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via Hand Delivery

Hon. Vernon A. Williams
Secretary
Surface Transportation Board
395 E Street, S.W.
Washington, D.C. 20423

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Re: AEP Texas North Company v. BNSF Railway Company.
Docket No. 41191 (Sub-No. 1)

Dear Secretary Williams

Attached are the original and 10 copies of BNSF Railway Company's Petition for Reconsideration in the above-captioned matter and a CD containing a PDF copy of the Petition. Also attached is the required filing fee.

Thank you for your consideration to this matter.

Sincerely,



Anthony J. LaRocca

Enclosure
cc: Parties of Record

**BEFORE THE
SURFACE TRANSPORTATION BOARD**

AEP TEXAS NORTH COMPANY	)	
v.	)	STB Docket No. 41191 (Sub-No.1)
BNSF RAILWAY COMPANY	)	

BNSF RAILWAY COMPANY'S PETITION FOR RECONSIDERATION

PREFACE AND SUMMARY OF ARGUMENT

Pursuant to 49 C.F.R. §1115.3, BNSF Railway Company ("BNSF") requests that the Board reconsider two aspects of its September 10, 2007 decision in the above-captioned case ("Decision")

First, the Board should reconsider its decision to provide AEP Texas North Company ("AEP Texas") with an opportunity to submit new SAC evidence in this proceeding. The Board erroneously concluded that "fairness dictates that AEP Texas have an opportunity to modify its SAC presentation in light of" the Board's adoption of the Average Total Cost ("ATC") revenue allocation methodology. Decision at 23. To the contrary, fairness dictates that this proceeding be terminated immediately.

Over 10 years ago, the Board ordered BNSF to reduce its rates for transportation of PRB coal to AEP Texas' Oklahoma Station by more than 30 percent. The Board also identified maximum reasonable rates for a 20-year period based on the SAC evidence submitted by AEP Texas' predecessor. While the rate prescription did not extend to movements from the PRB mines at issue in this proceeding, BNSF nevertheless adopted the Board's SAC rate prescription in setting the rates at issue here to ensure that the rates would not exceed a reasonable maximum rate. The rates challenged by AEP Texas in this proceeding have never exceeded the SAC-based

rates determined by the Board in its 1996 decision. Because BNSF never charged rates higher than those that the Board had determined were reasonable, it is hardly surprising that the Board's September 10, 2007 decision found the challenged rates to be reasonable. It is grossly unfair to require BNSF to have to defend, yet again in a new round of SAC evidence, the reasonableness of rates that have now been found on two separate occasions to be reasonable.

The Board's adoption of ATC does not justify giving AEP Texas another chance to submit SAC evidence. AEP Texas sought to use favorable revenue divisions on cross-over traffic as a device to obtain a rate reduction that was even larger than the rate reduction ordered by the Board in 1996. But the Board adopted ATC expressly to eliminate the bias created by the use of cross-over traffic. AEP Texas had no valid reason to expect that cross-over traffic could be used to improve the results of the 1996 SAC determination. Under these circumstances, it should not be given yet another chance to file SAC evidence.

Second, the Board erred by adopting a modified form of ATC that departs from the version of ATC adopted in Ex Parte No. 657.¹ ATC was adopted by the Board to allow complainants to use cross-over traffic in SAC analyses as a simplification mechanism that would approximate the results of a full SAC analysis. ATC avoids distorting the SAC results by maintaining the same relationship between revenue and average total cost on the on-SARR and off-SARR portions of a cross-over movement. Such a revenue allocation mechanism should make a complainant relatively indifferent as to SARR networks of different size.

The modified ATC methodology adopted by the Board in the September 10, 2007 decision in this proceeding abandons the premise of ATC and no longer allocates revenues in proportion to average total costs. Under the Board's modified ATC, revenues on many lower

¹ BNSF has raised an identical challenge to the use of modified ATC in *Western Fuels Association et al. v. BNSF Railway Company*, STB Docket No. 42088.

rated movements are allocated in direct proportion to variable on-SARR and off-SARR costs. For these movements, the SARR receives exactly the same pro-rata revenue allocation as the residual incumbent even though the SARR's costs per mile are undeniably lower by virtue of its economies of density. On higher rated traffic, the effect of density on total costs is diluted by double-counting variable costs in determining the allocation ratio. In both cases, the modified ATC approach reinstates the bias that ATC was designed to eliminate.

