 (Sub-No. 46)

Ms. Brown,

By decision served on July 5, 2016, the Board granted BNSF Railway Company (BNSF) terminal trackage rights over the Rosebluff Lead, a single track, approximately nine miles in length, jointly owned by The Kansas City Southern Railway Company (KCS) and Union Pacific Railroad Company (UP) in the Lake Charles area of Louisiana. In a subsequent decision, the Board, pursuant to 49 U.S.C. § 11102(a), established conditions of use for BNSF to directly serve a LyondellBasell (Lyondell) facility at West Lake Charles, La., and set forth a procedure for setting compensation. Pursuant to that procedural schedule, the parties completed briefing regarding the compensation due to KCS, including the submission of expert reports and evidence.

In reviewing the parties' filings and workpapers, the Board identified what it viewed as an apparent error in certain data related to line-segment earnings calculations submitted by KCS and its expert Dr. Kevin Neels. By decision served November 28, 2023, the Board ordered the parties to provide supplemental analysis and data, including workpapers, on several specified items to address this perceived error. (Decision No. 11). Due to the need to seek clarification of Decision No. 11, KCS (with no objections from BNSF or UP) requested a technical conference to better understand the Board's questions. By decision served January 10, 2024, the Board granted KCS's request for a staff-supervised technical conference. The staff-supervised technical conference was held on June 13, 2024.

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After the conference, the Board issued a revised schedule for the submission of the supplemental analysis and data as originally requested in Decision No. 11. Pursuant to that schedule, KCS's submission was due August 9, 2024. By stamp decision issued July 19, 2024, the schedule was further revised to set KCS's submission date on August 23, 2024. On that date, KCS submitted its comments in response to Decision No. 11. BNSF replied to those comments on September 23, 2024. As provided for in Decision No. 11, KCS hereby files its brief legal comments in rebuttal to BNSF's comments and submits the rebuttal analysis of Dr. Kevin Neels¹ addressing the criticisms raised by BNSF's expert, Mr. Michael Baranowski of FTI Consulting, in BNSF's reply.

As an initial matter, BNSF continues to insist, as it has throughout this proceeding, that it should not have to pay any compensation to KCS. KCS thoroughly addressed this issue in its May 21, 2021 Rebuttal Brief On Compensation ("KCS Rebuttal Brief"). As explained therein, BNSF's position is contrary to the statute. 49 U.S.C. §11102(a) requires the STB to "establish conditions and compensation for use of the facilities under the principle controlling compensation in condemnation proceedings." The "facilities" in this case is the jointly owned Rosebluff Lead. BNSF seeks to use the property that is owned, in part, by KCS. KCS is entitled to compensation, and it is the STB that is required to establish those conditions and compensation. KCS's statutory right to compensation cannot be set through private agreement between UP and BNSF, especially when that privately negotiated agreement was not set under the "principle controlling compensation in condemnation proceedings." See e.g., UP/SP Decision No. 44, slip op. at 150-51; UP/SP Decision No. 47, 1 S.T.B. 591, 613 (1996)

BNSF's position is also contrary to the Board's previous decision finding that KCS is entitled to compensation separate and apart from whatever BNSF pays UP for BNSF's current access via switch or haulage rights, which compensation is not shared with KCS. See Decision No. 8 at 15-16. Under the statute and the Constitution, KCS is entitled to compensation for the taking of its property that will occur through KCS being forced to allow BNSF to use its property.² And that compensation must be based upon what KCS has lost, not what the taker has

¹ Dr. Neels statement, Exhibit A, is being submitted as both a Public Version, which redacts Table I, which was based upon Highly Confidential Information, and a Highly Confidential version. These legal comments do not contain Highly Confidential or Confidential information.

² The fact that the Rosebluff Lead is owned jointly by UP and KCS does not mean that KCS is not also entitled to compensation. BNSF is already compensating UP at a negotiated rate. BNSF must now also compensate KCS at a rate "consistent with condemnation principles." The fact that KCS and UP, as co-owners, have chosen to establish operating windows (which can change at any time and are not always strictly followed because KCS and UP oftentimes continue past their operating windows) does not mean that KCS is not also entitled to compensation. If granted access, BNSF will be using KCS's share of an undivided interest in joint property.

