

BEFORE THE
SURFACE TRANSPORTATION BOARD

Canexus Chemicals Canada, L.P.)	
)	
Complainant)	
)	
v.)	Docket No. NOR 42132
)	
The BNSF Railway Company)	
)	
Defendant)	

REBUTTAL
Verified Statement
Of

Thomas D. Crowley
President
And
Charles A. Stedman
Vice President
L. E. Peabody & Associates, Inc.

On Behalf of
Canexus Chemicals Canada, L.P.

Due Date: April 12, 2012

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I. INTRODUCTION

We are Thomas D. Crowley and Charles A. Stedman. We are the same Thomas D. Crowley and Charles A. Stedman who filed verified statements in this proceeding on February 13, 2012 (“Opening VS”) and March 13, 2012 (“Reply VS”) on behalf of Canexus Chemicals Canada, L. P. (“Canexus”). Our qualifications and experience are attached to our Opening VS as Exhibit No. 1 and Exhibit No. 2, respectively.

Canexus is requesting that the Surface Transportation Board (“STB” or “Board”) prescribe reasonable rates, service terms and reparations associated with the transportation of chlorine via The BNSF Railway Company (“BNSF”) for the following two (2) movements:

1. North Vancouver, British Columbia, Canada to Glendale, AZ (“Glendale Movement”); and
2. North Vancouver, British Columbia, Canada to Albuquerque, NM (“Albuquerque Movement”).

In our Opening VS, we applied the STB’s procedures for the Three-Benchmark Methodology specified in the STB’s September 5, 2007 decision in Ex Parte No. 646 (Sub-No. 1) *Simplified Standards for Rail Rate Cases* (“*Simplified Standards*”). In support of Canexus’ request, we provided the following information:

1. The revenue / variable cost (“R/VC”) ratio for each of the issue movements;
2. The selection of comparable BNSF movements from the STB’s Unmasked Confidential Waybill Sample (“Waybill Sample”) for BNSF for each year 2006 through 2009; and
3. The upper boundary of the R/VC ratio for the comparison group (referred to as the “Maximum R/VC Ratio”) for each of the issue movements following the STB’s procedures specified in *Simplified Standards*.

Simultaneous with the filing of Canexus’ opening evidence on February 13, 2012, BNSF filed its opening evidence in this proceeding. In our Reply VS, we critiqued and responded to

BNSF's opening evidence and incorporated revisions to the analyses included in our Opening VS. Our Reply VS included the "Final Offer" comparable groups for each issue movement¹.

Simultaneous with the filing of Canexus' reply evidence on March 13, 2012, BNSF filed its reply evidence in this proceeding including its "Final Offer" comparable group for the issue movements.

In our Rebuttal verified statement ("Rebuttal VS"), we respond to the criticisms included in BNSF's reply evidence related to our Opening VS, and provide a critique of BNSF's reply evidence, analyses and results. Our Rebuttal VS is summarized under the following headings:

- II. Final Offer Comparison Groups
- III. Other Relevant Factors

¹ See Reply VS, Exhibit No. 10 (Glendale) and Exhibit No. 11 (Albuquerque).

II. FINAL OFFER COMPARISON GROUPS

Simplified Standards specified the procedures to develop the Maximum Revenue to Variable Cost (“R/VC”) ratio for the issue movements using the Three-Benchmark Methodology. The centerpiece of this methodology is each party’s development of its comparison group(s) for the issue move(s). In our Opening VS, we presented the results of our initial analyses following the STB procedures including our two initial comparison groups, *i.e.*, one for each issue move.² In our Reply VS, we presented the results of our analyses using our two “final offer” comparison groups and critiqued BNSF’s initial alternative case single comparison group.³ In this Rebuttal VS, we will critique BNSF’s “final offer” alternative case single comparison group and respond to BNSF’s reply criticisms of Canexus’ two comparison groups under the following topical headings:

- A. BNSF’s Final Offer Comparison Group; and
- B. Canexus’ Final Offer Comparison Groups.