Moreover, the concern that led the Board to adopt modified ATC is misplaced. The Board was concerned that the application of ATC on certain low rated traffic could result in SARR revenues that were less than the incumbent's variable costs and thereby deprive the SARR of any contribution from that traffic. But the SARR's costs are lower than the incumbent's costs, therefore revenues that are less than the incumbent's URCS variable costs could still provide a considerable contribution to SARR costs. In any event, if a complainant concluded that the available revenues were too low, it could exclude the traffic from the traffic group.

Finally, even if the Board's concern about the effect of ATC on low rated traffic justified suspension of the average total cost approach on that traffic, there is no conceivable justification for applying the modified ATC methodology to all cross-over traffic. The effect of modified ATC on the higher rated traffic is merely to dilute the impact of density on relative on-SARR and off-SARR costs. Application of modified ATC on high rated traffic reintroduces bias by favoring the SARR with an overly generous allocation of revenues that is not justified by the SARR's relative costs. Such a result is irrational and arbitrary.

ARGUMENT

I. AEP Texas Should Not Get Another Opportunity to Submit SAC Evidence

In its September 10, 2007 decision, the Board stated that it would provide AEP Texas with an opportunity to submit supplemental SAC evidence in this proceeding. According to the Board, “fairness dictates that AEP Texas have an opportunity to modify its SAC presentation in light of the new revenue allocation methodology.” Decision at 23. To the contrary, under the circumstances of this case, fairness dictates that AEP Texas’ complaint be dismissed with no further opportunity to present SAC evidence.

In 1996, the Board carried out a SAC analysis that identified the maximum reasonable rates on movements of PRB coal to AEP Texas’ Oklahoma Station for a 20-year period from 1995 to 2014. The rate prescription resulting from this SAC analysis applied only to movements originating at a single mine – the Rawhide mine – but the SAC analysis included coal traffic originating at other PRB mines, including the same mine origins involved in the rate challenges at issue in this case. BNSF has never charged AEP Texas a rate for movements from any PRB mine that exceeds the maximum reasonable rates determined in the 1996 SAC analysis. All of the challenged rates in this proceeding have been at or below the level of rates deemed in the 1996 SAC analysis to be reasonable rates.

There has been no substantial change in the market for coal transportation that would suggest that rates deemed to be reasonable in the 1996 SAC analysis have become unreasonable. As BNSF demonstrated in reply evidence in this proceeding, revenues available to the SARR posited in the 1996 SAC analysis have actually turned out to be far lower than forecast in the SAC analysis. BNSF Reply Narrative at III.A-16 to 24 (May 24, 2004). Other changes in economic factors also suggest that there is no reason to believe that rates that were deemed to be reasonable in the 1996 SAC analysis have become unreasonable. *Id.* The Board’s September

10, 2007 Decision merely confirmed that the rates deemed to be reasonable in the 1996 SAC analysis have in fact remained reasonable over time

That finding, which should not come as a surprise, should end these protracted proceedings. BNSF should not have to undertake any further effort and expense in defending the reasonableness of rates that the Board has now found on two separate occasions to be reasonable.

The Board is mistaken in its view that adoption of ATC justifies giving AEP Texas another opportunity to present SAC evidence. The adoption of ATC merely neutralized the bias that AEP Texas sought to create by using large volumes of cross-over traffic in its SAC analysis in this case. As BNSF explained in its Reply SAC evidence, the primary difference between AEP Texas' SAC evidence in the present case and the SAC analysis done in 1996 was its heavy reliance on cross-over traffic in the present case. BNSF showed that the addition of cross-over traffic to the 1996 SAC analysis increased capital costs by about 117% but increased revenues, under the Modified Straight Mileage Prorate ("MSP") revenue allocation methodology, by 159%. BNSF Reply Narrative at III A-22 to 24. It was clear that AEP Texas sought to take advantage of the overly generous allocation of revenue to a SARR under MSP to distort the results of the 1996 SAC analysis which had not included cross-over traffic.

