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April 27, 2006

VIA E-FILING

The Honorable Vernon A. Williams
Secretary
Surface Transportation Board
1925 K Street, N.W.
Washington, D.C. 20423-0001

**RE: Comments of Ameren Energy Fuel and Services Company, in
response to *Rail Fuel Surcharges*, Ex Parte No. 661 (STB served Mar.
14, 2006).**

Dear Secretary Williams:

Enclosed for filing in the above-referenced proceeding are the Comments of Ameren
Energy Fuel and Services Company.

Yours very truly,



Sandra L. Brown

SLB:kjm
Enclosures

**BEFORE THE
SURFACE TRANSPORTATION BOARD**

Ex Parte No. 661

REVIEW OF RAIL FUEL SURCHARGES

COMMENTS OF AMEREN ENERGY FUELS AND SERVICES COMPANY

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***ATTORNEYS FOR AMEREN ENERGY FUELS AND
SERVICES COMPANY***

April 27, 2006

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**BEFORE THE
SURFACE TRANSPORTATION BOARD**

STB Ex Parte No. 661

RAIL FUEL SURCHARGES

COMMENTS OF AMEREN ENERGY FUELS AND SERVICES COMPANY

I. INTRODUCTION

The Surface Transportation Board's ("STB" or "Board") decision served March 14, 2006 in this proceeding provided notice of a public hearing to be held on May 11, 2006 and request for testimony to address fuel surcharges collected by railroads (hereinafter "Notice"). Ameren Energy Fuels and Services Company ("AFS") hereby submits comments in response to the invitation in the Board's Notice requesting comments on fuel surcharges. On April 20th, AFS filed a Notice of Intent to Participate in this proceeding and present testimony at the May 11th hearing. The oral testimony will be presented by Robert K. Neff, Vice President of Coal Supply for AFS and Jay Roman of Escalation Consultants.

A. Identification and Interest of AFS

Ameren Corporation, the parent company of AFS, is a public utility holding company which provides electricity to approximately 2.3 million customers in Missouri and Illinois. Ameren Corporation, through its various operating subsidiaries (collectively "Ameren") has 11 coal-fired plants, 10 of which rely on rail service as the primary mode of transportation for coal. Ameren is the largest shipper in the country of Powder River Basin ("PRB") coal, shipping over 35 million tons annually. The primary railroads serving Ameren's plants are the Union Pacific Railroad Company ("UP") and Burlington Northern Santa Fe Railway Company ("BNSF").

At the current time, Ameren's transportation of coal is transitioning from fixed price confidential contracts to public pricing tariffs. The new public pricing tariffs implemented by UP and BNSF all contain a non-negotiable fuel surcharge, which will have a significant effect on Ameren and its customers. The length of haul for Ameren's coal averages more than 1000 miles. Ameren expects its annual freight cost, including base rates and fuel adders, to be over \$560 Million in 2007. Assuming that On-Highway Diesel remains at its April 15, 2006 level of \$2.70 per gallon throughout 2007, fuel surcharges will account for 15% (or \$83 Million) of Ameren's transportation bill. If the price rises \$.65 to \$3.35 per gallon, the amount in diesel fuel surcharges that Ameren will pay will rise to \$93 Million in 2007. Similarly, if the price were to fall \$.65 to \$2.05 per gallon, the amount of diesel fuel surcharges that Ameren would pay would be reduced to \$46 million in 2007.

These comments are focused on the fuel surcharges imposed by BNSF as set forth in BNSF Rules Book 6100, item 3380 and by UP as set forth in UP Circular 6603-A, item 690. It is Ameren's position that the fuel surcharge mechanisms imposed by UP and BNSF in their public pricing tariffs do not reflect the actual expenditures for fuel by these two railroads.

B. Summary of Comments

The Board has authority to review railroad fuel surcharge mechanisms. In addition, the STB can declare certain practices, such as the current fuel surcharge mechanism, unlawful without undertaking a rate reasonableness review. As the Board's predecessor has done in the past, the Board should prescribe practices to be followed to insure that railroads are only recovering their actual fuel costs.

Ameren does not object to railroads recovering their actual cost of fuel. Utilities have been recovering changes in their fuel costs for years through fuel adjustment clauses and purchased gas adjustment mechanisms. Utilities, like Ameren, understand the importance of

recovering fuel costs, but the adjustment mechanism must be fair and transparent. Ameren has reviewed the fuel surcharges that are applied to Ameren's coal movements and has found compelling indications that these surcharges are not cost-based and result in significant over-recovery for the cost of fuel for these movements. Thus, the Board should establish narrow, cost-based standards for permitting railroad fuel surcharges that permit the railroads to only recover significant documented increases in fuel costs.

In sum, the Board should (1) provide clarification that the lawfulness of a railroad fuel surcharge may be challenged separately from the level of a railroad rate; (2) find that BNSF's and UP's surcharges are unreasonable practices in violation of the Board's statute; (3) establish narrow standards cost-based standards for the imposition of fuel surcharges for the sole purpose of recovering actual costs of fuel expended for a particular shipper's transportation that are not recouped by other means; and (4) require transparency in the submission of revenue and cost data justifying the imposition of railroad fuel surcharges and provide oversight of railroad fuel cost recovery.

II. STB HAS AUTHORITY TO REVIEW RAILROAD FUEL SURCHARGES

A. Prior Regulatory Treatment of Fuel Surcharges

1. The Ex Parte No. 311 Proceeding

This proceeding is not the first time fuel surcharges have come to the attention of federal regulators, or the first time railroad fuel surcharges have been questioned for over recovering fuel costs. Prior to passage of the Staggers Rail Act of 1980¹ and the adoption of the Rail Cost Adjustment Factor ("RCAF") as discussed below, railroads had to seek prior approval of any rate increases. Any approved increases could not go into effect for 30-45 days.² When fuel supplies were threatened by the Middle East Oil Embargo in 1973, the Interstate Commerce Commission

¹ Staggers Rail Act of 1980, 96 P.L. 448 (Oct. 14, 1980).