A. BNSF’S FINAL OFFER COMPARISON GROUP

In BNSF’s Reply, BNSF continued to present two comparison groups, *i.e.*, a “preferred” comparison group and an “alternative” comparison group.⁴ In our Reply VS, we explained why BNSF’s “preferred” comparison group is not a valid comparison group because it is based on data which the STB ruled cannot be used in this proceeding.⁵ We also explained why BNSF’s initial alternative single comparison group was not appropriate for the two issue moves.⁶ As BNSF has made no modifications to its initial alternative single comparison group, all of the criticisms contained in our Reply VS remain applicable and need not be expanded on Rebuttal.

² See our Opening VS at pages 8 through 10.

³ See our Reply VS at pages 7 through 19.

⁴ See BNSF Reply at pages 5 through 7.

⁵ See our Reply VS at pages 7 and 8.

⁶ *Id* at pages 9 through 16.

**B. CANEXUS' FINAL OFFER
COMPARISON GROUPS**

In this section of our Rebuttal VS, we respond to BNSF's reply criticisms of Canexus' initial comparison groups and how these criticisms relate to Canexus' final offer comparison groups, if at all. Our discussion is contained under the following headings:

1. Primary Differences; and
2. BNSF's Alleged Principal Defects in Canexus' Comparison Groups.

1. Primary Differences

In its Reply, BNSF describes five primary differences between BNSF's and Canexus' initial comparison groups.⁷ A brief summary of BNSF's criticisms plus a brief summary of our response explaining why each criticism has no merit follows:

1. BNSF criticizes Canexus for including movements other than chlorine in its comparison groups while BNSF included only chlorine movements. In our Reply VS, we explained why TIH movements other than chlorine were valid for inclusion in the comparison groups.⁸ BNSF goes on to state that Canexus' comparison groups contain too few chlorine movements. While Canexus' disagrees that its initial comparison groups contained too few chlorine movements, this criticism is moot because Canexus increased the number of chlorine movements in its final offer comparison groups by adding nine local chlorine movements from BNSF's alternative case single comparison group to each of Canexus' comparison groups.⁹
2. BNSF criticizes Canexus for the way it handled the issue movements in its comparison groups. As explained in our Reply VS, Canexus handled the issue movements consistent with *Simplified Standards*.¹⁰ This issue is discussed further in the next section of our Rebuttal VS.
3. BNSF criticizes Canexus for including Waybill Sample movements from 2006 through 2008 in its comparison groups rather than limiting them to only 2009 movements as BNSF did. This is not a valid criticism for the simple reason that Canexus followed STB precedent and used four years of Waybill Sample data. Four years of Waybill Sample

⁷ See BNSF Reply at pages 8 through 10.

⁸ See our Reply VS at pages 11 through 13.

⁹ *Id* at pages 16 and 17.

¹⁰ *Id* at pages 10 and 11.

data were used by *all parties* in the four previous Three-Benchmark proceedings.¹¹ Canexus' use of four years of Waybill Sample data also conforms to the four years of data used by the STB to generate the RSAM and RVS_{>180} ratios required to develop the Maximum R/VC Ratio. Finally, the Board affirmed that four years of data would be supplied to the parties, and each could use all four years of the data if they wished to do so, in its *March 12, 2012 Decision*¹².

4. BNSF claims that its use of rebill (interline) movements in its alternative case comparison group is more appropriate than Canexus' use of only local movements. As discussed in our Reply VS, BNSF's inclusion of rebill movements is inappropriate and contrary to explicit STB precedent.¹³
5. BNSF claims that its "alternative comparison group has a more expansive mileage-band than does Canexus's group."¹⁴ Regardless of the merits of this criticism, it is moot as Canexus accepted BNSF's expanded mileage band for the local movements included in BNSF's alternative case comparison group¹⁵ when developing Canexus' final offer comparison groups.