AEP Texas had no legitimate reason to believe that the Board would accept this use of cross-over traffic to change the 1996 SAC results. At the time that AEP Texas filed its SAC evidence, the Board had never suggested that a complainant is entitled to use cross-over traffic to change the results of a SAC analysis done without cross-over traffic. To the extent AEP Texas believed that it was appropriate to use cross-over traffic to change the SAC results, it was testing the limits of SAC theory. The Board rejected AEP Texas' theory and adopted ATC expressly to

eliminate the bias created by the use of cross-over traffic and to approximate the results of a full SAC analysis done without cross-over traffic

The Board itself acknowledged that it does not generally allow complainants to “redesign their case in light of subsequent Board decisions.” Decision at 20. There is no reason to depart from this general rule here. The cases establish that the Board does not give complainants a second bite at the apple in SAC cases unless the complainant reasonably relied on an established rule or precedent that the Board later reversed. That exception to the general rule clearly does not apply here. Indeed, the 1996 SAC determination indicated that the challenged rates were reasonable. AEP Texas sought to produce different results by taking advantage of cross-over traffic and the generous allocation of revenue to cross-over traffic under MSP, but it had no reason to believe it would succeed in that effort.

It is instructive to contrast two recent SAC cases where this issue has been addressed, one where the Board gave the complainant a second chance and the other where the Board denied the complainant a second chance. These cases establish a rational approach from which the Board has departed here.

In *AEPCO*, the Board gave the complainant an opportunity to resubmit SAC evidence because the Board was concerned that the complainant might have been misled by a prior Board ruling in the case *Arizona Electric Power Cooperative, Inc. v. The Burlington Northern and Santa Fe Railway Company and Union Pacific Railroad Company*, STB Docket No. 42058 at 4-6 (served Nov. 18, 2003) (hereafter “*AEPCO*”). *AEPCO* presented a SAC analysis in its opening evidence that assumed the SARR did not have to build and maintain a line segment but rather could use the existing UP line segment and pay a trackage rights fee under an existing BNSF/UP trackage rights agreement. *Id.* at 5. The Board was concerned that *AEPCO*’s decision to use the

trackage rights fee rather than build the line segment was made in reliance on statements made by the Board in a decision that had been issued before AEPCO submitted its opening evidence. *Id.* Consequently, the Board gave AEPCO the opportunity to submit different evidence “in view of the Board’s statements in the *August 2002 Decision* and the expectations that may have been created.” *Id.* at 6

AEP Texas was not misled into believing that it could change the 1996 SAC results by positing a SARR with large volumes of cross-over traffic and using the MSP methodology to over-allocate revenue to that cross-over traffic. This was an aggressive strategy and AEP Texas should have known there was considerable uncertainty as to whether the Board would accept it. Before AEP Texas submitted its opening evidence, it was on notice that the Board had “not adopted a single preferred procedure for developing revenue divisions on cross-over traffic.” *PPL Montana, LLC v. The Burlington Northern and Santa Fe Railway Company*, Docket No. 42054 at 7, n. 14 (served August 20, 2002), *Duke Energy Corporation v. Norfolk Southern Railway Company*, Docket No. 42069 at 17, n. 27 (served Nov. 6, 2003)

Indeed, AEP Texas was on notice when it submitted opening SAC evidence that the Board not only had concerns about the MSP methodology but also would be receptive to adopting a cross-over traffic revenue allocation methodology that, like ATC, took density into account. In November 2003, when the Board initially used the MSP methodology to allocate revenues from cross-over traffic, the Board made it clear that it was doing so only “[i]n the absence of a better supported method.” *Duke Energy Corporation v. Norfolk Southern Railway Company*, Docket No. 42069 at 22 (served Nov. 6, 2003). In that case, the Board rejected a density-based methodology for allocating revenue from cross-over traffic proposed by the railroad but explained “[t]here may be merit in allocating revenues based on the relative

variable cost and average fixed cost to haul the traffic over each segment of the move, if those costs can be fairly approximated.” *Id* In a SAC decision served a month before AEP Texas filed its SAC evidence, the Board reiterated that it “has not foreclosed an approach that would incorporate relative densities, as densities could affect the defendant carrier’s relative costs of providing service over the relative segments.” *Duke Energy Corporation v CSX Transportation, Inc* , Docket No. 42070 at 20 (served Feb 4, 2004)