² See former 49 USC § 10762, as described in, e.g., *The Hanna Mining Company v. The Escanaba and Lake Superior Railroad Co.*, 498 F.Supp. 1267, 1269 (E.D. Mich. 1980).

("ICC") determined that the existing process for general rate increases, including the 30-45 day waiting period, "may not be adequate in the present circumstances to offset anticipated increases in fuel prices."³ It commenced a proceeding in order to allow railroads and motor carriers to increase transportation rates more expeditiously. Ex Parte No. 311, *Effect of Modifying Proclamation No. 3279 and Other Anticipated Energy Conservation Measures on the Operation of Carriers Subject to the Interstate Commerce Act*, 350 ICC 563, 564 (1975)("Ex Parte No. 311"). After a comment period, the ICC adopted expedited procedures providing interim relief from the regular 30-day notice required, but only if fuel prices were to escalate in the future as expected. *Id.* at 567.

In allowing this interim relief, the ICC declined the use of fuel surcharges. Specifically, the ICC had permitted the imposition of fuel surcharges on an "experimental basis" in 1973-74, primarily for motor carriers. *Id.* at 566. In Ex Parte No. 311 the ICC clarified that "it has been ~~the traditional view of this Commission that surcharges which add an element of confusion into~~ tariff use should only be sanctioned in unusual situations. Generally, surcharges have only been considered as appropriate in situations where it is anticipated that their use will be of temporary duration or where in extenuating situations the service performed under the surcharge is considered local to the carrier assessing the charge." *Id.* at 572 (emphasis added). Lastly, the ICC noted that while the price of fuel appeared as if it would remain higher for the foreseeable future, "the surcharge method of computing freight charges" was not an appropriate way to increase rates permanently. *Id.*

Because the ICC did not implement the expedited procedures adopted in Ex Parte 311 until 1979 and railroads did not begin recovering the high fuel costs of 1973-74 until June of 1979, the ICC in 1980 approved a 1.2% railroad fuel surcharge instituted as a general rate

³ 40 Fed. Reg. 5374 (1975).

increase. ICC Docket No. 37423, *Temporary Fuel Shortfall Recovery Surcharge, April 11, 1980*, 364 ICC 336 (1980). In this decision, the ICC utilized the Ex Parte 311 procedures ("even though...created for different purposes") because they represented the "best way to consider a fuel related surcharge." *Id.* at 337-338. Although the ICC initially declined to adjust the application of the surcharge on an individual shipper basis, in response to a successful appeal by Central Power & Light Company, the ICC removed the 1.2% surcharge as applied to that shipper because it shipped no traffic during the period in question. *Temporary Fuel Shortfall Recovery Surcharge, April 11, 1980*, Docket 37423, 365 ICC 299 (1981). The ICC eventually permitted a total of 4.7% of such surcharges to account for the delay in implementing Ex Parte No. 311. *Rates on Coal, Decker and Kleenburn to Illinois and Indiana*, Docket 37316, 364 ICC 158, 160 (1980) ("*Rates to Indiana and Illinois*") (describing ICC use of Ex Parte No. 311 to authorize a fuel surcharge of 4.7% in the first nine and a half months of 1979). In several instances, ~~railroads tried to apply the 4.7% increase to individual movements that were already subject to~~ existing rate and rate escalation arrangements. In these cases, however, the criteria utilized by the ICC to determine whether application of the surcharge was appropriate included whether the revenue generated by the surcharge was justified by the actual fuel costs incurred by the railroad or railroads to provide the service to that particular shipper or group of shippers. *Id.*, 364 ICC 158 (1980); and *Coal, Colstrip, Kuehn, and Decker, MT to Superior, WI*, Docket 37315F, 364 ICC 152 (1980). In the latter case, the ICC noted in particular that the railroad did not demonstrate that it would be harmed by waiting until it recovered the additional fuel costs for that movement through operation of the rate adjustment provision that had been agreed upon by the parties. *Id.* at 156.

In summary, prior to the passage of the Staggers Rail Act of 1980 and the development of the RCAF, the ICC only permitted fuel surcharges in very narrowly prescribed circumstances to

permit recovery of extraordinary and temporary increases in fuel costs prior to recovering such costs in rate increases or through a rate adjustment provision. Moreover, attempts to broadly apply surcharges to individual movements required some showing that the revenues generated by the surcharge did not exceed the actual fuel costs.

2. The Effect of the Adoption of the Rail Cost Adjustment Factor on Fuel Surcharges

In part at the behest of Congress, the ICC proposed in 1980 to replace the procedures for filing general rate increases with a procedure based on an inflation index, the RCAF. *Advance Notice of Proposed Rulemaking*, 45 Fed. Reg. 29103 (May 1, 1980). In publishing the proposed rules, the ICC stated that "the procedures proposed in this notice will permit railroads to recover fuel cost increases along with other cost increases on a quarterly basis... We thus propose that our current Ex Parte 311 fuel surcharge mechanism be discontinued." Ex Parte 290 (Sub No. 2), *Railroad Cost Recovery Procedures* 45 Fed. Reg. 81217 (Dec. 10, 1980).

The ICC adopted the newly-created RCAF railroad index just a few months later in April of 1981. *Railroad Cost Recovery Procedures*, Ex Parte 290 (Sub-No. 2), 364 ICC 841 (1981). According to the ICC, adoption of this index "permit[s] railroads to recover fuel cost increases along with other cost increases on a quarterly basis." *Id.* at 852. Furthermore, the RCAF meant that "[m]aintaining a separate surcharge mechanism for fuel would, in our view, serve no useful purpose once these rules are in place, and would, in fact, only complicate the operation of the new system." *Id.*

A few years later, the ICC adopted a revised methodology for the RCAF index based on the data gathered and submitted by the Association of American Railroads ("AAR"). *Railroad Cost Recovery Procedures*, Ex Parte No. 290 (Sub-No. 2), 1 ICC2d 207 (1984). In stating again that the creation of RCAF was in response to the Staggers Act, the ICC noted that "[w]e believe it was the intent of that Act to simplify the procedures for increasing rail rates and that the

application of the single RCAF to all base rates best accomplishes that intent.” *Id.* at 208. For the fuel component of the RCAF, the ICC decided that the AAR’s proposal, a survey of actual fuel prices paid by railroads was the best measure of the price of railroad diesel fuel. *Id.* at 217-218.