2. BNSF's Alleged Principal Defects In Canexus' Comparison Groups

Of the five foregoing "primary differences", BNSF claims three of the "principal differences are defects"¹⁶. Each of BNSF's claimed problems is discussed below under the following topics:

- a. Anhydrous Ammonia Shipments;
- b. Glendale Issue Traffic; and
- c. 2006 Through 2008 Movements.

a. Anhydrous Ammonia Shipments

BNSF continues to claim that Canexus' inclusion of anhydrous ammonia movements in its

¹¹ See STB Docket No. 42099 *E.I. DuPont de Nemours and Company v. CSX Transportation, Inc.* ("DuPont Non-Haz"), decision served June 30, 2008; STB Docket No. 42100 *E.I. DuPont de Nemours and Company v. CSX Transportation, Inc.* ("DuPont TIH"), decision served June 30, 2008; STB Docket No. 42101 *E.I. DuPont de Nemours and Company v. CSX Transportation, Inc.* ("DuPont Haz"), decision served June 30, 2008; and STB Docket No. 42114 *US Magnesium, L.L.C. v. Union Pacific Railroad Company* ("USM"), decision served January 28, 2010.

¹² See STB March 12, 2012 decision in Ex Parte 646 (Sub-No. 3), *Waybill Data Released in Three-Benchmark Rail Rate Proceeding* ("March 12, 2012 Decision").

¹³ See our Reply VS at pages 15 and 16.

¹⁴ See BNSF Reply at page 10.

¹⁵ See our Reply VS at pages 16 and 17.

¹⁶ See BNSF Reply at 10

two comparison groups is a “serious deficiency.”¹⁷ BNSF lists all the reasons it offered in opening that the transportation of chlorine and anhydrous ammonia is not comparable. We refuted all of those reasons in our Reply VS.¹⁸ In its Reply, BNSF provides two additional reasons why chlorine and anhydrous ammonia should not be considered comparable. As shown below, neither of BNSF’s new claims is valid.

First, BNSF included a table showing a comparison of “average” R/VC ratios for chlorine and anhydrous ammonia movements as of March 16, 2011 based on an analysis of BNSF publicly-available rates and BNSF-developed variable costs. This table is based on BNSF’s “Public Current Rate Adjustment” other relevant factor rate adjustment that BNSF presents for the first time in its Reply.¹⁹ As discussed in Section III of this Rebuttal VS, BNSF’s analysis of “common carrier price authorities” is not an analysis of actual rail movements, but rather is an analysis of “origin-destination lanes.”²⁰ BNSF’s hypothetical analysis does not demonstrate that any traffic actually moved under these common carrier rates or tariffs.

At page 12 of its Reply Evidence, BNSF included a table (Table 1) that compares the average R/VC ratio BNSF calculated for 27 chlorine lanes to the average R/VC ratio BNSF calculated for 12 anhydrous ammonia lanes. BNSF had published public tariff rates as of March 16, 2011 for all of these lanes and each was within 700 miles of either of the two issue movement distances. BNSF calculated the revenues for these lanes based on the published tariff rate and the applicable March 2011 fuel surcharge tariff. BNSF calculated the variable costs for these lanes based on the 2010 STB URCS unit costs indexed to 1Q11. BNSF’s table shows that the average R/VC ratio for the selected chlorine lanes as of March 16, 2011 was { } while the average R/VC ratio for the selected anhydrous ammonia lanes as of March 16, 2011 was { }. BNSF points to

¹⁷ See BNSF Reply at page 10.

¹⁸ See our Reply VS at pages 11 through 13.

¹⁹ See BNSF Reply at pages 11 and 12.

²⁰ *Id* at page 12.

this difference in R/VC ratios as proof that actual movements of anhydrous ammonia are not comparable to actual movements of chlorine.

There are several problems with BNSF's argument. First, using established tariff rates instead of the revenues and URCS variable costs of actual rail movements to establish R/VC ratios opens the door to a process of systematic gaming for the railroads. If this methodology was accepted by the Board, the railroads could simply publish tariff rates for lanes over which they know no movements will occur and then, when a shipper challenged rates that it actually used for transportation, point to those never-to-be-used rates as justification for the challenged rates where traffic does move.