When a complainant does not have a reasonable basis for assuming that its underlying SAC assumptions will be accepted, the Board does not give the complainant an opportunity to refile SAC evidence when those SAC assumptions are rejected Thus, in the *PPL* case, the Board determined that it would not be appropriate to provide the complainant with another opportunity to submit different SAC evidence In *PPL*, the Board applied a cross-subsidy test in the SAC analysis for the first time The complainant asked the Board to reopen the case so the complainant could modify its evidence, arguing that it would have submitted different evidence if it had known that the cross-subsidy test would be applied *PPL Montana, LLC v The Burlington Northern and Santa Fe Railway Company*, Docket No 42054 at 7 (served March 24, 2003) (“*PPL*”), *aff’d* 437 F 3d 1240 (D C Cir 2006) *PPL* argued that when it filed its opening evidence, it was not on notice from prior cases that the Board might apply a cross-subsidy test Nevertheless, the Board refused to allow *PPL* to submit different evidence, reasoning that “*PPL* cannot shift the responsibility for the choices that it made It is the shipper’s responsibility, and in the shipper’s interest, to design the least costly, most efficient SARR ” *Id* at 9. As the Board further explained, “[w]e reject the argument that *PPL* must be allowed to alter portions of its case-in-chief in light of our threshold cross-subsidy analysis, which merely applied well established principles to the particular facts and issues presented to us in this case Were we to

allow a disappointed party to revise its case in response to our rulings, there could be no end to an administrative proceeding ” *Id* at 11

The circumstances in this case provide even less justification for giving AEP Texas a second chance than in *PPL*. In this case, there was a prior SAC determination that the challenged rates were reasonable. AEP Texas sought to change that result through the use of cross-over traffic, but it had no reason to believe that the Board would find that what was reasonable under the prior SAC determination had become unreasonable principally through the use of cross-over traffic. AEP Texas sought to take maximum advantage of the distortions created by cross-over traffic and the MSP methodology and it should be held responsible for the litigation choices it made. Complainants have the burden of proof in SAC cases, and AEP Texas failed to carry that burden. Its complaint should be dismissed.

Congress emphasized in the governing statute the need to resolve regulatory proceedings expeditiously. Moreover, the statute reflects a policy to give railroads repose if cases are not determined within three years. *See* 49 U.S.C. §§10101(15), 11701(c). AEP Texas initiated this action on August 11, 2003 – over four years ago. The case has its origins in litigation begun thirteen years ago, in 1994, that resulted in a rate prescription in 1996. BNSF has never charged a rate that exceeds the maximum reasonable rate determined in that earlier round of litigation. It would be unfair to subject BNSF to further litigation. BNSF is entitled to have this litigation terminated now.

II. The Board Should Not Adopt Its Proposed Modified Version of ATC.

The Board erred by modifying the ATC methodology that it adopted in *Ex Parte No. 657*. The modified form of ATC is inconsistent with the fundamental principles underlying ATC and it reintroduces the bias in favor of SARRs that rely heavily on short-haul cross-over traffic that

the Board sought to eliminate when it adopted ATC. In addition to rejecting the modified version of ATC here, the Board should make clear that it will not apply the modified ATC in future SAC analyses.

The Board clearly explained the conceptual basis for its ATC approach to allocating revenue on cross-over traffic in *Major Issues in Rail Rate Cases*, STB Ex Parte No. 657 (served Oct. 30, 2006) (“*EP 657 Decision*”). According to the Board, use of cross-over traffic is a valid means of simplifying SAC presentations but it also has the potential for introducing bias into the SAC calculations, particularly in the allocation of revenue between the SARR and the residual incumbent. The Board concluded that the methodology used to allocate revenues on cross-over traffic should seek to preserve the simplifying benefits of cross-over traffic while eliminating to the extent possible any bias that would be introduced by the use of cross-over traffic. To eliminate bias, the methodology used to allocate revenue on cross-over traffic should produce SAC results that approximate the results of a SAC analysis done without cross-over traffic. As the Board explained:

In allowing the use of cross-over traffic, we seek to make the analysis more manageable without introducing bias. Thus, the goal in allocating revenue from cross-over traffic should be to ensure that a truncated SAC analysis using cross-over traffic will approximate the outcome of a full SAC analysis, which provides origin-to-destination service for the entire traffic group.