These statements from the ICC reveal that the RCAF was intended to not only replace the general rate increase method of adjusting rail rates with a simpler method, but also to supplant the need for fuel surcharges. Shippers and the AAR proposed competing methods of incorporating the price of fuel into the RCAF, but the ICC chose the AAR’s method. In other words, in response to the ICC’s request for rate adjustment methods that would replace the fuel surcharge mechanism, the railroads developed a method for incorporating fuel costs that was approved by the ICC. Any change to this railroad-proposed and ICC-approved mechanism for incorporating fuel costs in rates should only come in regulatory rulemaking.

~~The RCAF index is based on quarterly filings made by the AAR. These filings include a~~ forecasted railroad fuel cost for the next calendar quarter which is a mix of (1) actual diesel prices paid by railroads (for the weighting component) and (2) various projections by the major railroads’ fuel purchasing officers and others regarding the level of railroad diesel prices during the next quarter.⁴ These quarterly filings reveal that the RCAF methodology takes into account the fluctuation of railroad diesel prices caused by events in the world oil markets. For example, the filing made on December 5, 2005 by the AAR described the damage done by hurricanes Katrina and Rita as largely responsible for the rise in the fuel component of the RCAF. AAR forecast, Appendix B (page 1), Ex Parte 290 (Sub-No. 5) (2006-1), *Quarterly Rail Cost Adjustment Factor* (filed Dec. 5, 2005). These are exactly the same reasons now cited by the railroads for justifying the use of their privately developed fuel surcharges.

⁴ See generally “Rail Cost Adjustment Factor,” a publication from the Association of American Railroads (November 2001).

In adopting the revised RCAF in 1984, the ICC stated that "significant problems in the accuracy of fuel data" could warrant a change in the fuel component of the RCAF index. *Railroad Cost Recovery Procedures*, 1 ICC 2d at 218. In other words, there is a standing invitation to all parties to petition the Board for a change in the RCAF if they feel it does not accurately reflect Railroad fuel prices. This action is preferable to the railroads' exertion of their market power to adopt fuel surcharges that are clearly designed to enhance their overall revenues as opposed to enable the recovery of short term spikes in fuel costs.

B. The Lawfulness of Railroad Fuel Surcharges Should be Reviewed Pursuant to the Board's Authority under 49 U.S.C. § 10702 Governing Unreasonable Practices.

While the ICC decisions referenced above discuss the ICC's treatment of fuel surcharges, there is no clear Board precedent on this particular subject. Specifically, there is no precedent stating definitively whether the Board considers a fuel surcharge to be part of the rate for transportation or a "rule" or charge whose reasonableness can be challenged independent of the transportation rate. This lack of clear guidance is evident from filings in recent cases. For example, in STB Docket 42072, *Carolina Power & Light v. Norfolk Southern Railway Company*, the parties disagreed over whether NS could assess a fuel surcharge on top of a maximum reasonable rate prescribed by the Board in a case brought under the *Coal Rate Guidelines Nationwide*.⁵ While CP&L had claimed that all fuel costs had already been incorporated into the stand-alone cost ("SAC") analysis and prescribed rates over the DCF period, NS claimed the surcharge was a separate "rule" that had not been separately challenged by CP&L and, therefore, was not at issue in the case. CP&L Statement of Position at 8-9 (filed Jun. 4, 2004). The Board did not resolve this question in *CP&L*. Docket No. 42072, *CP&L v. NS*, at 6 (served Oct. 20, 2004). The same general question has been posed to the STB in other SAC cases, but no

⁵ 1 ICC2d 520 (1985).

answers have been provided. *See, e.g., Western Fuels Association v. Burlington Northern Santa Fe Railway Company*, Docket 42088 (complaint filed October 1, 2004); *Kansas City Power & Light Company v. Union Pacific Railroad*, Docket No. 42095 (complaint filed October 12, 2005). Thus, there is a need for the Board to specify that the fuel surcharges are railroad practices.

1. The Assessment of Fuel Surcharges is a Railroad Practice Subject to the Board's Jurisdiction.

Under 49 U.S.C. §§ 10702 and 10704(a)(1), the Board has authority over railroad practices. If a railroad practice is found to be unreasonable, the Board can order the railroad to cease engaging in it or the Board can prescribe the "practice to be followed." 49 U.S.C. § 10704(a)(1). Whether or not a particular railroad practice is unreasonable requires the Board to engage in a "fact-specific inquiry" to be conducted on a "case-by-case" basis. *WTL Rail Corporation – Petition for Declaratory Order and Interim Relief*, Docket No. 42092 at 6 (served February 17, 2006).