Second, under the Three-Benchmark methodology, use of the comparable moves contained in the unmasked Waybill file must be balanced through use of the corresponding expansion factors associated with each comparable movement. If the sampled movements are evaluated without regard for the corresponding expansion factors, the comparable movement group is not truly representative of the universe of comparable shipments. Because the Waybill sample is random and unbiased, there is a greater chance of the inclusion of shipments over high-volume lanes in the sample. The expansion factors account for this and ensure that the sampled movements, when expanded, are given the proper weighting. Under BNSF's model, every published tariff rate is given precisely the same weight, regardless of the volume of traffic (if any) that moved under each included rate on March 16, 2011 or at any other time since then. Therefore, BNSF's model cannot be assumed to be representative of the actual market for transportation of either commodity.

Third, BNSF's model only includes rates for movements governed by public pricing authorities. Because it ignores all movements governed by privately negotiated contracts, BNSF's model is critically flawed and cannot be assumed to be representative of the overall market for the transportation of either chlorine or anhydrous ammonia.

Fourth, it is important to remember that the main premise behind BNSF's attempt to create a distinction between chlorine and anhydrous ammonia rates is BNSF's claims that it imposed unilateral rate increases on chlorine movements around the time when BNSF issued the challenged rates. BNSF defends its rate increases as necessary and reflective of the costs it must incur to implement PTC systems and carry high liability risk premiums due to its common carrier obligation to carry TIH generally and chlorine specifically. At the time of BNSF's chosen data for this particular analysis, March 16, 2011, BNSF had completed the implementation of its unilateral rate increase on chlorine movements. The corollary to BNSF's point is that the rates for anhydrous ammonia were no longer comparable to the rates for chlorine as of that date because anhydrous ammonia did not receive a similar across-the-board rate increase.

However, based on BNSF's more recent tariffs governing the movement of chlorine and anhydrous ammonia (published as of March 31, 2012),²¹ it is evident that BNSF has just implemented a similar unilateral rate increase on anhydrous ammonia movements this year. We evaluated all of the { } anhydrous ammonia lanes and { } chlorine lanes BNSF included in its "Public Current Rate" analysis supporting its Table 1. We found that the rates for { } anhydrous ammonia movements and { } chlorine movements BNSF included in its analysis had expired as of March 29, 2012. For the remaining { } anhydrous ammonia lanes, the current rates increased by { } percent on average since March 16, 2012. For the remaining { } chlorine lanes, the current rates increased by only { } percent on average since March 16, 2012. Table 1 below contains a summary of the changes in chlorine and anhydrous ammonia rates for lanes BNSF included in its analysis since March 16, 2011.

²¹ BNSF 90096-5000 Rev 70 and BNSF 90084-3000-A Rev 95.

Table 1
**Summary of the Change in Rates for Lanes BNSF
Included in its Public Current Rate Analysis Since March 16, 2011**

<u>Commodity</u>	<u>Lanes Included in BNSF Analysis as of 3/16/2011</u>	<u>Lanes That Have Expired as of 3/29/2012</u>	<u>Remaining Lanes with Active Rates Published as of 3/31/2012</u>	<u>Average Rate Increase Since 3/16/2011 for Remaining Active Lanes</u>
(1)	(2)	(3)	(4)	(5)
1. Chlorine	{ }	{ }	{ }	{ }
2. Anhydrous Ammonia	{ }	{ }	{ }	{ }

Source: Work Paper "Public Current Rate Adjustment Canexus Reb v3.xlsx" level "rate comp summary"

Therefore, the R/VC ratio discrepancy BNSF notes in its Table 1 was only present for a brief moment in time (a calendar year) because BNSF happened to implement its price hike for chlorine a year before it implemented a similar price hike for anhydrous ammonia. This is precisely why the Board was correct to endorse the use of four years of waybill sample data in Three-Benchmark rate cases in its March 12, 2012 Decision, and it underscores why the universe of historical movement data is a superior source of comparable rates than the published tariff rates on any one particular day.

