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October 11, 2006

BY HAND DELIVERY

Honorable Vernon A. Williams
Secretary
Surface Transportation Board
1925 K Street, N.W., Room 711
Washington, D.C. 20423



Re: Ex Parte No. 657 (Sub-No. 1), Major Issues in Rail Rate Cases

Dear Secretary Williams:

Enclosed for filing in the referenced proceeding please find an original and 20 copies of the Joint Reply of Western Coal Traffic League, Concerned Captive Shippers, Western Fuels Association, Inc., Edison Electric Institute, National Rural Electric Cooperative Association and American Public Power Association to Supplemental Comments of BNSF Railway Company.

An additional copy of the Joint Reply also is enclosed. Kindly indicate receipt and filing by time-stamping this copy and returning it to the bearer of this letter.

Thank you for your attention to this matter.

Sincerely,

A handwritten signature in dark ink, appearing to read "Chris A. Mills".

Christopher A. Mills

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Enclosure

**BEFORE THE
SURFACE TRANSPORTATION BOARD**

MAJOR ISSUES IN RAIL RATE CASES	)	Ex Parte No. 657 (Sub-No. 1)
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**JOINT REPLY OF
WESTERN COAL TRAFFIC LEAGUE
CONCERNED CAPTIVE COAL SHIPPERS
WESTERN FUELS ASSOCIATION, INC.
EDISON ELECTRIC INSTITUTE
NATIONAL RURAL ELECTRIC COOPERATIVE ASSOCIATION
AND
AMERICAN PUBLIC POWER ASSOCIATION
TO SUPPLEMENTAL COMMENTS OF BNSF RAILWAY COMPANY**

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**National Rural Electric Cooperative
Association**

Dated: October 11, 2006

**BEFORE THE
SURFACE TRANSPORTATION BOARD**

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TO SUPPLEMENTAL COMMENTS OF BNSF RAILWAY COMPANY**

The Western Coal Traffic League, the Concerned Captive Coal Shippers, Western Fuels Association, Inc., the Edison Electric Institute, the National Rural Electric Cooperative Association and the American Public Power Association (collectively, "Coal Shippers") hereby reply to the Supplemental Comments of BNSF Railway Company ("BNSF") filed in this proceeding on October 4, 2006 ("Supplemental Comments").

BNSF's Supplemental Comments are not permitted under the procedural schedule governing this proceeding. Moreover, they essentially repeat the arguments made by BNSF in BNSF's opening, reply and rebuttal comments filed in response to the Board's Decision in this proceeding served February 27, 2006, at 3 ("*Decision*"). The Board should not consider BNSF's impermissible cumulative Supplemental Comments. If considered, BNSF's supplemental arguments should be rejected.

I.
THE BOARD SHOULD NOT CONSIDER BNSF'S FILING

This proceeding is governed by a procedural schedule.¹ That schedule calls for three rounds of Comments: Opening Comments (due May 1, 2006); Reply Comments (due May 31, 2006); and Rebuttal Comments (due June 30, 2006). This schedule does not permit or contemplate any additional “supplemental” filings by the parties, much less ones made shortly prior to the announced due date for a final decision in this proceeding (October 30, 2006).²

Ostensibly, BNSF submitted its Supplemental Comments to address a “new issue” that “arose after the end of the comment period” and that “involves the Board’s decision served July 28, 2006, in STB Ex Parte No. 646 (Sub-No. 1), *Simplified Standards for Rail Rate Cases*.” *Id.* at 2. (“*Simplified Standards*”) However, the “new” issues allegedly implicated by *Simplified Standards* are not new at all in the instant proceeding. These issues – the allocation of revenue on cross-over traffic between a stand-alone railroad (“SARR”) and the residual incumbent and the methodology for setting a maximum reasonable rate if SAC revenues exceed SAC costs – were raised by the Board in its *Decision* herein and fully addressed by interested parties in three rounds of written comments.

¹ See *Decision* at 39.

