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VIA E-FILING

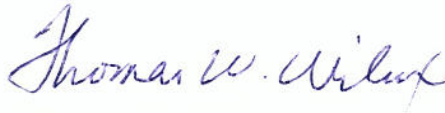
The Honorable Vernon A. Williams
Secretary
Surface Transportation Board
1925 K Street, NW
Washington, DC 20423-0001

Re: **Supplemental Joint Comments of Nevada Power Company, Sierra Pacific Power Company and Idaho Power Company, in response to *Rail Fuel Surcharges*, Ex Parte 661**

Dear Secretary Williams:

Enclosed for filing in the above-referenced proceeding are the Supplemental Joint Comments of Nevada Power Company, Sierra Pacific Power Company, and Idaho Power Company.

Sincerely,



Thomas W. Wilcox
An attorney for Nevada Power Company, Sierra Pacific Power Company and Idaho Power Company

Enclosure

cc: Colleen J. Rice, Esq.
Mr. Tom J. Harvey
Mr. Joseph R. Brignola

**BEFORE THE
SURFACE TRANSPORTATION BOARD**

Ex Parte No. 661

REVIEW OF RAIL FUEL SURCHARGES

**SUPPLEMENTAL JOINT COMMENTS OF IDAHO POWER COMPANY, SIERRA
PACIFIC POWER COMPANY AND NEVADA POWER COMPANY**

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October 2, 2006

**BEFORE THE
SURFACE TRANSPORTATION BOARD**

STB Ex Parte No. 661

RAIL FUEL SURCHARGES

**SUPPLEMENTAL JOINT COMMENTS OF IDAHO POWER COMPANY, SIERRA
PACIFIC POWER COMPANY AND NEVADA POWER COMPANY**

I.

INTRODUCTION

On March 14, 2006, the Surface Transportation Board (“Board” and “STB”) issued a notice of public hearing on rail fuel surcharges to be held on May 11, 2006, and invited interested parties to submit comments on railroad fuel surcharges (hereinafter “Notice”). Idaho Power Company (“Idaho”); Sierra Pacific Power Company (“Sierra”) and Nevada Power Company (“Nevada”) jointly submitted written comments in response to the Notice on April 27, 2006 (hereinafter “Joint Comments”). The identities and interests of Sierra, Nevada, and Idaho are set out in the Joint Comments at pages 4-5. On August 3, 2006, the Board issued a decision in this proceeding, the substance of which is discussed in more detail below, but that also requested additional comment on certain proposals. (“*Decision*”). Idaho, Sierra, and Nevada hereby jointly submit these Supplemental Joint Comments in response to the Board’s request.

The Joint Comments focused primarily on how the Union Pacific Railroad Company’s (“UP”) tariff fuel surcharge, set out in Item 690 of UP’s Circulars 6602-C and 6603-C, Applying

on Loading, Handling, Accessorial Charges, Fuel Surcharges, and General Rules for Trains Originating in (1) Colorado and Utah, and (2) Wyoming, respectively, was designed to enable UP to over recover the fuel costs associated with transportation to Sierra's, Nevada's, and Idaho's coal-fired electric generating facilities. In addition, the Joint Comments urged the STB to "(1) provide clarification that the lawfulness of railroad fuel surcharges may be challenged separately from the level of a railroad rate; (2) clarify that railroad fuel surcharges may only be used for the sole purpose of recovering actual costs of fuel expended for a particular shipper's transportation that are not recouped by other means; (3) take appropriate action to correct Item 690 to the extent it does not comport with the above standard; and (4) require UP submit detailed data reflecting its actual cost of fuel and the revenues associated with fuel cost recovery associated with each Nevada, Sierra, and Idaho movement for which the fuel surcharge was assessed." Joint Comments at 6-7. The Joint Comments stressed the fact that the primary deficiency of Item 690 was that the threshold for assessing a surcharge contained in the surcharge formula was tied to lower fuel prices of several years ago instead of the price UP currently pays for fuel, a formula that operated to automatically assess a fuel surcharge even if current fuel prices were unchanged or even decreased. Id. at 18-19. Moreover, the Joint Comments highlighted the inequities of assessing a fuel surcharge based on a percentage of the base rate. Id. at 19. Finally, the Joint Comments asked the Board to adopt more detailed fuel price and fuel cost reporting requirements in order to make fuel cost recovery by the railroads more transparent. Id. at 20-21.