Next, BNSF includes a chart comparing the Producer Price Indexes ("PPI") for chlorine and anhydrous ammonia from 2006 to the present.²² BNSF's chart is irrelevant for the following reasons. The issue that is being evaluated under the Three Benchmark methodology is the transportation rates and the variable costs of transporting the two commodities, not the entirely separate issue of the price of the commodities. In our Reply VS,²³ we discussed in detail BNSF's claims concerning the comparability of chlorine and anhydrous ammonia from a transportation perspective. BNSF provided no evidence that its rail rates for chlorine and anhydrous ammonia are related in any way to the prices of the commodities or that the fluctuation of commodity prices, such as that shown in BNSF's Chart 1, has any impact on the transportation rates being charged to

²² *Id* at pages 13 and 14.

²³ See our Reply VS at pages 11 through 13.

move these two, or any other, commodities. For example, BNSF ships a large volume of coal from the Powder River Basin (“PRB”) in Wyoming. The prices for the coal produced in the PRB can vary significantly based on the various characteristics of the coal available at each of the mines, the time of year, the weather and the availability of alternate fuels. BNSF publishes many common carrier price authorities for the transportation of coal from the PRB to locations all over the U. S. We do not know of any common carrier price authorities that change with the price of the coal being transported.

**b. Glendale
Issue Traffic**

BNSF objects to Canexus’ comparison group for the Albuquerque movement because it includes Glendale movements that are contained in the Waybill Sample and met our selection criteria. BNSF claims that this inclusion is only to “exploit the regulatory lag problem.”²⁴ BNSF is incorrect.

As discussed in our Reply VS, we excluded the issue movements from the comparison group for the particular movement being evaluated according to the requirements of *Simplified Standards*. In other words, Glendale movements were excluded from the Glendale comparison group and Albuquerque movements were excluded from the Albuquerque comparison group.²⁵ The two issue movements must be treated separately with specific comparison groups tailored to each movement. If each issue movement was filed under a separate complaint, there would be no discussion about including Glendale movements in a comparable group for the Albuquerque movement. As a result, Glendale movements, as well as any other movement other than the Albuquerque movement, are includable in the comparison group for the Albuquerque movement as long as they meet the specified selection criteria.

²⁴ See BNSF Reply at page 15.

²⁵ See our Reply VS at pages 10 and 11.

c. 2006 Through 2008 Movements

BNSF complains that Canexus relied too heavily on 2006 through 2008 Waybill Sample movements in the composition of its two comparison groups.²⁶ BNSF's complaint has no substance, especially when Canexus' final offer comparison groups are examined. For the Glendale final offer comparison group, fully half (25 out of 50) of the comparable movements are from 2009, including nine chlorine movements. For the Albuquerque final offer comparison group, two-thirds (22 out of 32) of the comparable movements are from 2009, including thirteen chlorine movements. More importantly, the STB's Three Benchmark Methodology relies on the relationship of revenues to variable cost, not absolute values. These relationships are consistent over all four years of the Waybill Sample data provided to the parties and used to develop the three factors that make up the Three Benchmark maximum rate methodology, i.e., the development of the RSAM, R/VC₁₈₀ and Comparison Group ratios.

²⁶ See BNSF Reply at pages 16 and 17.

III. OTHER RELEVANT FACTORS

In its Opening evidence, BNSF proposed four separate (upward) adjustments to the R/VC ratio calculated under the STB's Three Benchmark Methodology to account for "other relevant factors". BNSF's four separate, upward adjustments included:

1. Current Rate Adjustment
2. Historical PTC Adjustment
3. Liability Risk Adjustment
4. Future PTC Adjustment

In our Reply VS, we explained why each of BNSF's four "other relevant factors" adjustments was in violation of the Board's rulings and precedent and/or otherwise without merit. BNSF has not modified any of these proposed adjustments on Reply. All of our analyses and conclusions presented in our Reply VS are still valid.

In BNSF's Reply, BNSF introduced a brand new fifth "other relevant factor" upward adjustment, the "Public Current Rate Adjustment," which it presented as an alternative to BNSF's original "Current Rate Adjustment". This new adjustment suffers from the same critical flaws as BNSF's original "Current Rate Adjustment" proposal and should be rejected for the reasons we set out in our Reply VS, as supplemented below.