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gained. See Mo.-K.T.R. Co. v. Kan. City Terminal Ry., 198 I.C.C. 4, 7-8 (1933). See also KCS Rebuttal Brief. Put another way, condemnation principles require that BNSF pay KCS what KCS will lose by virtue of BNSF's direct terminal trackage rights access – i.e., the market value of the access.³

Mr. Baranowski and BNSF also criticize KCS and Dr. Neels for presenting a methodology that only accounts for access to Lyondell and not for the entire Lead. However, this methodology results directly from the conscious choice by BNSF to request the STB to set terms and conditions for access to Lyondell. BNSF-132 at 1. The STB established terms for BNSF access to Lyondell, saying that it would establish compensation for access to Lyondell. “[P]ursuant to 49 U.S.C. § 11102(a), the STB establishes conditions for BNSF’s use of the Rosebluff Lead [“Lead”] to directly serve the Lyondell facility and sets forth a procedure for setting compensation.” Decision No. 8 at 1. Furthermore, as the STB stated in Decision No. 8, SSW is determined by “case-specific facts concerning the market value of the property, the tenant’s proportionate use, and the costs associated with such use.” Id., at 16. Because the proceeding at this stage is directed only for service to Lyondell, the STB cannot, and should not, use apply or transfer findings here to all shippers on the Lead. Other criticisms to Dr. Neels’ analysis are addressed in Exhibit A, Dr. Neels’ rebuttal verified statement to Mr. Baranowski’s criticisms.

Finally, BNSF has moved to strike Dr. Neels' alternative average total cost (“ATC”) approach, which excludes BNSF traffic in implementing the ATC revenue division

³ Although KCS’s expert, Dr. Neels, has presented calculations, analysis, and a methodology consistent with SSW Compensation precedents, KCS does not support imposition of the SSW Compensation methodology. SSW was intended to apply to overhead trackage rights and has never been used to set compensation that included access to local shippers over terminal tracks owned by a non-merging carrier. Furthermore, due to BNSF’s below-market access to Lake Charles shippers via a UP switch or haulage rate, KCS and UP earnings have been artificially suppressed for 28 years, which makes application of SSW Compensation inconsistent with condemnation principles. The only legally acceptable means to compensate KCS is to set a market-based fee based upon what KCS and BNSF would normally negotiate for BNSF’s access to KCS-served shippers. If BNSF cannot compete using that market-based rate, BNSF can continue to access Lake Charles shippers via a UP switch or haulage rate as it has done for 28 years which, consistent with merger precedent, is the most narrowly tailored and least intrusive merger remedy for competitive harm. KCS Rebuttal Brief, n. 11; Burlington N. Inc.--Control & Merger--Santa Fe Pac. Corp., 10 I.C.C.2d 661, 730 (1995). Indeed, it is important to note that Lyondell, the shipper for which the trackage rights fee is being developed for BNSF to directly serve, did not, prior to the UP/SP merger, have access to more than two carriers. Granting BNSF direct access actually increases the number of serving carriers to three, contrary to Board merger precedent. Id., at 729.

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methodology. BNSF first argues that it should be stricken because it relied upon a proprietary model that was not available to Mr. Baranowski. That is not accurate. Dr. Neels and this counsel offered several times to provide counsel for BNSF and Mr. Baranowski access to the model pursuant to a separate confidentiality agreement. It was BNSF's counsel and Mr. Baranowski that chose not to sign that agreement. Indeed, they never suggested modifications, changes, or a willingness to even negotiate over the language. As such, their unwillingness to negotiate any form of access should not form the basis for a motion to strike. Indeed, as Dr. Neels explains in Exhibit A, Mr. Baranowski did not need access to the model to confirm or check the accuracy of Dr. Neels' removal of the BNSF traffic from the ATC model.

The second basis for BNSF's motion to strike is BNSF's claim that the removal of BNSF from the ATC model is new "evidence" and "argument" that should be stricken. Dr. Neels' alternative ATC approach was not new evidence. As Dr. Neels explained in the August 24 Verified Statement and as elaborated further here in Exhibit A, removal of BNSF was simply an alternative explanation and method supporting his previously submitted ATC approach. As such, it was fully consistent with Decision No. 11's directive to provide "supplemental analysis and data, including workpapers, for its line segment earnings calculations" and to "provide an explanation, with supporting workpapers, showing how its data would not produce anomalies or inconsistencies if the CE methodology were applied." Decision No. 11, slip op. at 8. The discussion and removal of BNSF traffic was squarely within the parameters of that language. Furthermore, as noted above, Mr. Baranowski could have had access to the model and data during the earlier stages of this proceeding. He likewise could have obtained access for purposes of his September 23, 2024 submission, and even further, he could have used BNSF's own data to confirm or check Dr. Neels' work. Having taken no such steps, the request to strike should be denied.⁴