The fact that a railroad's public fuel surcharge is incorporated by reference into a transportation contract should be irrelevant for the purposes of this proceeding. Ameren, like other shippers, has no choice but to accept the fuel surcharge terms in whatever pricing method is used. Therefore, it is clear that surcharges are universal rules or charges subject to Board jurisdiction as "transportation-related" practices such as demurrage. *Capitol Materials Incorporated – Petition for Declaratory Order – Certain Rates and Practices of Norfolk Southern Railway Company*, Docket No. 42068 at 2 (served April 12, 2004). The manner in which the railroads calculate and assess their individual fuel surcharges is subject to a determination of reasonableness under 49 U.S.C. § 10702. In order to ensure that railroad practices are reasonable, the Board has previously used its authority under 49 U.S.C. § 10702 to assert jurisdiction over various other railroad rules and surcharges. The Board has evaluated the

specific demurrage charges assessed against a shipper under the unreasonable practice standard. *Capitol Materials* at 6. The Board has found a light-density line surcharge to be an unreasonable practice when used in conjunction with contract service. *Parrish & Heimbecker, Inc. – Petition for Declaratory Order*, Docket No. 42031 at 10 (served May 26, 2000). The Board has begun a proceeding to evaluate whether BNSF's imposition of storage and demurrage charges on all types of empty private cars awaiting loading is an unreasonable practice. *North America Freight Car Association – Protest and Petition for Investigation – Tariff Publications of the Burlington Northern and Santa Fe Railway Company*, Docket No. 42060 (Sub-No. 1) at 9 (served August 13, 2004). The Board has also evaluated whether it was unreasonable for a railroad to limit the hours its track could be used by a second railroad under a trackage rights agreement. *Granite State Concrete Co., Inc. and Milford-Bennington Railroad Company, Inc. v. Boston and Maine Corporation and Springfield Terminal Railway Company*, Docket No. 42083 at 1 (served September 24, 2004).

2. Shippers Should be Able to Bring Individual Challenges to Specific Fuel Surcharges Without Using the Board's Rate Reasonableness Procedures.

As shown above, the Board can evaluate the Class I railroads' general fuel surcharges under the unreasonable practice standard of 49 U.S.C. § 10702. A fuel surcharge is a universally-applicable tariff item that exists independently of the rate. As the Board recognized in the Notice, whether a fuel surcharge is a reasonable practice can be determined by examining whether the mechanism developed by the railroad "fairly reflect[s] the increasing fuel costs of the particular movements to which [it is] applied." Notice at 2. There is no need for a stand-alone cost or other rate analysis to make this determination. For example, the Board has previously determined the reasonableness of a particular demurrage charge without resort to rate reasonableness standards. *Capitol Materials* at 4 (finding a \$60 per day demurrage charge to be reasonable without resort to the rate reasonableness standards). The determination of whether a

purported fuel surcharge fulfills its cost recovery purpose can be aided by the submission of fuel cost and revenue data by the railroad(s) seeking to assess the fuel surcharge.

III. THE FUEL SURCHARGES IMPOSED BY BNSF AND UP ARE NOT COST BASED

A. BNSF's Fuel Surcharge in Item 3380

Item 3380 imposes a fuel surcharge on Coal Unit Trains and Trainload Shipments which is calculated by applying a percentage increase to the overall transportation rate. According to BNSF, the "fuel surcharge will be applied to the total freight charges for each shipment waybill dated on or after the 1st day of the second following calendar month." *BNSF Rules Book 6100, Item 3380*. The fuel surcharge will be included in the freight charges for each assessed shipment. Fuel surcharge rates will be adjusted monthly and calculated according to the U.S. Average Price of Retail On-Highway Diesel Fuel ("HDF") when the month of the second prior month equals or exceeds \$1.24 per gallon. For example, when the Time Period's Average Price of HDF is ~~between \$1.96 and \$1.999 the applicable surcharge rate would be 0.5% of the total freight~~ charges. When the U.S. National Average Fuel Index exceeds \$1.999 per gallon, the fuel surcharge rate will increase by 0.5% for every \$0.04 per gallon increase. BNSF provides the example of a fuel surcharge applied to shipments during the month of July. This example assumes the prior time period's May average monthly price of HDF was \$1.338 per gallon, therefore calculating the July's fuel surcharge as 1.5%. "Thus, for each \$10.00 of freight charges applicable to a shipment, the Fuel Surcharge would be \$0.15." *Id.*

Item 3380 is a revenue-based fuel surcharge. According to BNSF, the fuel surcharge is intended to allow BNSF to recover its fuel costs due to diesel fuel market volatility, but there is no correlation to BNSF's actual costs. Nevertheless, on BNSF's web site in response to a question on whether the fuel surcharge is over-compensating the railroads, BNSF admits that its pricing is market-based not cost-based. This "pricing" includes the imposed fuel surcharge.

B. BNSF's Mileage-Based Fuel Surcharge

BNSF's Mileage-Based Fuel Surcharge is calculated by multiplying the fuel surcharge per mile times the number of miles per carload per shipment.⁶ The mileage-based fuel surcharge is determined by using the U. S. Average Price of Retail On-Highway Diesel Fuel ("HDF"), the same fuel pricing table as used in Item 3380. "Mileage calculations will be based on BNSF Railway Miles between shipments' billed origin and destination as published on BNSF web page titled "BNSF Coal Unit Train and Trainload Mileage Table."⁷

The mileage-based fuel surcharge was targeted to be implemented on certain agricultural and coal traffic beginning on January 1, 2006. According to BNSF, railroads have traditionally applied a fuel surcharge based on a percentage of revenue to be gained from each shipment. However, during this time of high fuel prices, BNSF admits that a fuel surcharge based on percentage of revenue has and will continue to create significant disparities between the fuel surcharge assessed and their actual incremental fuel costs.⁸ ~~The mileage-based fuel surcharge~~ program is BNSF's attempt to "better align the fuel surcharge assessed...with the actual incremental fuel cost of transporting...goods."⁹

While distance may be a better proxy for the amount of fuel used in a movement than the transportation rate, it still is unnecessarily imprecise. The use of distance ignores a variety of factors that affect fuel usage, such as topography, train weight, train speed, frequency of stops, and the time required for the movement. The mileage-based surcharge also suffers from the same basic deficiency as Item 3380 in that it uses as a baseline a fuel price that (1) has no relation to BNSF's actual fuel costs; and (2) is not reflective of the current cost of diesel fuel,

⁶ Coal Mileage-Based Fuel Surcharge: http://www.bnsf.com/tools/prices/fuelsurcharge/pdf/coal_mileage.pdf

⁷ "BNSF Railway Miles" is a calculation of miles a carload is transported in the loaded direction. This calculation can be performed on the BNSF website. Also, see the "BNSF Coal Unit Train and Trainload Mileage Table."