Also in BNSF's Reply, BNSF applied its four original and one new "other relevant factor" adjustments to a subset of the comparison traffic groups proposed by Canexus in its Opening. We address the application of BNSF's "other relevant factor" adjustments below.

A. PUBLIC CURRENT RATE ADJUSTMENT

As we discussed in our Reply VS, BNSF's "Current Rate Adjustment" is based on selected BNSF 2011 data from its internal files. The STB has ruled repeatedly that the use of selected waybills from railroads' internal files cannot be used in this or any Three Benchmark Methodology

proceeding. Additionally, the STB specifically prohibited the use of selected 2011 waybills from BNSF's internal files in this case. Therefore, we did not critique the mechanics of BNSF's Current Rate Adjustment.

On March 12, 2012, the day before the parties filed their reply evidence in this case, the STB released its *March 12, 2012 Decision* which affirmed prior STB declarations which clearly articulated that any comparison group based on traffic data other than the four-year Waybill Sample provided by the STB is impermissible. Specifically, the STB ruled that:

The rail carriers argue that, instead of permitting the use of four years of Waybill Sample data, we should instead require the carrier to make available its most recent traffic data... We disagree. Based on our experience in Stand-Alone Cost (SAC) cases and in processing the annual Waybill Sample data, we have already concluded that using the prepared Waybill Sample data is one of the linchpins to the simplified rate review process. The release of four years of Waybill Sample data to the parties minimizes the possibility that additional traffic data will be needed for the parties to develop their comparison groups.²⁷

BNSF's original "Current Rate Adjustment" explicitly violated the Board's policy because it relied on "its most recent traffic data." BNSF's new "Public Current Rate Adjustment" does the same thing. Specifically, BNSF's "Public Current Rate Adjustment" relies on a subset of "its most recent traffic data" common carrier tariff rates.

BNSF's justification for its "Public Current Rate Adjustment" is that it "address[es] the fundamental regulatory lag problem that is presented in this case."²⁸ BNSF claims that its "Public Current Rate Adjustment" is needed to account for BNSF's belief that, "chlorine R/VC levels in 2009, not just chlorine rate levels, differed from (and were not comparable to) current chlorine R/VC levels."²⁹ More specifically, BNSF asserts that it implemented an across-the-board rate increase on chlorine shipments in 2011 that "resulted in rate increases for transporting chlorine and other TIH products that are significantly greater than would have been necessary to simply cover

²⁷ *March 12, 2012 Decision*, p 5.

²⁸ BNSF Reply, p. 18.

²⁹ *Id.*, p. 19, fn 43.

inflationary increases in variable costs.”³⁰ Interestingly, BNSF’s rate increase was applied in the same manner to “chlorine and other TIH” shipments, despite BNSF’s claims that an appropriate comparison group for determining the maximum reasonable R/VC should include only chlorine shipments.

As a threshold matter, BNSF’s “Public Current Rate Adjustment” is impermissible because it is actually a thinly veiled attempt to replace the comparison group. This BNSF adjustment replaced shipments selected from the historical Waybill data, with a substitute comparison group comprised of shipments using current data. In BNSF’s model, BNSF first calculates an R/VC ratio for the chlorine movements for which it had issued public tariff rates as of March 16, 2011 (“2011 R/VC ratio”). BNSF then compares its 2011 R/VC ratio to the R/VC ratio it had calculated for the movements BNSF selected from historical waybill data in its “alternative” comparison group (“2009 R/VC ratio”) and, based on the differential between the two R/VC ratios, makes an upward adjustment to the Three-Benchmark R/VC ratio. Therefore, like the “Current Rate Adjustment”, the “Public Current Rate Adjustment” simply replaces the historical comparable moves BNSF selected with an altered set reflecting the R/VC ratio of its preferred (and prohibited) comparable movement group. BNSF is simply attempting to use the “Other Relevant Factors” portion of the Three-Benchmark process to try and introduce current traffic data that is expressly prohibited in the “Comparison Group” portion.