Sincerely,

/s/ William A. Mullins

William A. Mullins

Counsel for The Kansas City Southern Railway
Company

cc: Parties of Record

⁴ City of Colorado Springs and Metex Metropolitan District – Petition For Declaratory order – Abandonment Determination; The Denver And Rio Grande Western Railroad Company – Petition For Declaratory Order – Spur Track Determination, FD Nos. 31271 and 31230, 1989 ICC LEXIS 78 (ICC decided Mar. 22, 1989)(Denying various motions to strike in order to provide a more complete record, ensure fairness, and the information was proper and just as needed to decide the issues of the case); see also, City of Alexandria, Va.--Pet. for Declaratory Ord., FD 35157, slip op. at 2 (STB served Nov. 6, 2008)(Denying motion to strike because no party would be prejudiced and the information ensured a more complete record).

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**HIGHLY CONFIDENTIAL—FILED UNDER SEAL
BEFORE THE
SURFACE TRANSPORTATION BOARD**

FD 32760 (SUB-NO. 46)

**BNSF RAILWAY COMPANY
– TERMINAL TRACKAGE RIGHTS APPLICATION –
THE KANSAS CITY SOUTHERN RAILWAY COMPANY AND
UNION PACIFIC RAILROAD COMPANY**

**KCS’S REBUTTAL TO COMMENTS ON COMPENSATION CONCERNING BNSF’S
USE OF THE ROSEBLUFF LEAD**

EXHIBIT A

REBUTTAL VERIFIED STATEMENT OF DR. KEVIN NEELS

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I. Introduction

In 2021, I, Dr. Kevin Neels, filed three Verified Statements on behalf of KCS, in which I submitted SSW calculations for BNSF's use of the Rosebluff Lead ("Lead") in Lake Charles, Louisiana.¹ In response to questions raised by the Surface Transportation Board ("Board") in a November 28, 2023 Decision,² I filed an additional Verified Statement on behalf of KCS on August 23, 2024.³ On September 23, 2024, Mr. Michael Baranowski of FTI Consulting filed a Verified Statement on behalf of BNSF commenting upon my August 23, 2024 Verified Statement, and on other filings in this proceeding.⁴ I am filing this Verified Statement on behalf of KCS in rebuttal to criticisms raised by Mr. Baranowski in his September 23, 2024 Verified Statement.

II. Responses to Mr. Baranowski's Most Recent Verified Statement

Mr. Baranowski in his most recent reply statement has made a number of criticisms of the analyses, assumptions, findings, and opinions expressed (and sometimes not expressed) in my

¹ Verified Statement of Kevin Neels, filed as part of KCS's Opening Statement and Evidence on Compensation, Concerning BNSF's Use of the Rosebluff Lead ("KCS Opening on Compensation"), on January 26, 2021, as corrected on March 5, 2021 ("Neels Opening VS").

Verified Statement of Kevin Neels, filed as part of KCS' Reply Statement and Evidence on Compensation Concerning BNSF's Use of the Rosebluff Lead, on April 12, 2021 ("Neels Reply VS").

Dr. Kevin Neels Rebuttal Verified Statement, filed as part of KCS' Rebuttal Brief on Compensation, on May 11, 2021 ("Neels Rebuttal VS").

² BNSF Railway Company — Terminal Trackage Rights — Kansas City Southern Railway Company and Union Pacific Railroad Company (Decision No. 11), FD 32760, (STB Served Nov. 28, 2023).

³ Verified Statement of Dr. Kevin Neels, filed as part of KCS' Supplementary Evidence on Compensation Concerning BNSF's Use of the Rosebluff Lead, on August 23, 2024 ("Neels Supplemental VS").

⁴ Reply Supplementary Statement on Compensation - Verified Statement of Michael R. Baranowski, filed September 23, 2024. ("September 23, 2024 Verified Statement of Michael Baranowski")

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August 23, 2024 Neels Supplemental VS, and in prior filings in this proceeding. In this rebuttal, I will attempt to summarize and respond to these various criticisms.

- A. **Mr. Baranowski asserts that one of the conceptual flaws in my work is my failure to explain “why it is only now, under BNSF direct access, that KCS would be entitled to any more compensation than it receives currently under the long-running BNSF reciprocal switch access.”⁵**

The reason I did not focus on this question is because it is a legal question, rather than an economic question, and hence was not part of what I was asked, as an economist, to opine on. I understand, however, that the reason KCS has not previously been entitled to compensation is that, prior to the newly granted direct access regime, BNSF has not actually run trains over KCS-owned track. Instead, what BNSF did under the old indirect access regime was to interchange its traffic via haulage rights or switching rights to UP, and UP would deliver or pick up such BNSF traffic. In that instance, BNSF was not directly using any tracks owned either in whole or in part by KCS, and BNSF paid no compensation to KCS. In this proceeding, BNSF is seeking to run its trains and cars directly over the Rosebluff Lead; thus, becoming a tenant of KCS and UP. I understand that under the STB rules and precedent, a railroad granted the right to run traffic over track owned by another railroad must pay the owner fair compensation. This makes sense to me in that a tenant using the assets of an owner should compensate that owner for his use. However, because this is a legal issue rather than an economic issue, I was not asked to address or comment upon this issue.