⁸ Frequently Asked Questions: BNSF Mileage-Based Fuel Surcharge:
<http://www.bnsf.com/tools/prices/fuelsurcharge/faqs.html>.

⁹ *Id.*

thereby guaranteeing the surcharge will be assessed. These fuel surcharge practices therefore still do not correlate with actual costs.

C. Summary of UP Item 690

Item 690 in UP Circular 6603-A describes the fuel surcharge UP has established for common carrier shipments made pursuant to the Circular. UP states that Item 690 is an attempt to recover incremental costs for diesel fuel and has been included as a result of the volatility in the diesel fuel market. This fuel surcharge is often incorporated by reference into transportation contracts.¹⁰ Similar to the BNSF fuel surcharge, the UP surcharge is applied to line haul freight charges when the average price of Retail Highway Diesel Fuel ("HDF") calculated monthly, equals or exceeds \$1.35 per gallon. When this threshold is met, a fuel surcharge of 1.5% times the line haul rate is triggered. For every five cent increase above \$1.35 per gallon, the multiplier increases 0.5%. The fuel surcharge is applied to the freight charge for each shipment having a bill of lading dated on or after the 1st day of the second calendar month following the month with the HDF price increase. The average price is determined by adding the weekly HDF and dividing the result by the number of weeks reported, rounded to the nearest cent. The freight charge will never be reduced below the base freight charge as a result of applying the fuel surcharge. Also, the application or the removal of the fuel surcharge will not be retroactive.

D. BNSF's and UP's Fuel Surcharges Do Not Measure Actual Fuel Costs

Item 3380 and Item 690 both over-compensate actual fuel costs. In addition, the HDF is not an accurate estimate of the price BNSF and UP pay for fuel. Use of the HDF monthly average as a basis for the surcharge is not representative of actual fuel costs because the HDF is a retail price index and railroads do not purchase locomotive fuel in that manner. Like all the other Class I railroads, UP and BNSF both buy diesel fuel in bulk and pays wholesale prices, not retail

¹⁰ "The surcharge in this item applies to those agreements that indicate they are subject to this circular by reference unless that same agreement contains either a fuel surcharge or a specific rate adjustment mechanism that is tied to the RCAFU or other index that contains a fuel component." See *UP Circular 6603, Item 690, 3rd Revised Pg. 24.*

prices for their fuel. In addition, as discussed below, railroads are in a position to engage in large scale hedging on fuel.

Item 3380 does not measure actual fuel costs, but instead is applied when the HDF monthly average equals or exceeds \$1.24 per gallon. However, the HDF has not been at or below that level since March 2002.¹¹ Furthermore, BNSF buys diesel in bulk at wholesale prices, not retail prices for fuel. Thus, HDF is not an accurate estimate of either the price BNSF pays for fuel or the changes in that price. For example, BNSF's average cost for diesel fuel in 3rd Quarter 2003 was \$0.864 per gallon and its average cost of diesel fuel for 3rd Quarter 2004 was \$0.988 per gallon.¹² BNSF cost of fuel increased 14.4% from 3rd Quarter 2003 to 2004. In contrast, the HDF 3rd Quarter 2003 price was \$1.46 per gallon and \$1.83 per gallon in 3rd Quarter 2004, amounting to a 25.3% increase. Due to this disparity in increase percentages, BNSF shippers paid 11% more than the actual price BNSF paid for fuel from 3rd Quarter 2003 to 2004 because Item 3380 is tied to the HDF threshold. ~~BNSF's fuel surcharge program also results in~~ over-recovery of fuel costs because it ignores the 9% fuel efficiency improvement achieved by BNSF over the past ten years.¹³

Along the same lines, Item 690 allows UP to more than recover temporary spikes in the cost of fuel for a particular rail movement. Use of the HDF monthly average as a basis for the surcharge is not representative of actual fuel costs because the HDF is a retail price index. As noted above, UP buys diesel fuel in bulk and pays wholesale prices, not retail prices for its fuel. In 2005, UP paid an average of \$1.77 per gallon of diesel, but the average HDF price used in Item 690 during the year was \$2.40 per gallon. UP's 2005 Annual Report at 26.¹⁴ Moreover, due to the fact that Item 690 merely acts as a multiplier of transportation rates, it does not take

¹¹ See <http://tonto.eia.doe.gov/dnav/pet/hist/ldr001m.htm>

¹² BNSF Investors' Reports available at www.bnsf.com

¹³ BNSF 2005 Annual Report at 13.

¹⁴ The HDF table of fuel prices is found at http://www.uprr.com/customers/surcharge/surcharge_coal.shtml.

into account the fuel efficiency gains achieved by UP. Fuel usage by UP locomotives was 2% more efficient in 2005 compared to 2004; efficiency increased another 2% in the first quarter of 2006 compared to the first quarter of 2005. UP's 2005 Annual Report at 16; UP Form 8-K, filed with the Securities and Exchange Commission ("SEC") on April 20, 2006. Lastly, UP utilizes an array of other strategies to reduce its exposure to volatility of diesel prices. UP's 2005 Annual Report at 35 ("We may use swaps, collars, futures and/or forward contracts to further mitigate the impact of adverse fuel price changes."); UP's 2003 Annual Report at 16 ("To help reduce the impact of fuel price volatility on earnings...we will continue to adhere to our hedging strategy.").

In the fourth quarter of 2005, UP revenues increased \$404 million compared to the 2004 fourth quarter, but the UP "fuel and utilities" category of operating expenses increased only \$220 million. UP Form 8-K, filed with the SEC on January 19, 2006. Similarly, for the first quarter of 2006, UP's operating revenue was \$558 million higher than the first quarter of 2005, but its "fuel and utilities" expenditures increased only \$153 million. UP Form 8-K, filed with the SEC on April 20, 2006.