The Board considered and rejected this very sort of adjustment in its June 30, 2008 Decision in STB Docket No. 42099.³¹ In that case, CSXT attempted to adjust the comparison group R/VC to account for “Regulatory Lag” by “adjust[ing] revenues by publicly available data... adjust[ing] costs by using publicly available data and the indexing methods used in stand-alone cost cases...

³⁰ Id.

³¹ *E.I. Du Pont De Nemours & Co. v. CSXT Transp. Inc.* NOR 42099 (“DuPont”), served June 30, 2008.

[and] raising the R/VC ratios in the comparison groups.”³² In explaining its rejection of CSXT’s proposed adjustment, the Board noted several problems with the theory behind the adjustment, including the fact that such an adjustment would create a disconnect between the applicable expansion ratio ($RSAM \div R/VC_{>180}$) and the corresponding traffic group from which comparable movements had been selected. Specifically, the Board pointed out that the expansion ratio will change as pricing changes, thus offsetting the impact of the rate increases in a Three-Benchmark case.³³ Put simply, if BNSF changes its pricing structure to significantly increase rates, then it will require less differential pricing of potentially captive traffic. As a result, the expansion ratio applicable to its comparison group R/VC in Three-Benchmark rate cases will necessarily decrease as the higher rates are implemented. However, in this case BNSF seeks to apply both the unadjusted expansion ratio that reflects 2009 rates and the adjusted R/VC ratio that reflects 2011 rates. BNSF’s proposed adjustment is therefore one-sided and a maximum rate level based on this adjustment would be unreliable (and in this case, too high).

In addition to being flatly contrary to the Board’s prohibition on using traffic data other than historical Waybill data in Three Benchmark cases, there are several other problems with BNSF’s approach. First, just because BNSF has issued tariff rates for chlorine shipments does not mean that the rates are reasonable or that any shipments have moved under them – or even, in today’s climate where the railroads publicly state they do not want to handle TIH commodities – whether there is any intention for the rates to be used. If this “Public Current Rate Adjustment” was legitimized in

³² *DuPont*, p. 18.

³³ *Id.* As the Board explained:

“We expressed concerns about an apple-to-oranges adjustment in Simplified Standards (at 84-85). Consider a hypothetical example where a carrier was revenue adequate in 2006, such that the $RSAM \div R/VC_{>180}$ ratio shows the carrier earning 5% more from its potentially captive traffic than would be needed to earn adequate revenues in that time period. In that situation, the expansion ratio would serve to reduce the R/VC ratios of the comparison group in 2006 by 5% to more accurately reflect reasonable rates. Assume further that the carrier had increased all revenues by 10% between 2006 and 2007. It does not follow that the comparison group R/VC ratios should be adjusted upward by 10%, as those R/VC ratios would already provide the carrier more than needed to achieve adequate revenues in 2006 and there is no evidence to suggest that higher rates would be proper. In fact, in this hypothetical, the evidence would suggest that an opposite adjustment should be made. That is, if a revenue adequate carrier had been raising rates, then it would need less (not more) differential pricing of potentially captive traffic. When the 2007 information becomes available, the $RSAM$ and $R/VC_{>180}$ benchmarks for 2007 would change accordingly and suggest that the comparison group R/VC levels should be adjusted downward, not upward as sought by the carrier.”

this proceeding, the railroads could easily game the Three Benchmark analysis by simply issuing tariff rates that would never be used by shippers, or that would be used to move only a handful of shipments. The railroads could then claim that the existence of published rates that were never (or little) used were legitimate justification for artificially high rates on higher-volume routes. The STB recognized this problem and seeks to determine a reasonable rate based on evaluation of sufficient historical data to provide a long-term understanding of the issue market.

