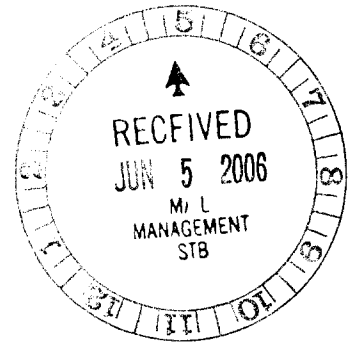


Public Redacted Version
BEFORE THE
SURFACE TRANSPORTATION BOARD

EX PARTE NO. 661
RAIL FUEL SURCHARGES



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UNION PACIFIC REPLY TO
ARKANSAS ELECTRIC COOPERATIVE CORPORATION

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June 5, 2006

**BEFORE THE
SURFACE TRANSPORTATION BOARD**

**EX PARTE NO. 661
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**UNION PACIFIC REPLY TO
ARKANSAS ELECTRIC COOPERATIVE CORPORATION**

On May 15, 2006, Arkansas Electric Cooperative Corporation ("AECC") submitted a report purporting to analyze "the extent of over-recovery of increased fuel expense for the movement of coal from the Powder River Basin to the Independence and White Bluff power plants." May 15, 2006 Letter from Martin Bercovicci, Counsel for AECC. Pursuant to 49 C.F.R. Part 1104.13(a), Union Pacific Railroad Company ("UP") submits this reply. In a separate filing, UP seeks a protective order so that confidential contract terms are not disclosed on the public record.

UP's reply demonstrates that, contrary to AECC's speculation, there is no over-recovery of fuel expense due to fuel surcharge mechanisms. We will first show that no { } to either plant. Then we will show that AECC's speculation about rates and fuel surcharges relative to fuel expense rests on numerous factual errors and faulty assumptions.

AECC Bears No Fuel Surcharge on UP Moves of PRB Coal

AECC's representative at the May 11 hearing, Steve Sharp, head of Fuel Procurement, alleged that fuel surcharges over recover for fuel costs by a total of \$1.5 million annually for the White Bluff plant and \$3 million for the Independence plant. On May 15, AECC filed a report by Mr. Michael Nelson to support Mr. Sharp's claims of railroad over-recovery.¹ The Nelson Report estimated that "the combined over-recovery is at least \$5.0 million per year" for surcharges at April 2006 levels for BNSF² and UP. Id. at 9. The AECC claims and the Nelson Report estimates are wrong as to UP fuel surcharges.

UP recovers no revenue from {
}. The UP contract that
applies to these movements provides that all rates will be adjusted by {
}. No
provision is made for any other adjustment related to changes in fuel costs.

¹ "Rail Fuel Use and Surcharges for White Bluff and Independence Plants" prepared by Michael A. Nelson, dated May 15, 2006. ("Nelson Report").

² BNSF serves the White Bluff plant pursuant to protective conditions imposed on the UP-SP merger and a Settlement Agreement between UP and Entergy STB Finance Docket No. 32760 (Sub-No 21) Decision No. 19 (served 11/08/01) at 8 (hereinafter "SP Merger Decision No. 19"). UP's reply address only the AECC claims regarding the alleged UP over-recovery.

AECC Speculation About Possible Future Fuel Surcharges

Is Rife with Errors

The Nelson Report hedges the scope of its conclusions. It states that in some instances the analysis may reflect the current actual situation; in other circumstances the analysis "may reflect the situation that is expected to exist upon the expiration of existing contracts." Id. at 1. The analysis in the report does not offer any useful insight as to whether or how much UP may recover for fuel surcharges when the existing contract expires { } years from now. Aside from the inherent problems of accurately predicting the future, the analysis in the Nelson Report deserves a failing grade for its estimates of the impact of UP's current fuel surcharge program.

UP urges the Board to be wary of any analysis that purports to predict the amount of over-recovery in the next decade.³ No one can know today whether in { }:

- UP would still apply a fuel surcharge;
- how such a fuel surcharge would be structured;
- what rates would apply to UP transportation to either plant;
- whether UP will still carry PRB coal to White Bluff; or
- what fuel will cost UP.

³ The term of the UP contract expires on { }

Caution in relying on the conclusions in the Nelson Report is especially justified when its estimates for the current impact of UP's fuel surcharge rest on a number of serious errors. These include:

- 1) assuming that the Independence rate is nearly 14% greater than the White Bluff rate. Nelson Report at 3-4. (compare \$13.74/NT to \$12.09/NT) {
}
- 2) increasing the White Bluff rate with an amortization allowance to reflect "fact that the build-out that would permit BNSF to serve the plant has not yet been constructed." Nelson Report at 3. BNSF has served the White Bluff plant since October 2002 and because it relies on trackage rights over UP, it has no need to construct track. SP Merger Decision No. 19 at 8 (served 11/08/01).
- 3) understating UP's current cost for diesel fuel. The Nelson Report assumes that UP's average price for fuel in April was \$1.889/gallon. Id. at 5. As news reports proclaimed ever-rising prices for a barrel of oil and UP's Comments confirmed, prices rose dramatically in April. By the time of UP's first quarter earnings release, we were paying \$2.10/gallon. Id. at 7.
- 4) overstating the "normal" price of fuel where no fuel surcharge would apply. The Nelson Report uses a base fuel price of \$0.763/gallon when the UP surcharges are designed to apply to incremental increases above \$0.75/gallon. Compare Nelson Report at 12 Table 3 and UP Comments at 8.

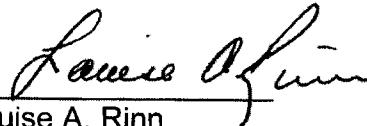
In addition, Mr. Nelson attempts to minimize the amount of fuel consumed by coal trains by suggesting that the slower speed of coal trains relative to intermodal trains and the lower elevations of White Bluff and Independence plants relative to PRB are *the* critical physical characteristics. But elementary physics teaches that weight matters: energy consumption is the product of mass (weight) times distance. Watching locomotives straining to begin movement of a 130-car coal train with more than 15,000 net tons on a flat grade or how, even with an additional locomotive, a coal train struggles up the 1% grade on Logan

Hill in the PRB provides the empirical proof. Likewise, wind resistance encountered by empty cars returning to PRB increases fuel consumption for coal trains.

Conclusion

The additional filing by AECC does not support its claims that it is overpaying UP for fuel costs for PRB.

Respectfully submitted,

A handwritten signature in cursive script, appearing to read "Louise A. Rinn", written over a horizontal line.

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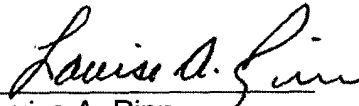
Certificate of Service

I certify that I have this day served a copy of the Public Version of UP's Reply upon the following by first class United States Mail:

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