This built-in differential is compounded by the fact that UP and BNSF have not rebased the \$1.24 and the \$1.35 thresholds in Item 3380 and Item 690 to account for the fact that increases in the cost of diesel fuel are eventually reflected in newly established transportation rates. Specifically, the last time the HDF was below \$1.35 was in September, 2002. As UP and BNSF have negotiated or established new transportation rates for Ameren since September, 2002, such rates have included the current cost of locomotive fuel, as well as that particular movement's share all of UP's or BNSF's current variable and fixed costs. Thus, using the 4Q05 numbers above, a transportation rate provided in 4Q05 should include UP's and BNSF's current cost of fuel. To the extent that UP's or BNSF's actual fuel costs do not subsequently "spike," or fuel cost increases are covered by a rate adjustment provision such as the RCAF, there is no

justification for assessing the fuel surcharge multiplier to the transportation rate because the rate would reimburse UP and BNSF for all of the fuel costs it incurs to provide the issue transportation.

UP's and BNSF's fuel surcharges have increased substantially over the past 5 years when calculated as a percentage of revenue. The fuel surcharge has become more of a revenue-producing practice every year since surcharges were first implemented. Moreover, to the extent UP is providing the subject transportation pursuant to common carrier rates established pursuant to Circulars 111, 112, or 113, UP has reserved its right under applicable law "to adjust or cancel rates subject to 20 days' notice for increases." *See e.g.*, UP Circular 112 at 2 and UP Circular 111, Service/Rate Selection: Option 1 at 1. Such increases are obviously subject to the Board's jurisdiction.

The BNSF and UP fuel surcharge programs bear no relation to the amount of fuel used for the movement being assessed the charge. ~~Clearly, if there is no evaluation of the amount of~~ fuel used or the actual cost paid for fuel, then the surcharge is not "used only to recover the increased cost of fuel for the particular movements to which the surcharge is applied." Notice at 2. A further illustration of the lack of correlation between cost and recovery is that the fuel surcharge sets a floor whereby if the price of fuel dropped below the minimum threshold, no benefit incurs to the shipper.

This overcompensation is further compounded by the fact that the multiplier is largely independent of the distance of the movement or any other characteristics that affect fuel consumption for a particular movement.

Moreover, railroads consume huge quantities of railroad diesel fuel annually and previously engaged in price hedging activities. Railroads are in a unique position of being able to perform large scale physical hedging because of the substantial amounts of fuel they use.

Ameren believes that the railroads should be allowed to pass through prudently incurred fuel-related expenses to their customers, similar to the manner in which public utilities are able to pass through the actual cost of natural gas and fuel increases, subject to review by their regulators. Railroads, like public utilities, should have the obligation to keep costs down to the best of their abilities. This includes utilizing a well-thought out and reasonable hedging program with both financial and physical hedging.

IV. AMEREN'S RECOMMENDED ATTRIBUTES OF FAIRNESS FOR ANY RAILROAD FUEL SURCHARGE OR FUEL COST RECOVERY MECHANISM

Ameren does not dispute that railroads should be able to recover their increases in fuel costs. Regulated utilities are familiar with volatility in the fuel markets, and have an even greater percentage of their output tied to fuel costs than the railroads. But fuel cost recovery should not be a mystery. Utilities have been recovering changes in their fuel costs for years through fuel adjustment clauses and purchased gas adjustment mechanisms. Utilities understand the importance of recovering fuel costs, but they also understand that customers and regulators must be able to understand and be comfortable with the adjustment mechanism.

Utility fuel pass-through clauses are generally regulated by the state public service commissions and share four common attributes of fairness which Ameren recommends that the Board adopt for railroad fuel cost recovery:

1. The recovery of railroad fuel costs must be based on actual costs that the railroads incur.
2. Railroad fuel pass-through mechanisms must be transparent so all parties know what costs are included, how costs are calculated and the methodology of calculation.
3. Railroads should not be allowed to over-recover or benefit from their cost recovery of fuel.
4. Railroads should be expected to minimize their recoverable fuel purchase expenses through hedging programs and prudent purchasing practices.

As shown in these comments, these attributes of fairness are not currently being followed. First, the current recovery method for BNSF and UP under the HDF model recovers more than actual fuel costs. Second, the current fuel surcharge mechanism is not transparent. Third, the current fuel surcharge programs double count fuel cost increases. Fourth, oversight may be necessary to insure that the railroad industry meets its obligation to minimize their recoverable fuel costs.

V. THE BOARD SHOULD REQUIRE TRANSPARENCY IN THE SUBMISSION OF REVENUE AND COST DATA JUSTIFYING THE IMPOSITION OF RAILROAD FUEL SURCHARGES AND PROVIDE REGULATORY OVERSIGHT OF RAILROAD FUEL COST RECOVERY

To the extent the Board believes that neither current reporting requirements nor data received in this proceeding enable the Board to determine whether a particular fuel surcharge provides a railroad with more revenue than it needs to recover its fuel costs for a particular movement, the Board should adopt procedures to govern the submission of such data. The Board ~~has clear authority to obtain the data it needs under 49 U.S.C. § 721(b).¹⁵ Railroads already~~ provide certain fuel cost data to the AAR for the STB on a quarterly basis through the RCAF process. 49 U.S.C. § 10708.¹⁶ In addition, the Board also requires railroads to submit certain cost and revenue data under 49 CFR Parts 1200 through 1300. Furthermore, railroads are required to report certain information regarding carrier rates and service terms pursuant to 49 CFR Parts 1300 through 1332. Thus, Ameren believes the Board has the requisite power to use

¹⁵ 49 U.S.C. § 721 (b) (2006). "Inquiries, Reports, and Orders. - The Board may - (1) inquire into and report on the management of the business of carriers providing transportation and services subject to subtitle IV; (2) inquire into and report on the management of the business of a person controlling, controlled by, or under common control with those carriers to the extent that the business of that person is related to the management of the business of that carrier; (3) obtain from those carriers and persons information the Board decides is necessary to carry out subtitle IV; and (4) when necessary to prevent irreparable harm, issue an appropriate order without regard to subchapter II of chapter 5 of title 5."