II.

SUPPLEMENTAL COMMENTS

Idaho, Sierra, and Nevada were pleased that the *Decision* favorably addressed the primary issues they and other parties raised in their comments. More specifically, the Board made the following important rulings:

1. That the Board has jurisdiction under 49 U.S.C. §10702(2) to address the unreasonable practice “of applying what the railroads label a fuel surcharge in a manner that is not limited to recouping increased fuel costs that are not reflected in the base rate.” *Decision* at 4.
2. That it is not a reasonable practice to compute fuel surcharges as a percentage of existing rates. Rather, a lawful surcharge must be “directly tied to and limited to the incremental changes in that particular cost for the movements to which the surcharge is applied. *Id.* at 4-5. Moreover, alternatives to tying a surcharge to an existing rate must “have a reasonable nexus to the fuel consumption of the movement involved.” *Id.* at 5.
3. That it is not a reasonable practice to adjust a rail rate using the Rail Cost Adjustment Factor (“RCAF”) and also assess a fuel surcharge. *Id.*
4. The Board also implicitly ruled that the price of West Texas Intermediate Crude Oil (“WTI Price”) is not an appropriate index upon which to base a fuel surcharge formula. *Id.* at 6.

In conjunction with the above findings, the Board sought public comments on several proposals “designed to preclude [the] unreasonable practice” of assessing what is labeled a fuel surcharge but that is not limited to recouping increased fuel costs not reflected in the base rate. *Id.* at 4.

II.

SUPPLEMENTAL COMMENTS

A. The STB Correctly Applied 49 U.S.C. § 10702(2)

A threshold issue facing the Board concerning the lawfulness of railroad surcharges was whether the STB has authority to regulate the fuel surcharge practices of the railroads. The

Board's affirmance that it has such authority, and the basis for this conclusion, are both sound. See the discussion of the Board's authority to regulate surcharge practices under 49 U.S.C. §§ 10702 and 10704(a)(1) contained in the Joint Comments at 6-9. Idaho, Sierra, and Nevada also refer the Board to similar discussions contained in the comments submitted by other parties in this proceeding.¹

B. Linkage of Surcharge to Actual Movement-Specific Fuel Costs

In the Decision the Board rightfully determined that it is an unreasonable practice under 49 U.S.C. § 10702(2) to compute fuel surcharges as a percentage of existing rates. *Decision* at 4. This is how fuel surcharges are computed and assessed under Item 690. Joint Comments at 17. The Board indicated that a fuel surcharge could pass muster under §10702(2) if it was "directly tied to and limited to the incremental changes in that particular cost for the movements to which the surcharge is applied," and "tied not to the level of the base rate but to those attributes of the movement that directly affect the amount of fuel consumed: either mileage alone, or preferably weight and mileage. Railroads would have discretion to devise an alternative methodology, so long as it would have a reasonable nexus to the fuel consumption for the movement involved." *Id.* In the *Decision*, the Board indicated a preference for a ton-mile approach.

Sierra, Idaho and Nevada fully support the requirement that a fuel surcharge must have a direct correlation to the increases and decreases in the fuel costs specific to a particular movement. As stated above, however, implementation of this important standard requires three important factors: (1) the starting point, or base, of the unit fuel price in a fuel surcharge formula must match the unit price for fuel embedded in the base rate; (2) the surcharge must be limited to

¹ See, e.g., Written Testimony Submitted by the National Industrial Transportation League, dated April 27, 2006 at 22-25; Comments of the Concerned Captive Coal Shippers, dated April 27, 2006 at 9 -11; Testimony of the Edison Electric Institute at 2-5; Comments of Ameren Energy fuel and Services Co., dated April 27, 2006 at 8-11.

permitting the railroad to recoup only those additional costs that are not recovered by other means; and (3) the surcharge must not only require a shipper to pay fuel cost increases but also provide for credits to the shipper in the event that fuel prices decrease below the base unit price.