EP 657 Decision at 24 (note omitted)

The Board further concluded that the results of a full SAC analysis can best be approximated, thereby eliminating bias, by allocating revenue on cross-over traffic based on the relative costs of the on-SARR and off-SARR portions of the cross-over movement. Ideally, the cost relationship should be based on the SAC costs of the cross-over SARR and the SAC costs of a full SARR.

[T]he portion of the revenue allocated to those facilities replicated by the SARR should ideally equal the total revenue from that movement, multiplied by the share of total SAC costs represented by the cross-over segments of the movement (i.e., multiplied by the ratio of the SAC costs with cross-over traffic to the total SAC costs without cross-over traffic).

Id. But total SAC costs are not known, so it is not possible to develop a precise ratio of on-SARR SAC costs to off-SARR SAC costs. The Board nevertheless concluded that the ratio of the *incumbent's* costs over the portion of its system that would be replicated by the SARR and the residual portion of the movement was a valid proxy for the ideal SAC cost ratio. “By focusing on the ratio of actual costs incurred by the carrier, the revenue allocation method should maintain, to the extent possible, the relationship between revenues and costs that would exist in a full SAC analysis.” *Id.* at 25

The Board acknowledged that the relative density of the on-SARR and off-SARR portions of a through movement is a critical factor in determining the proper cost relationship between the two segments and therefore is a critical element in any cross-over revenue allocation methodology. The Board emphasized that it had been strongly encouraged by the U.S. Court of Appeals for the District of Columbia Circuit to adopt a revenue allocation methodology that “took account both of the economies of density and of the diminishing returns thereto.” *Id.* at 26 (internal quotation omitted)

Thus, the Board’s core justification for using ATC was that it allocates revenues based on the relative costs of providing service over different segments of a through movement and takes account of the impact of density on those costs. As the Board explained,

A successful allocation of cross-over revenues would produce the same revenue-to-cost relationship as would be produced if the complainant modeled the entire movement. Rather than arbitrarily allocating revenue to low-density lines, the ATC method more

accurately is keyed to the defendant carrier's relative costs of providing service over the two segments

Id at 35 The Board further explained that the ATC calculations must focus on average *total* costs rather than average *variable* costs to take proper account of economics of density

Economics of density reflect how average total costs for a network of a given size initially decrease with increases in output Accordingly, any approach that seeks to account for economics of density must examine the average total costs, rather than the average variable costs

Id at 34 The Board expected that ATC would "level the playing field by allocating costs according to a reasonable estimate of the relative costs to own and operate the various parts of the larger network " *Id* at 35.

The modified ATC methodology set out in the Decision repudiates the fundamental objective of ATC to provide a non-biased, cost-based allocation of through revenues between the SARR and the residual incumbent Modified ATC does not allocate revenues in proportion to average total costs and therefore does not produce the unbiased result that the Board said was required in Ex Parte 657.

The original ATC methodology allocates through revenues based directly on the relationship of on-SARR average total costs to off-SARR average total costs. To the extent the off-SARR portion of a movement has higher average total costs, the off-SARR portion of the movement therefore receives higher revenues in direct proportion to its higher average total costs Average total costs on both segments are determined by adding the variable costs on the segment to the average fixed costs on the segment The modified version of ATC adopted by the Board destroys the relationship between average total costs and revenues. Under modified ATC, the Board first allocates revenues to each segment of a through movement sufficient to cover the incumbent's URCS variable costs It then allocates the remaining through revenue to the on-

SARR and off-SARR portions of the through movement based on ATC as calculated under the original ATC formula

Two straightforward examples illustrate that modified ATC abandons the cost-based allocation approach that is at the heart of ATC. In the first example, the fixed costs on each segment of a through movement are ignored altogether under modified ATC and revenue is allocated entirely based on variable costs. In the second example, the effect of density on fixed costs is diluted by effectively double-counting variable costs in determining the revenue allocation. In all cases, modified ATC systematically disfavors the residual portion of a movement and reintroduces the bias in favor of a SARR using cross-over traffic that ATC was designed to eliminate.