¹⁶ 49 U.S.C. § 10708 (a) (2006). "Rail cost adjustment factor: (a) The Board shall, as often as practicable, but in no event less often than quarterly, publish a rail cost adjustment factor which shall be a fraction, the numerator of which is the latest published Index of Railroad Costs (which index shall be compiled or verified by the Board, with appropriate adjustments to reflect the change in composition of railroad costs, including the quality and mix of material and labor)...."

existing or new regulations to obtain any additional information needed to ensure that "railroad fuel surcharges are being set in such a manner as to insure that they are used only to recover the increased cost of fuel for the particular movements to which the surcharge is applied." Notice at 2.

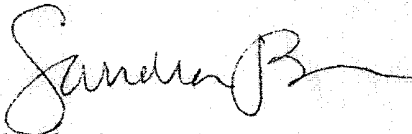
Oversight by the STB is particularly important because of the inability of shippers to determine what unit price level is assumed in newly established transportation rates, i.e., the threshold level at which point the fuel charges "kick in" or become effective, or the then-current fuel cost level.

VI. CONCLUSION

Ameren applauds the Board for taking action on the fuel surcharge issue and holding a public hearing. However, the Board must take definitive steps to rectify the problem following the public hearing. The Board should (1) provide clarification that the lawfulness of a railroad fuel surcharge may be challenged separately from the level of a railroad rate; (2) find that BNSF's and UP's surcharges, and other similarly imposed surcharges, are unreasonable practices in violation of 49 USC § 10702; (3) establish narrow, cost-based standards for recovering actual cost variations of fuel expended for a particular shipper's transportation that are not adjusted by

other means; and (4) require transparency in the submission of revenue and cost data justifying the imposition of railroad fuel surcharges and provide oversight of railroad fuel cost recovery.

Respectfully submitted,



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Appendix A

Public Statements Regarding the Revenue Enhancement of BNSF's Fuel Surcharges

"What hasn't slowed is the railroad's earnings. A 3 percent increase in volume, 6 percent increase in rates and 9 percent increase in fuel surcharges yielded an 18 percent increase in freight revenue and a 20 percent jump in operating income at BNSF in the fourth quarter [2005]. The railroad reported nearly \$13 Billion in revenue last year." John Gallagher, *Assembly Required: Greater Velocity, More Car Turns Outstrip Higher rates, Volume, Rose Says, as BNSF Double Tracks to the Future*, Traffic World, Apr. 3, 2006 at 9.

"Rail carriers reported strong financial results for 2005, citing rare increases and fuel surcharges as major contributors to earnings growth. Rail freight buyers saw nothing but decreased capacity and continued price increases. ... Burlington Northern was able to increase its fuel surcharge by 9% and its rates by about 9% for an 18% gain in freight revenue. This is the ninth straight quarter Burlington Northern has increased its prices." David Hannon, *Shippers see tighter capacity, higher rates continuing*, Purchasing, Mar. 2, 2006 at 30.

"Fourth-quarter freight revenue increased 18 percent to a quarterly record of \$3.45 billion, compared with 2004 fourth-quarter freight revenues of \$2.92 billion. The company said it shipped more units and implemented price increases, and also raised fuel surcharges by 9 percent." *Burlington Northern Fourth-Quarter Earnings Up 24 Percent as Strong Demand Drives Revenue*, Associated Press Financial Wire (Fort Worth, TX), Jan. 24, 2006, § Business News.

"Most of the \$0.05 upside surprise came from a better-than-expected fuel surcharge collection and pricing," James valentine, a rail analyst at Morgan Stanley, wrote Tuesday in a note to clients. He has forecast that the railroad would earn \$1.20 a share. Total operating revenue climbed 19.2 percent for the quarter to \$3.6 billion. For all of 2005, BNSF's net income almost doubled, soaring to \$1.5 billion, or \$4.01 a share, from the year-ago \$791 million, or \$2.10. Total operating revenue rose to \$13 billion, an 18.6 percent jump." Katherine Yung, *BNSF Forecast is Upbeat*, Dallas Morning News, Second Edition, Jan. 25, 2006 at 8D.

The railroad's third quarter 2005 freight revenues increased \$480 million, or 18 percent, to a quarterly record \$3.22 billion compared with \$2.74 billion during the same period a year ago. The increase was a combination of volume, fuel surcharges, and price increases. "BNSF continues to operate a fluid rail network and, as a result, we have recorded our fourteenth consecutive quarter of year-over-year volume increases," Rose said. Revenue for the third-quarter of 2005 included fuel surcharges of \$296 million compared with \$95 million in the third-quarter of 2004. John Gallagher, *Record Profits at BNSF*, Traffic World, Oct. 25, 2005 § Rail at WP.

"We are really pleased looking at our results for the third quarter. Freight revenue increased 16% to an all time high of \$2.7 billion. Of the 16% increase 3% was attributable to fuel surcharges and another 3% was due to price, [said Matt Rose, CEO of BNSF]" *Q3 2004 Burlington Northern Santa Fe Corporation Earnings Conference Call—Final*, Fair Disclosure Wire, Oct. 26, 2004.

"We billed about \$66 Million more fuel surcharge revenue than a year ago... Total freight revenue grew 16%. Coal revenues increased 15% on a 10% increase in volume [said John Lanigan, Exec. VP, BNSF]" Anne Fitzgerald, *SKY HIGH; As Record Grain Yields Pile Up, Fuel Prices Are Soaring to New Heights and Eating Into Profits*, The Des Moines Register, Nov. 7, 2004, § Iowa Agriculture at 1M.

"BNSF Chairman and CEO Matthew Rose and other executives notes that the railroad has a newfound ability to boost rates and add fuel surcharges." Dan Piller, *BNSF sees record revenue in 3rd Quarter*, Fort Worth Star Telegram (Texas), Oct. 27, 2004 at 3C.