⁵ September 23, 2024 Verified Statement of Michael Baranowski, page 3.

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B. Mr. Baranowski asserts that my “calculations fail to consider properly the parameters of the direct access granted BNSF by the Board”⁶

Although Mr. Baranowski does not define what he means by “the parameters of the direct access granted BNSF,” based on his past statements I believe that the most likely interpretation is that he is referring to the fact that the direct access to the Lead by BNSF is supposed to be confined to a four-hour window within the twelve-hour window within which UP currently operates.

KCS and UP each possess a fifty percent ownership interest in a single entity -- the Rosebluff Lead. Despite the fact that the ownership shares of each of these two parties extend to the entire Lead, Mr. Baranowski frequently talks about the KCS ownership interest and the UP ownership interest as though they cover two separate and independent facilities in different locations.⁷ For example, in his March 2021 Verified Statement Mr. Baranowski asserted that:

“KCS’s ownership interest in the Rosebluff Lead is not affected by BNSF’s access under the conditions of use imposed by the STB, and KCS is therefore not entitled to any interest rental related compensation. In addition, in accord with the Board’s express direction, BNSF will operate its direct service trains solely during UP’s 12-hour operating window, and BNSF will not use or infringe upon KCS’s rights as an owner of the Rosebluff Lead.”⁸

Several comments about this statement are in order.

First, there is no inherent or fundamental relationship between the two twelve-hour operating windows in effect on the Lead and the ownership interests of the co-owners. The

⁶ September 23, 2024 Verified Statement of Michael Baranowski, page 3.

⁷ There are numerous examples of Mr. Baranowski’s treatment of KCS’ and UP’s ownership shares as distinct facilities. See, e.g., Opening Statement and Evidence on Compensation - Verified Statement of Michael R. Baranowski, filed January 26, 2021 (“January 26, 2021 Verified Statement of Michael Baranowski”), page 3, 15.

⁸ September 23, 2024 Verified Statement of Michael Baranowski, page 2.

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twelve-hour operating windows currently in effect reflect the arrangements currently established by the co-owners to coordinate their operations. Different arrangements have been established in the past,⁹ and different arrangements could be established in the future. The current arrangements are not chiseled in stone.

Second, my understanding is that even under the current operating arrangements it is not uncommon for the operations of the two co-owners to spill beyond the boundaries of their assigned temporal windows. Given possibilities for accidents, equipment failures, weather events and other unforeseen disruptions, such spillovers are hardly surprising. There is no reason to expect BNSF to be immune from such unforeseen developments. To the extent BNSF will directly operate over the Lead as well, even if in theory solely within UP's window, these operations can only increase the likelihood that UP will be pushed into operating in KCS's window. Hence, there is every reason to expect that KCS will sometimes find itself forced to work around BNSF traffic, and to encounter increased interference from UP's operations.

Third, because UP and KCS each own an undivided fifty percent share of the Rosebluff Lead, BNSF's direct trackage rights would be using KCS's undivided property interest, even if it did so during and exclusively within UP's window. Simply because UP and KCS have for operating purposes created 12-hour windows does not mean KCS is not entitled to rental income when BNSF is using KCS's property.

⁹ The operating arrangements between KCS and UP have a history of being modified and changed. Originally, one railroad operated all traffic along the Lead for a period of 2 years, before switching responsibility to the other railroad. The companies alternatively have alternated responsibility for traffic to Zones 1 and 2. They now use this 12-hour operating structure. See Section III.1 of Neels Reply VS for a detailed account.

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Fourth, there is absolutely no basis for arguing that the fact that BNSF and KCS operate during different time windows will insulate either from competing with the other. The Rosebluff Lead serves a limited set of shippers, and those shippers generate a limited set of rail traffic. Any shipment carried by BNSF is a shipment NOT carried by UP or KCS. One must assume that BNSF is seeking direct Lead access because it believes that having that access will allow it to compete more effectively and/or more efficiently for Lead traffic. Its success or failure in that competition will directly impact the success or failure of KCS, regardless of how the operations of KCS, UP, and BNSF are arranged temporally. Because of these facts, it was neither necessary nor appropriate for me to consider “the parameters of the direct access granted BNSF.”