As to the first point, a significant reason why the current fuel surcharge formulas utilized by the railroads are an unreasonable practice under §10702(2) is that they contain thresholds tied to lower fuel prices of the 2002 timeframe. Id. at 20-22. To the extent that a purported fuel “surcharge” contains a threshold tied to a fuel cost level that is lower than the fuel cost embedded in the base rate, the formula will calculate “surcharge” revenues even if the fuel costs embedded in the base rate do not increase (or even if they decline if the threshold is low enough), thus providing the railroad with revenues in excess of actual fuel costs. Id. at 18-19. As Idaho, Sierra and Nevada pointed out in the Joint Comments, a significant reason why Item 690 over recovers the fuel cost of UP for a particular movement is that UP has not adjusted the surcharge threshold to account for the fact that increases in the price of diesel fuel that UP has paid since the 2002 timeframe are included in new transportation rates. Id.

An important but unstated underlying assumption in the *Decision* is that a railroad’s current cost of fuel is accounted for the base rates provided to a shipper. This assumption is reasonable and logical, since it would seem illogical and counter to good business practice to assess a base rate that did not reflect the current price of all factors that made up the relevant service. In its comments in this proceeding UP discussed in detail how diesel fuel prices have increased since 2002. Comments of Union Pacific Railroad Company at 10-11. However, the comments submitted by UP and other Class I railroads in this proceeding are silent on the extent to which new rates developed and offered to shippers during the 2000 – 2006 have taken into account increased fuel prices, thereby obviating the necessity for an older fuel price threshold for

that shipper. See Id.; Comments of CSX Transportation at 6; Written Statement of Norfolk Southern Railway at 4-8.

Moreover although it is relatively easy to determine the price a railroad pays for diesel fuel in a given year, when railroads supply base rates they typically do not supply the customer with a breakdown of the fuel and non-fuel costs embedded in a given rate. Without this information the validity of a fuel surcharge cannot be determined and verified because (1) the starting point for purposes of establishing the necessary linkage between a surcharge and fuel cost embedded in the rate cannot be established; (2) the extent of “double-dipping” cannot be calculated; and (3) the appropriate industry index to be used in a surcharge formula cannot be accurately determined. To resolve this problem, Idaho, Sierra, and Nevada suggest that the Board adopt one or both of two mechanisms. First, the Board could adopt rules that require a railroad, when it supplies a base rate, to supply and convincingly demonstrate the fuel cost that is included within that rate. Second, the Board could adopt a rebuttable presumption that the railroad’s current fuel cost is represented in any base rate provided to a rail shipper. Such current costs can easily be determined using the STB’s URCS costing methodology or the reporting requirements adopted in this proceeding. This rebuttable presumption would apply to both common carrier and proposed contract rates. Such a presumption is entirely appropriate, since it must be assumed that the railroad acted prudently and established rates at levels that cover all of the current operating costs of the movement. For this reason, the railroad’s burden for overcoming the presumption should be high, and the railroad should be required to convincingly demonstrate that the price of fuel embedded in a given rate is not what the railroad pays for fuel at the time the rate is offered.

C. “Double Dipping” and Use of the RCAF

The Decision also determined correctly that the assessment of a fuel surcharge in addition to adjusting the base rates using the RCAF is an unreasonable practice under §10702(2) because it charges the customer twice for the same fuel cost increases. The Board noted this occurs when the base rate is increased using the RCAF (or similar index with a fuel component) and then this increased rate is assessed a fuel surcharge. *Decision* at 5-6. The Board has proposed to generally prohibit the use of a fuel surcharge to recover increases in fuel costs to the extent those same fuel cost increases are recovered through the application of the RCAF other rate adjustment mechanisms that take into account fuel cost increases. Idaho, Sierra, and Nevada support this proposal. Nevertheless, the Board stated in the *Decision* that “[r]ailroads could continue to collect a fuel surcharge if they remove the fuel cost component from the RCAF (or other index) used to escalate the base rate. That approach would have the benefit of avoiding the longer time lag for recovery that is associated with the quarterly RCAF, in favor of a fuel surcharge that is adjusted more rapidly.” *Decision* at 6. Idaho, Sierra, and Nevada believe that the extent to which the RCAF lags behind actual increases to the detriment of railroads has been overstated. First, the RCAF methodology is based on fuel price forecasts provided by the railroads themselves that take into account the fluctuation of railroad diesel prices caused by events in the world oil markets. Joint Comments at 11, citing filing made by the AAR on December 5, 2005 describing the damage done by hurricanes Katrina and Rita as largely responsible for the rise in the fuel component of the RCAF. Ex Parte No. 290 (Sub-No. 5) (2006-1), *Quarterly Rail Cost Adjustment Factor*, AAR forecast, Appendix B (page 1) (filed Dec. 5, 2005). Thus, the railroads have the ability to minimize potential lag time through accurate forecasting. The railroads have made no showing in this proceeding that fuel prices have exceeded their forecasts in the past