In the first example, assume a 100-mile movement that generates through revenues of \$100. Assume that the incumbent's URCS variable costs for the movement are \$100 so the movement generates an R/VC ratio of 100%. Assume that the fixed costs are \$60 (system-average fixed costs of \$60 per mile times 100 miles). Assume also that the distance on and off SARR is the same (50 miles), but the traffic density on the on-SARR segment is twice that of the off-SARR segment. Table 1 below illustrates how revenue would be allocated under ATC as originally proposed and under the modified version applied by the Board in this case.

TABLE 1

	SARR	Residual Incumbent	Total
ATC			
Variable Costs	50	50	100
Fixed Costs	20	40	60
Total Costs	70	90	160
Segment Share of Total Costs (ATC)	$= 70 / (70 + 90)$ 43.8%	$= 90 / (70 + 90)$ 56.3%	100 0%
Modified ATC			
Variable Cost	50	50	100
Total Contribution (= 100 - 100)	---	---	0
Contribution	$0 * 43.8\% = 0$	$0 * 56.3\% = 0$	0
Modified ATC Revenue	$= 50 + 0$ 50	$= 50 + 0$ 50	100
Modified ATC Division	50.0%	50.0%	100 0%

It is beyond dispute that the average on-SARR costs are lower than the average off-SARR costs because density is higher on the SARR and therefore the fixed cost per ton on-SARR is lower than the fixed cost per ton off-SARR. The original ATC methodology recognizes this cost difference and allocates proportionally less revenue to the SARR to account for its lower costs. Under ATC, the SARR receives 43.8% of the through revenue to reflect the SARR's relatively lower average total costs. As the Board noted in Ex Parte No. 657, this is the desired result because it reflects the impact of density on cost. The SARR's average costs per unit of traffic are lower due to the higher density on SARR lines and the SARR should therefore receive proportionally less revenue.

Under the modified version of ATC used by the Board in this proceeding, however, the SARR and the incumbent would split the through revenue evenly. Even though the SARR's average total costs are clearly less than the residual incumbent's, the SARR gets exactly the same

amount of revenue as the residual incumbent. This result is inconsistent with the objective of ATC to allocate revenues based on relative costs.

The modified ATC methodology also violates the Board's explicit directive that the revenue allocation should be based on average *total* costs rather than average *variable* costs. In this example (and in the case of all traffic that moves at R/VC levels that are at or below the incumbent's URCS variable costs), fixed costs are ignored altogether. As a result, the modified ATC reintroduces bias into the SAC calculations. Table 2 summarizes the results for the hypothetical movement in Table 1 – where through revenues equal variable costs – and shows that the SARR does better under the modified ATC approach, thereby destroying the neutrality that the Board sought by adopting ATC.

TABLE 2

	SARR	Residual Incumbent	Total
Total Costs	70	90	160
ATC Revenue			
ATC Revenue	44	56	100
Revenue-to-Total Cost Ratio	63%	63%	63%
Modified ATC Revenue			
ATC Revenue	50	50	100
Revenue-to-Total Cost Ratio	71%	56%	63%

Under ATC, the revenue-to-total cost relationship is the same for the SARR and the residual incumbent – 63%. Thus, the allocation methodology eliminates any bias in the use of cross-over traffic. The results of the SAC analysis using cross-over traffic should approximate the results of a full SAC analysis because a more extensive SARR would receive additional revenues in direct proportion to its additional costs. But under modified ATC, the complainant is no longer neutral as to the size and scope of the SARR and instead has the incentive to build a

SARR that uses cross-over traffic to take advantage of the distorted revenue allocations. In the above example, there is a higher revenue-to-total-cost ratio for the SARR segment (71% for the SARR segment compared to 56% for the residual incumbent). Thus, a complainant would clearly be rewarded for building a short-haul SARR rather than the full SARR. Likewise, the complainant would be penalized for building a larger SARR since the additional revenue that would be available by building the extended lines would be proportionally lower than the total costs of constructing and operating over the larger network. Modified ATC reintroduces precisely the distortion that ATC was designed to eliminate.