C. Mr. Baranowski criticizes me for my “restriction of scope of compensation to portions of the Rosebluff Lead needed to access only Lyondell.”¹⁰

I restricted my analysis to Lyondell access because this is what I was asked to do.

D. Mr. Baranowski criticizes me for my alleged “failure to provide the Brattle Network Model,” claiming that this failure “hindered ... [his] efforts to properly restate... [my] results.”¹¹

For a number of reasons, these claims are entirely groundless.

First, as the record in this proceeding makes clear, Brattle never refused to provide the Brattle Rail Network model to Mr. Baranowski. Indeed, as Mr. Baranowski himself admits in his Verified Statement, Brattle offered to make this model available subject to certain restrictions aimed at protecting Brattle’s legitimate interests in this valuable intellectual property.¹² Mr.

¹⁰ September 23, 2024 Verified Statement of Michael Baranowski, page 7.

¹¹ September 23, 2024 Verified Statement of Michael Baranowski, page 1.

¹² September 23, 2024 Verified Statement of Michael Baranowski, page 15.

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Baranowski refused to agree to these restrictions. He notes in his Verified Statement that these restrictions were more limiting than those protecting the confidentiality of the commercially sensitive waybill data. In doing so he seems to imply that the waybill data restrictions should have been sufficient, ignoring the differences between a set of proprietary data strictly limited in terms of its temporal and geographic coverage, and a generalized software-based modeling system broadly applicable across a wide range of potential applications. Although Mr. Baranowski objected to the protective language proposed by Brattle, my understanding is that he never suggested changes or alternative language that he would have found acceptable (except, perhaps, for arguing that it should have been covered by the existing waybill data protective order). Nor did he explain why the additional remedy of equitable relief in the event FTI misappropriated Brattle's proprietary rail network model was unacceptable. For all these reasons it is inaccurate to assert that Brattle simply refused to make this model available to him.

However, quite apart from the question of whether he had or would have been able to gain access to the Brattle Rail Network Model, Mr. Baranowski's claim that he was unable to verify the details of my calculations is completely incorrect. He has either deliberately misrepresented the materials provided to him or failed to understand their nature. He could, in fact, have reproduced all my calculations.

Access to the Brattle Rail Network Model is not critical for Mr. Baranowski's evaluation of my SSW calculation. The Brattle Rail Network Model is a complex piece of software with multiple applications beyond how it was used in this matter. In the current matter, I used the Brattle Rail Network model to identify the routings taken by specific shipments on specific railroads. For each such shipment, the output of the model consists of a sequential listing of the route segments traversed by that shipment. Each such route segment is associated with a unique

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identifier. The same segments and identifiers are used to describe the routing of any shipment processed by the model.

The datasets included in working papers filed with my August 23, 2024 Neels Supplemental VS provided all these routing details for all the shipments used in my SSW analysis. Further, this Verified Statement provided precise mathematical instructions for using these datasets and the routing details they contained. With this information, Mr. Baranowski could have reproduced all the results presented in that statement. There are no deficiencies in the materials provided to Mr. Baranowski that would prevent him from verifying the calculations underlying my work.

Furthermore, if Mr. Baranowski had concerns about the routing details generated by the Brattle Rail Network Model, he could have used the working papers datasets to compare the total lengths of haul generated by the Brattle Rail Network Model to the lengths of haul reported in the Confidential Waybill sample. Thus, he could not validly complain of an inability to evaluate the reliability of the Brattle Rail Network Model output.

For all these reasons, Mr. Baranowski's claims that deficiencies in materials provided to him prohibited him from assessing the accuracy of my calculations and analyses are inaccurate and should be dismissed.

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E. Mr. Baranowski criticized me for what he calls my “failure to account for KCS’s partial ownership share.”¹³

UP and KCS each own an undivided fifty percent share of the Rosebluff Lead. However, that fact does not automatically mean that KCS is entitled to only 50 percent of an SSW-based trackage fee calculated using the combined UP and KCS earnings for the entire Lead. Mr. Baranowski has repeatedly sought to create an artificial distinction between UP’s property rights and KCS’s property rights. He has divided the calculated SSW capitalized earnings in half, arguing that as a joint owner KCS is owed no more than that amount. However, as with any rental income for property that is jointly owned, how that income is divided is not for the tenant (in this case, BNSF) to determine. It is for the owners to determine how that rental income is divided. Here, as I understand the statute, BNSF is required to pay an access fee for use of the Rosebluff Lead, and absent use of a market-based fee, that fee should be based upon a capitalized earnings approach based upon the value of the Lead to its owners. How UP and KCS divide that rental fee is decided by the two owners.

