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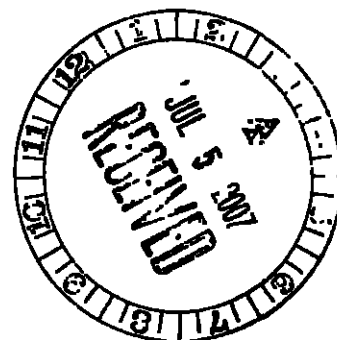
July 5, 2007

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VIA HAND DELIVERY

The Honorable Vernon A. Williams
Secretary
Surface Transportation Board
Attn: STB Ex Parte No. 672
395 E Street, SW
Washington, D.C. 20423-0001

Re: Ex Parte No. 672, Rail Transportation of Resources
Critical to the Nation's Energy Supply

Dear Secretary Williams:

Please find an original and ten (10) copies of the Written Testimony of Dairyland Power Cooperative in the above-referenced proceeding.

We have enclosed an additional copy of this Written Testimony. Please indicate receipt and filing by time-stamping this copy and returning it with our messenger.

Thank you for your attention to this matter.

Sincerely,

A handwritten signature in black ink, appearing to read 'John H. LeSeur'.

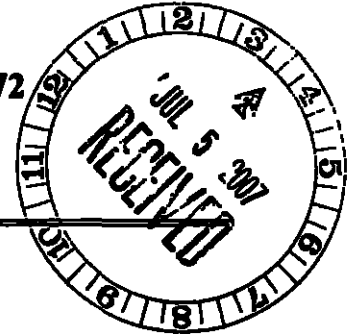
John H. LeSeur
An Attorney for
Dairyland Power Cooperative

Enclosure

**BEFORE THE
SURFACE TRANSPORTATION BOARD**

**RAIL TRANSPORTATION
OF RESOURCES CRITICAL
TO THE NATION'S ENERGY
SUPPLY**

Ex Parte No. 672



**WRITTEN TESTIMONY OF
DAIRYLAND POWER COOPERATIVE**

My name is Dennis Rackers. I am Director of Procurement for Dairyland Power Cooperative ("Dairyland"). As Director of Procurement, I am responsible for obtaining coal and coal transportation for Dairyland. Dairyland appreciates the opportunity to participate in this hearing.

Dairyland is a generation and transmission utility based in LaCrosse, Wisconsin that provides wholesale electricity and other services for 25 electric distribution cooperatives and 18 municipal utilities. These cooperatives and municipals, in turn, supply the energy needs of more than half a million people.

Dairyland's service area encompasses 62 counties in five states (Illinois, Iowa, Michigan, Minnesota, and Wisconsin), providing reliable electrical energy and related services to its customers. The utility's mission is to provide competitively priced energy and services to its customers and maximum value to its owners, consistent with the wise use of resources.

Dairyland owns and operates three coal fired generating stations: Alma, Genoa and Madgett. These stations collectively burn over 3 million tons of coal annually. This coal has been sourced from low-sulfur western mines because this fuel has been the most cost-effective method of compliance with Dairyland's sulfur-dioxide emission limits. All of this coal has been transported in whole, or in part, by western rail carriers under contract or common carrier arrangements.

RATES

For many years, Dairyland paid reasonable rates to the railroads providing us with coal transportation service, but that is no longer the case. Our rail contracts with the western carriers expired at the end of 2005. Dairyland's rail rates went up, on average, 93% on January 1, 2006 (including fuel surcharges), raising our total rail bill to about \$75 million annually at that time (it is now even higher). Dairyland's rates increased so dramatically because of fundamental dysfunctions in the western coal transportation marketplace, including the following:

- **Public Pricing.** Dairyland traditionally received coal transportation service via confidential contracts. Now approximately two-thirds of our rail business moves under so-called "public pricing" documents manufactured by Burlington Northern Santa Fe Railway ("BNSF") and Union Pacific Railroad Company ("UP"). Dairyland's high public rail prices provide clear signals between these western carriers concerning their elevated pricing aspirations for the Dairyland traffic.

- **Refusals to Bid.** A significant portion of Dairyland's coal traffic goes to two plants which are served by barge transportation (Alma and Genoa). These plants are "competitive plants" in the sense that BNSF and UP can compete to transport coal by rail from western mines to rail-to-barge transloading facilities located on the Mississippi River. Subsequently, the coal moves by barge to the Alma and Genoa Stations. Prior to the expiration of our contracts, we asked UP and BNSF to provide us with proposals for this business. BNSF refused to do so and UP offered its public pricing. "Competition" does not work in a duopoly market if one of the duopolists refuses to bid.