² See *Decision* at 3 (“We intend to issue our final decision within 120 days after all comments have been received”). As required by the *Decision*, rebuttal comments were filed on June 30, 2006, so the decision date is October 30, 2006.

In *Simplified Standards* the Board proposed to apply some of the same SAC methodologies that it uses in “full-SAC” proceedings to a new category of medium-sized rail rate disputes involving a “simplified SAC methodology” “(SSAC)”. *See id.* at 12-14. The Board’s action in *Simplified Standards* is not a valid reason to permit BNSF belatedly to submit additional comments in this proceeding. To the extent BNSF wishes to address issues involved in the *Simplified Standards* proceeding, it is free to do so in its opening comments in that proceeding, which are due on October 24, 2006.³

In this regard, the Coal Shippers note that while the Board indicated that it would apply some of the same methodologies in SSAC cases that it adopts in the instant proceeding, this is nothing more than a proposal. BNSF is free to propose alternative methodologies for SSAC cases, and the Board is free to adopt an alternative methodology if it believes this is warranted. In short, there is absolutely no valid reason for permitting BNSF to have another bite at the apple in this proceeding under the guise that similar issues may also arise in the *Simplified Standards* proceeding.

II.

BNSF’S REPETITIVE ARGUMENTS ARE WITHOUT MERIT

BNSF presents nothing new in its Supplemental Comments. Rather, it re-hashes its previous comments and objections to the methodologies proposed by the Board

³ BNSF itself has indicated its intent “to develop a full record on these issues in its comments in Ex Parte No. 646.” Supplemental Comments at 4.

in the *Decision* for allocating revenue on cross-over traffic and for setting maximum reasonable rates when SAC revenues have been found to exceed SAC costs. The Coal Shippers responded to BNSF's positions and arguments in their Reply Comments and in their Rebuttal Comments.

A. Maximum Rate Determinations

In its *Decision*, the Board properly concluded that its "percent reduction" method for setting SAC rates is severely flawed because railroad defendants can use it to "manipulate the outcome of the Board's regulatory process." *Id.* at 7. The Board proposed two alternatives to percent reduction, the Maximum Contribution Methodology ("MCM") and the Maximum Mark-up Methodology ("MMM"), that addressed these manipulation concerns.

In its Opening and Reply Comments in this proceeding, BNSF asserted that the Board's proposed MCM and MMM methodologies for allocating SAC rate relief flouted differential pricing principles by imposing uniform average rates per ton-mile, or average revenue-to-variable cost ratios, on SARR traffic. BNSF repeats these arguments in its Supplemental Comments.

In their Reply Comments and their Rebuttal Comments, the Coal Shippers demonstrated that, in fact, both the MCM and the MMM methods are consistent with the differential pricing principles that underlie the *Coal Rate Guidelines* because they allocate SAC among the shippers in a SARR traffic group in a manner that respects their relative

elasticities of demand (as measured by the underlying rate structure). In addition, both methods properly allocate SAC revenue reductions to the most demand-inelastic SARR customers. *See* the Coal Shippers' Reply Comments at 13-18, Rebuttal Comments at 8-11; Rebuttal Verified Statement ("V.S.") of Dr. George Borts at 3-5.⁴

The Coal Shippers also demonstrated that the MCM/MMM methods, as well as rate reduction methods presented in two pending rate cases, are superior to the present "percent reduction" methodology for allocating SAC relief from the standpoint of consistency with demand-based Ramsey pricing principles. *See* Coal Shippers' Opening Comments at 17-24. All of the shipper-supported methods are intended to provide rate relief to the SARR's most demand inelastic traffic. In contrast, under percent reduction, each shipper in the SARR traffic group gets exactly the same percentage reduction in its rates, regardless of its demand elasticity – a result which squarely conflicts with demand-based pricing principles.