"Up until February, for instance, the Burlington Northern and Santa Fe Railway Company charged customers an extra 2.5 percent in fuel surcharges. They will reach 7 percent in November." Kris Axtman, *As Gas Prices Soar, Truckers Battle Record Costs*, Christian Science Monitor, Oct. 4, 2004 at 3.

"With high fuel prices eating into profits, Burlington Northern-Santa Fe Railway has been regularly increasing the fuel surcharges its customers have to pay.... For most of 2004, the surcharge was at or below 5 percent. BNSF has announced that the surcharge will be 16 percent in November. In other words, if a 110-car train is loaded with corn and had a regular shipping rate of \$350,000, another \$56,000 would be added to the transportation cost. The \$56,000 is 16 percent of \$350,000. "In response to feedback from our customers, BNSF announced in March the railroad industry's first mileage-based fuel surcharge program," said John P. Lanigan, the company's executive vice president and chief marketing officer in a statement. BNSF says the change will be revenue neutral. Its purpose is to "better align the fuel surcharge to our customers with the actual incremental fuel cost of transporting their goods." Scott Waltham, *Price spike fuels rising rail rates*, Aberdeen American News (South Dakota), Nov. 4, 2005 at 88.

"North America's biggest railroad, Union Pacific, hit fourth quarter record net income of \$551 million, a 46 percent increase over its 2002 net profit of \$378 million... For the year, revenue increased 4.8 percent over last year, from \$8.98 billion to \$9.4 billion. Net profits increased 7.4 percent to \$816 million in 2003. Fuel figured big for BNSF during the quarter, as it collected \$31 million in fuel surcharges against \$14 million in the fourth quarter 2002." John Gallagher, *Picking Up Steam; Railroads Close Out 2003 With Strong Results, See Fuel Pricing Clouding 2004 Outlook*, Traffic World, Feb. 2, 2004, § Rail at 28.

"Burlington Northern Santa Fe Corp. and Union Pacific collected a combined \$2.12 billion in fuel surcharges last year, compared with \$680 million in 2004, according to securities filings. The add-on fees generated 8% of their total 2005 revenue, compared with 2.9% a year earlier. Fuel expense at the two railroads rose 44% to \$4.35 billion." *Tensions Mount over Fuel Surcharges Set by Railroads*, Wall Street Journal, Apr. 18, 2006 available at: www.wsj.com

Public Statements Regarding the Revenue Enhancement of UP's Fuel Surcharges

"Union Pacific Corp. reported fourth-quarter profit Thursday that topped Wall Street's expectations, with its fuel surcharge and improved operating margins boosting results at the nation's No. 1 railroad operator.... Union Pacific said the main component of its earnings growth

was an 11% increase in average revenue per car. The growth was helped by fuel surcharges—fuel costs rose to an average of \$2.08 a gallon from \$1.46 a gallon—and improvements in yield.” Padraic Cassidy, *Union Pacific 4th-period Profit Higher On Wider Margins*, Dow Jones Business News, Jan. 19, 2006.

“In terms of hedging, our view here is we've got to continue to focus on our fuel surcharge program, getting it -- getting up to 100% over time here. If things dip significantly, we might take a shot at it here in terms of fuel, but right now the fuel surcharges are key.”

JOHN LARKIN: And a question on the fuel surcharge you may have already mentioned this and I may have missed it. But did you mention what percentage of the business is currently on a fuel surcharge?

JIM YOUNG: Rob, do you want to take that?

ROB KNIGHT: We did not mention that, John. But it's about 90% of our revenue base has some sort of a fuel recovery component or another.

JOHN LARKIN: Okay. What would you expect that to be, let's say, at the end of '06?

ROB KNIGHT: It continues to grow. We're not going to be satisfied till it gets to 100% coverage, which won't happen at the end of '06....” *Q4 2005 Union Pacific Earnings Conference Call - Final FD*, (Fair Disclosure) Wire, Jan. 19, 2006.

“Union Pacific Railroad officials said high fuel prices mean they plan to seek larger fuel surcharges from shippers. About 80 percent of the railroad's customers currently are paying the surcharges.” *Robust Freight Volume; Slants & Trends*, U.S. Rail News, Dec. 1, 2004, No. 24, Vol. 27 at 185.

~~“Fuel costs also are hurting earnings, the [Union Pacific] Railroad said. However, a new fuel~~
surcharge program being paid by customers is reducing the impact.” *Union Pacific Corp.*, U.S. Rail News, Jun. 16, 2004, No. 12, Vol. 27, at 94.

“Union Pacific Corp. reported Thursday that second-quarter profit rose 47% as the railroad operator shipped more commodities and gained from a fuel surcharge.” Padraic Cassidy, *Union Pacific's Profit rises on Commodity Shipments*, Marketwatch, Jul. 21, 2005.

“Union Pacific Corp. reported last week that profits more than tripled in the fourth quarter of 2005 as the company benefited from higher rates, greater efficiency and fuel surcharges....

“Union Pacific is operating more efficiently, allowing us to handle record volumes and recover more rapidly from challenges such as hurricanes, the Kansas washouts and severe winter storms,” said James Young, Union Pacific's chief executive officer, who assumed the top job Jan. 1. “We have gained traction throughout the year with our operating initiatives. I am particularly pleased that we converted strong revenue growth into a significant increase in operating income.” Earnings jumped to \$296 million, or \$1.10 per share in the fourth quarter, compared with \$79 million, or 30 cents per share one year earlier.” *Union Pacific reports strong 4th Quarter despite weather and high volumes*, Capitol Press, LLC, Jan. 25, 2006.

“Union Pacific Corp., the largest U.S. railroad, on Thursday announced earnings well above market expectations on fuel surcharges it passed along to customers, price rises and a stable network performance despite bad weather.” Nick Carey, *Corrected—Update 3-Margins, Fuel Charges Boost Union Pacific 4th Quarter*, Reuters, Jan. 30, 2006.