- **Fuel Surcharges.** The base rail rates imposed on us in 2006 were set at a time of high fuel prices. However, our fuel surcharge payments are determined by changes in fuel prices relative to prices that prevailed in 2002 – not the changes that have occurred since the new base rates went into effect in 2006. Needless to say, the 2002 fuel price levels were substantially lower than the 2006 fuel price levels. Also, the fuel prices used in the surcharge formulas are not railroad-incurred fuel prices but substantially higher highway fuel prices. *The net effect of the carriers' surcharge mechanisms is to provide substantial additional profit recovery under the guise of fuel cost recovery.*

Dairyland's experiences with the new western rail transportation marketplace are not unique. I have spoken with many other western coal shippers who have had similar experiences. The general consensus in the western coal transportation market is that rates on formerly competitive western coal movements are rapidly rising

because BNSF and UP have stopped competing. Rates on captive movements are also increasing dramatically.

SERVICE

Like many western coal-fired utilities, Dairyland was hard hit by rail service problems first from Utah in 2004 and then from the Powder River Basin in 2005-2006. These service disruptions prevented Dairyland from getting the bituminous and PRB coals needed to meet its generation requirements. As a result, Dairyland was forced to pay higher prices for replacement coal and purchased power. Today, Dairyland's rail service is better than it was in the 2004-2006 timeframe, but we remain concerned about when the next unexpected service crisis will hit the western coal transportation marketplace.

Dairyland is also very concerned that the western railroads are no longer offering to it any meaningful form of binding service guarantees. Based upon my discussions with other shippers, Dairyland's experience is commonplace. The western carriers appear to have jointly decided not to offer any meaningful service guarantees anymore to their coal shippers. In the past, coal shippers had some form of contractual remedies for bad service – but not today.

CONSUMER IMPACTS

The impact of high prices, and poor service, has had significant adverse impact on our utility customers. These impacts were summarized in our Annual Report.

Like other shippers who rely on the railroads for transportation, Dairyland has experienced

severe deterioration in the quality of rail service. In the last two years, failure by the railroads on several occasions to meet contractual delivery obligations forced Dairyland to seek alternative coal sources or curtail power plant generation due to inadequate coal inventories. This has led to higher costs, since replacement coal has generally cost more, , and energy purchased on the market is usually based on natural gas prices, which are dramatically higher than coal.

Even as service quality is suffering, railroads are taking advantage of a lack of competition in the rail industry to impose drastically higher rail rates. Dairyland experienced a 93 percent average increase in rail rates as of January 2006. On an annual basis, it will now cost about \$75 million to ship \$30 million worth of coal. This means transportation will account for over 70 percent of Dairyland's delivered coal cost in 2006.

The magnitude of this increase, combined with coal supply and purchased power costs, forced Dairyland's Board of Directors to raise rates by about 20 percent to maintain our cooperative's financial strength. While our members have worked hard to absorb some of the impact, cost increases must ultimately be passed on to our consumer-members. Unfortunately, this is at a time when consumers are also being subjected to dramatic price increases in home heating fuels, gasoline and diesel fuels.

Dairyland's 2005 Annual Report at 2. The current dysfunction in the western coal transportation marketplace hurts our customers and both the regional and national economies.

WHAT THE BOARD CAN DO

Dairyland suggests that the Board consider the following remedial actions:

- **Maximum Rates.** The STB has jurisdiction to determine maximum rates in captive rail markets. The STB's recent decisions in coal rate cases have been very disappointing to coal shippers. Dairyland urges the Board to reassess its coal ratemaking authority to reach results that strike a better balance of the needs of railroads, shippers and the consuming public.
- **Rail Fuel Surcharges.** Dairyland appreciates the Board's action and decisions in the **Rail Fuel Surcharges** proceeding (Ex Parte No. 661). Dairyland hopes that the Board will take additional actions, on individual complaints, to address shipper-specific complaints that the surcharges they are paying do not reflect applicable actual carrier fuel cost changes incurred in handling their movements.
- **Competitive Problems.** Dairyland urges the Board to conduct a thorough and complete investigation of carrier actions in the formerly competitive western coal transportation marketplace, including the use of public pricing; refusals to deal; and other anticompetitive actions. Dairyland also urges the Board to reconsider its prior decisions involving competitive access and bottleneck rate relief.
- **Infrastructure.** Dairyland joins other groups, such as the Western Coal Traffic League, in asking that the Board take a close look at railroad claims that "infrastructure" needs necessitate the huge rate increases western carriers are forcing on Dairyland and other western coal shippers. Dairyland supports a strong national coal

delivery network by rail but opposes monopoly and duopoly price gouging of coal shippers to subsidize railroad shareholders.