several years to the point that an accelerated recovery of fuel costs is justified and necessary. Moreover, to the extent that the railroads believe the RCAF is not allowing them to recover their fuel costs in a timely fashion, they can seek appropriate relief from the Board. See Joint Comments at 11. Second, the Board must recognize that any “lags” under the RCAF flow both ways. Specifically, while the Decision focuses on the inability to quickly recoup fuel price increases, the STB must also take into account that to the extent the price a railroad pays for fuel rapidly decreases ahead of the operation of the RCAF, the railroad receives the benefit of the cost savings pending the quarterly adjustment to the RCAF.

The Board’s concern with “time lag” led to its endorsement in the *Decision* of the relatively recent practice of purportedly recovering fuel costs by applying a rate adjustment mechanism without a fuel cost component and assessing a separate “fuel surcharge.” In Idaho’s, Sierra’s and Nevada’s experience, this has meant using the AAR’s All Inclusive Index Less Fuel (“AIILF”) in combination with Item 690. However, the AIILF is a creation of the AAR that has not been not formally approved by or subject to the approval of the STB. As such, unlike the RCAF, the AIILF index can be modified in any respect by the Class I railroads through the AAR without seeking the Board’s permission. Joint Comments at 12. More significantly, the assessment of a fuel surcharge in this manner, *i.e.*, in combination with an index that does not have a fuel cost component, is really not a true “surcharge” at all. Rather, the combined index and “surcharge” become a surrogate for the RCAF with the fuel component. If the Board is really concerned with the speed at which fuel costs can be recovered under the RCAF, then the Board should work within the RCAF process instead of endorsing the use of the AIILF (or similar index) in combination with a fuel surcharge to be a surrogate for the RCAF with the fuel component. Working within the RCAF process is the better, more transparent, and more

equitable means to address these concerns. In any event, to the extent the Board permits the AAILF or other alternative indices to be used with a fuel surcharge to recover fuel costs, it should require the railroad to convincingly demonstrate that the fuel costs it seeks to recover via a surcharge are not embedded in the base rates or recovered by any other means.

D. Use of the U.S. No. 2 Diesel Retail Sales by All Sellers (Cents per Gallon)

In the *Decision*, the Board proposed to require all Class I railroads to use “a single, uniform index to measure increases in fuel costs.” *Decision* at 6. Presumably, the Board intends for such index to be used when the RCAF with the fuel component is not being used to recover fuel costs. In any event, the *Decision* proposes that railroads use the Energy Information Agency’s “U.S. No. 2 Diesel Retail Sales by All Sellers (Cents per Gallon)” (“HDF”). *Id.* This is the price index used by Item 690.

As Idaho, Sierra, and Nevada pointed out in the Joint Comments, the HDF is not a measurement of UP’s true fuel costs. Joint Comments at 19-20. Instead of using a retail highway fuel price index, Idaho, Sierra and Nevada submit that the goal of producing a fuel surcharge that solely (1) compensates the railroads for fuel cost increases that are not recovered in the base rate or and adjustment formula, and (2) credits the shipper when the price of fuel declines below the base price level would be best accomplished using actual railroad fuel price data. For example, there does not seem to be any impediments to using (1) the actual fuel cost data supplied to the Board on a per gallon basis by the railroads; or (2) the AAR fuel cost index, both of which are rail-based measurements as opposed to a retail highway-based index.