I understand that UP has stated that it does not expect to receive any fee for BNSF direct access to the Lead other than the compensation to which it is currently entitled in its settlement agreement with BNSF. As acknowledged by all parties, including the Board itself, that fee is not SSW-based. My understanding is that the fact that BNSF and UP have agreed upon what BNSF should pay UP does not excuse BNSF’s obligation to pay the full access fee for Board-imposed access under the statute. How that fee is divided between UP and KCS is up to those two parties. Given that UP’s compensation for existing BNSF access was the result of a privately negotiated condition outside of the terminal trackage rights statute and that UP expects no more

¹³ September 23, 2024 Verified Statement of Michael Baranowski, page 4.

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compensation than that fee, it is reasonable to assume that UP has already agreed that KCS would be entitled to the entire amount of any new access fee imposed under 49 U.S.C. §11102.

F. Mr. Baranowski criticizes me for my “inclusion of a phantom contribution from UP and KCS switching rates that are by design cost based and generate no contribution.”¹⁴

Mr. Baranowski has made this argument before in previous filings, and I have responded to it before in previous filings. For the sake of completeness, I will reiterate here the points I have made before.

First, there is nothing “artificial” about these switch movements. They reflect the actual movement of freight on the Lead. Ignoring these movements is equivalent to assuming that all KCS shipments involving Zone 2 customers and all UP shipments involving Zone 1 customers simply terminate in the Rosebluff Yard, which is clearly not accurate.

Second, while I am aware of the many limitations and inaccuracies of URCS, it *is* the Board’s official regulatory costing system. In sanctioning the use of URCS for this purpose, the Board has weighed URCS’ limitations against the benefits of having a readily available costing system that all parties can use.¹⁵ The Board maintains that the benefits of URCS outweigh its costs.

Third, while it is true that UP and KCS have agreed, as owners, that the switch fees they charged to each other should be cost-based, this agreement does not extend to third parties.

¹⁴ September 23, 2024 Verified Statement of Michael Baranowski, page 4.

¹⁵ In Ex Parte 657, the STB weighed the merits of permitting parties in SAC-based rate reasonableness cases to make movement-specific adjustments to URCS costs. It concluded that “we do not believe that the use of movement-specific adjustments leads to a more accurate result than using the URCS system-wide average.” See Major Issues In Rail Rate Cases, EP 657 (Sub-No. 1), slip op. at 51 (S.T.B. served October 30, 2006).

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Indeed, the owners' agreements prohibited either owner from giving a third-party access to the Lead without the written approval of the other owner.

Finally, although the owner switch fees are supposed to be cost-based, it is also true, as Mr. Baranowski himself points out, that the last time these rates were benchmarked to actual costs was in 2004 – 20 years ago. Over the ensuing two decades, switching rates have only undergone periodic formulaic adjustments, and have had ample opportunity to drift apart from actual costs. My calculations of the contribution associated with switch movements reflect the actual fees paid by UP and KCS, as determined by the 20-year sequence of formulaic adjustments. They also reflect the only available measure of *current* costs: URCS.

G. Mr. Baranowski criticizes me for “failure to account for fixed costs when calculating the available earnings from revenues... [I allocate] to the Rosebluff Lead.”¹⁶

I addressed this criticism in my May 2021 Neels Rebuttal Verified Statement. I will explain more fully here why his analysis, as opposed to the simple criticism contained in his September 23, 2024, verified statement, is meaningless, and should be ignored.

To understand and evaluate this criticism, it is important to understand where in my analysis, in Mr. Baranowski's view, this “failure” occurs.

As part of my effort to use the capitalized earnings approach in my SSW analysis, I sought to establish the current value of the Rosebluff Lead. For this purpose, I used a multiplier approach, a method widely used in valuation analysis. Under this approach one first selects a base --- a quantity which is closely related to capital value, and which can be calculated both for

¹⁶ September 23, 2024 Verified Statement of Michael Baranowski, page 4.

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the entity to be valued, and for a comparable entity whose capital value is known. Commonly used bases include revenues, earnings, and EBITDA.¹⁷ In my analysis I used contribution as the base. In a standard multiplier analysis, one uses the comparison entity to compute a multiplier by dividing its capital value by the size of its base, arriving at measure of capital value per unit of base. In my analysis, the base was contribution – revenue minus variable cost – and the comparison entity was the US portion of KCS or UP. I calculated capital value per dollar of contribution for all US operations and multiplied this number by the contribution generated by the Lead.