The bias created under the Board's modified approach is not limited to traffic that covers only its variable cost and makes no contribution to the incumbent's fixed cost. Table 3 uses the same example in Table 1, but assumes a movement that generates \$200 of revenues and therefore has an R/VC of 200%.

TABLE 3

	SARR	Residual Incumbent	Total
ATC			
Variable Costs	50	50	100
Fixed Costs	20	40	60
Total Costs	70	90	160
Segment Share of Total Costs (ATC)	$= 70 / (70 + 90)$ 43.8%	$= 90 / (70 + 90)$ 56.3%	100.0%
Modified ATC			
Variable Costs	50	50	100
Total Contribution (= 200 - 100)	---	---	100
Contribution Allocated to Segments by ATC Share	$= 100 * 43.8\%$ 44	$= 100 * 56.3\%$ 56	100
Modified ATC Revenue	$= 50 + 44$ 94	$= 50 + 56$ 106	200
Modified ATC Division	46.9%	53.1%	100.0%

As Table 3 demonstrates, under the Board's modified approach, the SARR receives a revenue share in excess of its share of average total costs even when the traffic in question clearly covers more than its variable costs. In this example, the SARR's share of the average total cost of the through movement is 43.8% but it receives 46.9% of the through revenue. Once again, use of the modified ATC destroys the neutrality that the Board sought to achieve with ATC. Under modified ATC, the complainant is rewarded for building a short-haul SARR because it receives more revenue than is justified by the relative costs to provide service over the SARR lines. The results of the SAC analysis with cross-over traffic no longer approximate the results of the full SAC analysis.

In the example set out in Table 3, the reason that the SARR receives an excess share of revenue is that the Board's modified approach does not appropriately account for economies of density. As the Board correctly noted in Ex Parte No. 657, economies of density are reflected in average total costs, not average variable costs. The Board's modified approach impermissibly dilutes the impact of density by effectively double-counting variable costs in establishing the ratio used to allocate through revenues. The Board's modified approach first allocates to the SARR sufficient revenue to cover the incumbent's variable costs on the SARR segment. The Board then allocates any revenue in excess of variable costs based on the SARR's relative average *total* costs, which consist of the sum of variable and fixed costs. Application of the modified ATC ratio thus provides the SARR with an allocation of additional revenue reflecting variable costs that have already been covered. This approach dilutes the effect of relative density on average unit costs, overcompensates the SARR, and leaves the residual incumbent with an insufficient share of revenues to cover the proportionally higher costs of its low density lines.

The Board had no valid reason for abandoning its original ATC methodology in favor of a methodology that reintroduces the bias that ATC was designed to eliminate. The Board explains in the Decision that it decided not to apply the original ATC methodology out of a concern that the traffic group selected by AEP Texas “includes considerable traffic with total revenue either below or barely above” BNSF’s variable cost. Decision at 15. The Board was concerned that applying ATC to these low rated movements would drive the R/VC for the SARR portion of the move below 100% of the incumbent’s URCS costs. The Board deemed this to be an “illogical and unintended result,” and therefore decided first to allocate sufficient revenues to cover the incumbent’s variable costs and then to apply the ATC formula only to what it termed the “total revenue *contribution* (i.e., revenue in excess of variable cost as calculated by URCS).” *Id.* (emphasis in original)

But there is nothing “illogical” about an allocation methodology that would allocate revenues generated by low rated traffic to the SARR that are less than the incumbent’s URCS variable costs while allocating revenue to the residual incumbent that are somewhat higher than the incumbent’s variable costs. The Board concluded in Ex Parte No. 657 that “a successful allocation of cross-over revenues would produce the same revenue-to-cost relationship as would be produced if the complainant modeled the entire movement.” *EP 657 Decision* at 35. If the average total costs on the SARR are less than the average total costs off the SARR, which one would expect, the allocation mechanism should reflect that relationship. The SARR *should* receive proportionally less revenues to reflect its proportionally lower costs. Applying ATC under these circumstances accomplishes exactly the Board intended – it allows cross-over traffic to be used without introducing a distortion into the SAC calculations.