That being said, the HDF index appears to be an acceptable alternative because changes in the index prices have highly correlated with railroad fuel prices. *Decision* at 6. The much larger and more significant issue, however, is that whatever index the Board selects, the use of

such an index must be subject to the previously discussed requirements that (1) the threshold for assessing a fuel surcharge must match the price of fuel embedded in the base rate; and (2) the fuel surcharge mechanism must be limited to permitting the railroad to recover actual and verifiable fuel costs above the base level, and crediting the shipper when fuel costs drop below the base level. More specifically, while Item 690 uses the HDF index, the surcharge formula does not reflect current fuel prices paid by UP and embedded in newer rail rates. The percentage multiplier applied to the base rate, which the *Decision* also found to be unlawful, compounds the over recovery. Joint Comments at 18-20.

E. Reporting Requirements

Idaho, Sierra, and Nevada commend the Board for proposing increased reporting requirements for fuel prices and costs, and for requiring the railroads to immediately comply with such requirements. These parties respectfully submit that additional reporting requirements are necessary. These are summarized as follows:

- a. The Class I railroads should report cost statistics in their monthly report by major commodity group as reported in the railroad's financial reports, and separated between interchange and non-interchange traffic;
- b. The Class I railroads should report cost increases recovered through both fuel surcharge and non-surcharge price recovery mechanisms by each commodity group.

These additional reporting requirements would allow the STB and rail shippers to ascertain the extent to which railroad cost recovery mechanisms "double dip" fuel cost recovery in violation of the *Decision*, as well as the extent to which one type of traffic or traffic group is disproportionately supplying a majority of a railroad's fuel price recovery. This additional information would also help provide the necessary transparency to the process of establishing valid fuel surcharges.

F. The Board's *Decision* is Only One Part of Re-Balancing the Interests of Railroads and Their Customers

The *Decision* reflects a recognition on the part of the Board that the tariff fuel surcharges implemented by the Class I railroads are designed to overcompensate them for the fuel costs they incur for a particular movement. The assessment of such surcharges is clearly an unreasonable practice under 49 U.S.C. §10702(2). Given these findings, Idaho, Sierra, and Nevada believe the Board should have gone farther than “admonish[ing] the railroads to reexamine their method of calculating fuel surcharges.” *Decision* at 5. The Board could have and should have ordered the railroads to immediately modify their tariff “fuel surcharges” to be consistent with the *Decision's* findings. The Board should emphasize that the clear intent of the standards set out in the *Decision* was that railroad tariff fuel surcharges will be reduced.

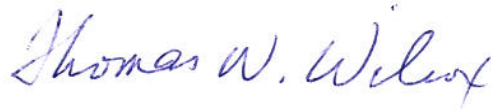
It is imperative that the *Decision* is accompanied by meaningful changes to the Board's rules and procedures for establishing reasonable rail rates, and by actions on the part of the Board to increase competition in the railroad industry. Failing to fix the current rate setting rules and procedures and generally facilitating more competition in the industry will provide opportunities to the railroads circumvent the *Decision's* salutary findings. For example, some railroads may seek to obtain the same revenues they previously obtained via a now-unlawful fuel surcharge through precipitous increases in base transportation rates. To the extent the STB has jurisdiction over the rates at issue such action would require shippers to determine the reasonableness of such revenues in a stand alone rate complaint case, an avenue which presently is extremely expensive, burdensome, time consuming, and of extremely uncertain outcome. The Board should address this issue in its subsequent decisions in this proceeding, and state that the act of “rolling in” former fuel surcharge revenues into existing common carrier rates and offered contract rates is itself an unreasonable practice under § 10702(2). In any event, the STB must

anticipate that even if fuel surcharges are reduced as a result of the efforts of the Board in this proceeding, that is far from the end of the matter on the question of whether the revenues the railroads are charging their customers in rates and surcharges are lawful and reasonable.

VI. Conclusion

In conclusion, Idaho, Sierra, and Nevada commend the Board for taking action that corrects the current fuel surcharge practices of the Class I railroads. These parties generally support the findings the Board made in the Decision, and they offer these additional comments on the various proposals to preclude the current unreasonable practice of assessing fuel surcharges that are designed to recover significantly more revenues from a particular movement than just increases in fuel costs that are not reflected in the base rates and recovered by rate adjustment mechanisms.

Respectfully submitted,



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