It is readily apparent that one could obtain nonsensical results if one were to use one base for the entity to be valued, and another base for the comparison entity. Doing so would be like establishing the price for a package of hamburger by multiplying the butcher shop's price per *pound* by the number of *ounces* of hamburger in the package.

One might try to argue, for purposes of valuing rail segments, that earnings (revenues minus variable costs minus allocated fixed costs) are a more appropriate base than contribution (revenues minus variable costs).¹⁸ However, in his analysis Mr. Baranowski does not really employ an earnings-based valuation multiplier.

Instead, Mr. Baranowski's fixed cost adjustment is a mongrel calculation that combines inconsistently derived measures into a result that is conceptually and economically meaningless. He first calculates a measure of Lead earnings by subtracting the fully allocated costs (variable

¹⁷ The acronym EBITDA stands for earnings before interest, taxes, depreciation, and amortization.

¹⁸ My own opinion is that in valuing rail segments the contribution-based approach is superior. I believe that there is an inherent element of arbitrariness in the process of allocating fixed costs to rail segments that undermines the reliability of the valuation process.

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and fixed) associated with UP and KCS movements along the Lead from the revenues associated with those same movements. However, he then capitalizes this measure using my original contribution-based multipliers – an inconsistent, and thus overtly flawed, approach.

If I believed that this valuation calculation should be based on earnings rather than contribution – which I do not – the correct way to determine the effect of such a change would require re-computation of multipliers using earnings as the base. Earnings would, of course, be smaller than contribution and, when divided into the capital value number, would yield a much higher valuation multiplier. Multiplying a smaller earnings measure by this higher valuation multiplier would yield a much higher number than Mr. Baranowski’s mongrel approach and would produce something close to my original result.

H. Mr. Baranowski criticizes me for the “use of a flawed and unsupported enterprise value to capitalize earnings.”¹⁹

In his September 23, 2024, Verified Statement, Mr. Baranowski provides no explanation of what he means by this statement, or what basis he has for making it. In order to respond to this statement, I must go back to his 2021 Reply statement, where he discusses this objection at greater length.²⁰ There, he states first that my approach “is founded on the faulty premise that enterprise valuations are proportional to physical asset historical gross book values.”²¹ He also asserts that I attribute “the profitability and growth characteristics assumed for the KCS and UP systems to the profitability and growth characteristics of the [Lead].”²²

¹⁹ 2024 Verified Statement of Michael Baranowski, page 7.

²⁰ Verified Statement of Michael R. Baranowski, April 12, 2021, as filed with BNSF’s Reply Statement and Evidence on Compensation (“April 12, 2021 Verified Statement of Michael Baranowski”), at 22-25.

²¹ April 12, 2021 Verified Statement of Michael Baranowski, page 23.

²² April 12, 2021 Verified Statement of Michael Baranowski, page 23.

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Neither of these assertions is correct.

First, my approach does not rest upon any broad or overarching assumption regarding the proportionality of gross book value and enterprise value. Valuations under my approach are established by the market values of the equity and debt of the two railroads. My calculation uses book values only for two limited purposes: to separate the values of KCS's U.S. and Mexico operations, and to separate, for both KCS and UP, the values of the "below the wheel" assets from the values of the "above the wheel" assets that BNSF would not be using. For these limited purposes, the use of gross book value is entirely appropriate. The road property investments that make up the "below the wheel" assets are geographically immobile and thus serve as the value anchors for the various geographic divisions of the KCS and UP networks.

More generally, even though gross book value is not a perfect measure of value, one would certainly expect it to be closely related to value. If this were not true, why would large companies devote substantial effort and expense to tracking and reporting the book values of their assets?

The gross book value measure that Mr. Baranowski criticizes is closely related to the RCNLD measure that he endorses. Under RCNLD, the values of assets are set at their current replacement costs less depreciation. The primary difference between RCNLD and gross book value is that the latter measures values of assets at their original acquisition costs, and so does not account for the effects of subsequent inflation.

In fact, the effect of the relative "staleness" of the prices at which gross book values are recorded imparts a downward bias to my results. The road property assets that my valuation focuses upon tend to have much longer lives than equipment assets, and hence tend to be

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recorded at older and lower prices, imparting downward bias into the calculation of the “below the wheel” asset shares. The net result is that my calculations should be regarded as conservative.