Logically, for two identical movements that have identical costs, a cost-based revenue allocation should result in the same percentage division of revenues regardless of the level of revenues on those movements. Tables 1 and 3 posit two movements that have the same costs — they are identical movements except for the amount of revenue that they generate. A cost-based revenue allocation methodology should allocate through revenues in the two examples in exactly the same proportion, as ATC does. There is nothing illogical about the results produced by ATC.

The Board's real concern appears to be that it would somehow be unfair to the SARR to allocate revenues to it that are less than the incumbent's URCS variable costs because it would deprive the SARR of a contribution to its fixed costs. But this concern is also misplaced. First, SARRs are supposed to be configured to operate as efficient, least-cost railroads, so it would be reasonable to expect that a SARR's variable costs would be lower than those of the incumbent, and perhaps substantially lower. Indeed, if a complainant includes traffic in the SARR traffic group that generates revenues that are close to (or below) the incumbent's URCS variable costs, it is appropriate to assume that the complainant expects that the variable costs of the SARR would be sufficiently lower than the incumbent's to allow the traffic to provide a contribution to the SARR's fixed costs.

Second, the *Guidelines* permit the complainant to select the SARR's traffic group so that the complainant has the opportunity to maximize revenue contribution to the SARR. If a complainant believes that a particular low rated movement may not contribute to the SARR's costs, it can exclude that traffic from the SARR traffic group. There is no valid reason for the Board to manipulate its revenue-allocation methodology to enable a complainant to include even the lowest rated traffic on the incumbent's network in the SARR traffic group. The Board's

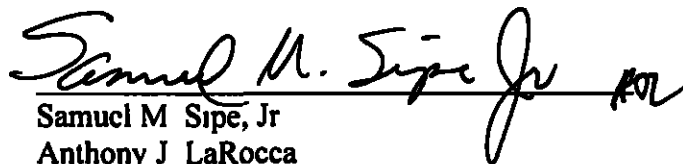
modification of the ATC approach does nothing other than tip the scales in favor of complainants

Finally, even if there were a valid reason to ensure that the SARR receives sufficient revenue to cover the incumbent's URCS variable costs, which there is not, there is no reason to apply the modified ATC methodology to all cross-over traffic, including high-rated traffic. As is evidenced in the second example described above, for movements that generate R/VC ratios well in excess of variable costs, there is no risk that ATC will allocate to the SARR less than the incumbent's URCS variable costs. Applying the modified ATC to high-rated traffic therefore unnecessarily distorts the cost relationship between the on-SARR and off-SARR segments by diluting the impact of density on total costs.

III. Conclusion

For the reasons set out above, the Board should grant BNSF's Petition for Reconsideration and rule that (1) AEP Texas is not entitled to present new SAC evidence in this proceeding, and (2) the Board will apply its original ATC methodology to allocate revenues on cross-over traffic rather than modified ATC in all future SAC analyses

Respectfully submitted,

A handwritten signature in black ink, reading "Samuel M. Sipe, Jr." followed by a stylized monogram.

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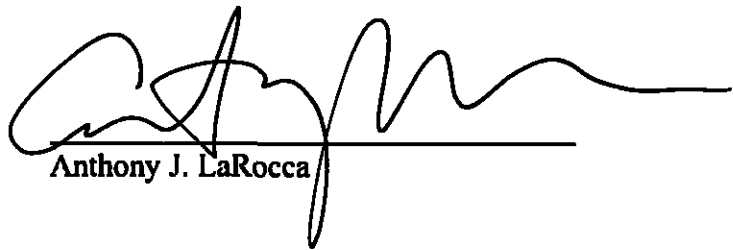
Attorneys for BNSF Railway Company

October 22, 2007

CERTIFICATE OF SERVICE

I hereby certify that this 22 day of October, 2007, I served a copy of BNSF's Petition For
Reconsideration to the following by hand delivery.

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