B. Cross-Over Traffic Revenue Allocations

The STB, and the ICC, have consistently used mileage-based methods to set SARR divisions on cross-over traffic. These methods properly consider market and cost

⁴ BNSF's citation of *Burlington Northern Railroad Co. v. United States*, 985 F.2d 589 (D.C. Cir. 1993) ("*Burlington Northern*") in support of its challenge to MCM and MMM (Supplemental Comments at 5-6) is neither new nor apposite. BNSF previously cited *Burlington Northern* in its initial Comments in this proceeding (*id.* at 36-37). Moreover, *Burlington Northern* did not involve calculations of SAC. Instead, it addressed ICC-sponsored alternatives to the SAC test.

factors. *See* Coal Shippers Opening Comments at 47-48. In its *Decision*, the STB proposed a new method to set SARR cross-traffic divisions – the Average Total Cost (“ATC”) method. This proposed method was opposed by shippers and railroads alike. As succinctly summarized by UP’s Witness Neels, “there is remarkable agreement among railroads and shippers” that the ATC method “suffers from incurable” methodological defects. *See* UP Reply Comments, V.S. Neels at 2-3. These defects include ATC’s arbitrary assignment of fixed costs; ATC’s failure to consider line-specific investments; ATC’s failure to consider market factors; and ATC’s inherent revenue shortchanging of low mileage, high density SARR’s. *See* Coal Shippers’ Opening Comments at 48-54; Reply Comments at 22-24; Rebuttal Comments at 17-20.

In its opening, reply and rebuttal comments in this proceeding, BNSF asked the Board to adopt a new method other than ATC to set cross-over traffic divisions; argued that cost-based approaches like ATC “have the potential for introducing bias into the SAC results;” and supported the Board’s adoption of ATC only if the Board permitted carriers to address “bias” issues raised in individual cases. *See* BNSF Opening Comments at 47-54.

In its Supplemental Comments, BNSF contends that ATC “is a proper methodology” to set SARR cross-over divisions. *Id.* at 10. In so doing, BNSF fails to tell the Board that ATC is not BNSF’s first divisions choice; BNSF ignores its prior

reservations concerning “biased” results from ATC; and BNSF ignores the overwhelming record evidence demonstrating ATC should not be adopted by the Board.⁵

BNSF also argues in its Supplemental Comments that application of ATC “would not involve significant burdens.” *Id.* at 11. In fact, ATC is far more complicated to implement than the STB’s current mileage-based division formulas because ATC requires access to, and review of, detailed internal carrier line-specific density data. This is a time-intensive and expert-driven exercise that requires additional discovery by complainants in SAC rate cases. Moreover, some carriers, including those that have been defendants in STB rate cases, do not maintain the line-specific data bases needed to apply ATC. *See Minnesota Power, Inc. v. Duluth Missabe and Iron Range Ry.*, STB Docket No. 42038 (STB served May 11, 1999) at 7 (Defendant carrier “states it does not keep track of gross ton-miles either for line segments or for valuation sections”).

CONCLUSION

The Coal Shippers submit that BNSF’s Supplemental Comments raise no “new” issues. All issues BNSF raises have already been exhaustively addressed in the parties’ opening, reply and rebuttal comments. Accordingly, BNSF’s Supplemental Comments should not be considered by the Board. If considered, BNSF’s supplemental arguments should be summarily rejected.

⁵ The Coal Shippers’ detailed response to BNSF’s internally contradictory positions and evidence concerning SARR divisions on cross-over traffic is set forth in their prior comments. *See, e.g.*, Coal Shippers Rebuttal Comments at 18 and Rebuttal V.S. Crowley at 66-74.

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Dated: October 11, 2006

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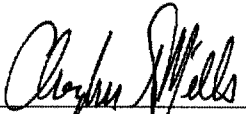
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Association

CERTIFICATE OF SERVICE

I hereby certify that on this 11th day of October, 2006, I caused a copy of the foregoing Reply to Supplemental Comments of BNSF Railway Company and accompanying cover letter to be served by hand-delivery upon counsel for BNSF Railway Company, and by first-class United States mail in the case of all other parties of record in this proceeding.



Christopher A. Mills