I. Mr. Baranowski criticizes me for my “use of the wrong empty-to-loaded ratio to estimate empty car miles.”²³

Before I respond to this point, I must address an issue of terminology. One input into my SSW calculation was the ratio of total cars to loaded cars.²⁴ I based my calculation of the total-to-loaded ratio on the Lead upon actual system-wide total and loaded car-miles. In his 2021 Reply, Mr. Baranowski asserts that “the actual *empty* to load ratio” on the Lead is 2.0,²⁵ a claim he repeats in his September 23, 2024, Statement.²⁶ I can only assume that he intended to refer to the total-to-loaded ratio.

Setting aside issues of terminology, the more salient problem with this claim by Mr. Baranowski is that he cites no evidence or data of any kind to support his assertion, other than the fact that he says that this is so. His assertion implies that there is zero backhaul efficiency on the Lead. Relaxing his assumption and permitting any amount of non-empty backhaul movement increases the resulting SSW compensation. In contrast, as described above, I based my calculation of the total-to-loaded ratio of [[1.72]] upon actual system-wide data on loaded and empty car-miles, as reported in annual R-1 Reports—a data-driven, and more dependable, approach. The data produced by the parties in this case do not include information on empty

²³ September 23, 2024 Verified Statement of Michael Baranowski, page 7.

²⁴ Neels Opening VS, at Table 3 (p. 21) and Table 11 (p. 44).

²⁵ April 12, 2021 Verified Statement of Michael Baranowski, page 25 (emphasis added).

²⁶ September 23, 2024 Verified Statement of Michael Baranowski, Table 3.

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movements on the Lead, and so the system-wide average from the railroads that are parties to this case was the best possible data-driven proxy.

To shed some actual Lead-related light on this subject, I briefly examined traffic on the Lead, breaking it down by direction and by car type. The directionality of Lead traffic has an obvious bearing on opportunities for loaded backhauls. In the limit, if all shipments on the Lead were inbound, there would be no opportunities for loaded backhaul. Such opportunities are maximized when flows are more balanced directionally.

I therefore examine some actual shipment data to provide some insight to the potential for loaded backhaul. I note that *any* loaded backhaul would result in a total-to-loaded ratio that is lower than that assumed by Mr. Baranowski. I conducted this simple analysis at the car type level to assure that any backhaul commodities were compatible with the incoming equipment. To simplify the analysis, I focused on the five most frequently used car types. For this analysis I relied upon the KCS traffic tapes, which unlike the UP or BNSF traffic tapes, are limited to shipments involving Lead customers. The results of this simple analysis are shown in Table 1 below. It is clear from the table that, at the very least, there seems to be ample potential for loaded backhaul on the Lead within four out of the five most frequently-used car types.

**Table 1: Illustration of Potential for Loaded Backhaul on the Rosebluff Lead
KCS, Top 5 Most Frequently Used Car Types [1]**



]]

Sources & Notes:

[2], [3]: Number of inbound, outbound cars on the Lead. Calculated from KCS's traffic tapes.

[4] = [2] + [3].

[5] = |[2] - [3]|. Minimum empty backhaul required based on observed number of inbound, outbound cars.

[6] = [4] + [5].

[7] = [6] / [4]. Minimum possible total car to loaded car ratio based on observed number of inbound, outbound cars.

I fully recognize that these results are at best illustrative, and present something of a best-case picture of opportunities for loaded backhauls. Other factors can be expected to influence the prevalence of loaded backhauls, including timing (the inbound shipment must occur before the outbound shipment in order for the inbound equipment to be available for use) and car ownership (inbound and outbound shipments would either both have to involve the car owner, or be facilitated by intercompany car sharing agreements). Nonetheless, the fact that the inbound and outbound shipment volumes are somewhat balanced and often rely upon similar equipment suggests the “best case” (for BNSF), zero-efficiency assumption employed by Mr. Baranowski is unlikely to be accurate. In contrast, the system-wide number utilized in my analysis, [[1.72]],

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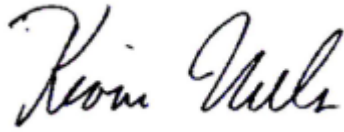
seems to align reasonably well with the ratios presented in Table 1. This conclusion is reinforced by the fact that the total car to loaded car ratios reported in Table 1 assume maximum possible backhaul efficiency. For the reasons enumerated earlier, I would expect the actual ratios on the Lead to fall, like the value used in my analysis, somewhere between the maximum efficiency numbers shown in Table 1 and the zero-efficiency number asserted by Mr. Baranowski.

VERIFICATION

I, Kevin Neels, declare under penalty of perjury that the foregoing is true and correct.

Further, I certify that I am qualified and authorized to file this Verified Statement.

Executed on October 7, 2024.

A handwritten signature in black ink, appearing to read "Kevin Neels", written in a cursive style.

Kevin Neels