[I]n a rate case, we are not asked to determine the maximum lawful rate on the day the tariff was issued, but for a multi-year prescriptive period.³⁴

Second, BNSF alleges that its new rate setting philosophy appears to be based on a belief that it should be able to allocate costs to TIH shipments in a manner that overrides the STB's long-standing use of the Uniform Railroad Costing System ("URCS") variable costs to determine reasonable rates. As noted in BNSF's opening evidence,³⁵ the reasons BNSF gives for instituting universal rate increases on TIH shipments is that BNSF believes TIH shipments are responsible for costs it incurs (1) to implement PTC equipment as required by Federal regulation; and (2) in premiums for high liability insurance coverage levels it claims it carries only because it transports TIH. Stated differently, BNSF justifies its higher rates based exclusively on a claim that these higher costs are incurred exclusively because of, and directly attributable to, TIH shipments. For reasons we discussed in detail in our Reply VS, neither the costs associated with PTC implementation nor the costs associated with high liability premiums are directly attributable to TIH traffic. However, even if they were (and if BNSF's rate increases were justified), then by definition BNSF's "Public Current Rate Adjustment" would be critically flawed.

Specifically, the alleged cost increases BNSF associates with TIH shipments and BNSF's inflated rates must either be considered together or not at all. Yet its Public Current Rate Adjustment would apply the rate increases independently to alter the R/VC ratios. This application

³⁴ *March 12, 2012 Decision*, p. 9.

³⁵ See BNSF opening at pages 17-18.

completely ignores the relationship between costs and rate setting that BNSF uses to justify its new rate structure.

Stated another way, BNSF claims the current rate adjustment is required to reflect BNSF's new philosophy on TIH rate setting (that TIH shippers should bear higher costs associated with PTC investment and insurance premiums). However, in its "Public Current Rate Adjustment," BNSF compares the new higher rates (purportedly established to defray higher costs associated with TIH traffic) to system average variable costs, so the "higher costs" are not reflected in the comparison.

In reality, if BNSF's rates were actually set to recover BNSF's estimated cost increases, the R/VC ratios would go down, assuming constant margins. The following Table 2 simple hypothetical example demonstrates the flaw inherent in BNSF's methodology.

Table 2 <u>Demonstration of Critical Flaw in BNSF's "Public Current Rate Adjustment"</u>		
<u>Item</u> (1)	<u>Source</u> (2)	<u>Amount</u> (3)
Hypothetical Movement Prior to <u>BNSF Cost Re-allocation and Rate Changes</u>		
1. Pre-Adjustment Rate	Assumed	\$2,800
2. System Average Variable Cost	Assumed	\$1,000
3. Calculated Margin	Line 1 minus Line 2	\$1,800
4. R/VC Ratio	Line 1 ÷ Line 2	2.80
Hypothetical Movement After <u>BNSF Cost Re-allocation and Rate Changes</u>		
5. TIH-Specific Variable Cost	Assumed	\$2,000
6. Constant Margin	Line 3 above	\$1,800
7. Rate Adjusted to Reflect Increased Costs	Line 5 plus Line 6	\$3,800
8. R/VC Ratio	Line 7 ÷ Line 5	1.90
BNSF Current Rate <u>Adjustment R/VC Overstatement</u>		
9. System Average Variable Cost	Line 2 above	\$1,000
10. Rate Adjusted to Reflect Increased Costs	Line 7 above	\$3,800
11. Calculated Margin	Line 10 minus Line 9	\$2,800
12. R/VC Ratio	Line 10 ÷ Line 9	3.80

As demonstrated above, if BNSF's new rate structure truly reflected cost increases then the R/VC ratio would logically go down, not up. By ignoring the alleged TIH-specific cost increases in developing its "Public Current Rate Adjustment," BNSF is artificially inflating the R/VC ratio associated with TIH shipments. In addition, BNSF's rate increases are only justifiable if the cost increases based on allocation of PTC and insurance costs to TIH shipments are valid, which we have demonstrated is not the case. However, even if the cost increases are valid, then they must be considered together with the increased rates and reflected in the R/VC ratio calculation. Otherwise, neither the alleged cost increases nor the unjust rate increases should be considered. The Board recognized this disconnect when it issued its decision in the *March 12, 2012 Decision*:

For example, relying only on data provided by the carrier presents the problem that, unlike the Waybill Sample data, the traffic data provided by the carriers would not include the variable cost data necessary to determine R/VC ratios.³⁶

B. APPLICATION OF BNSF ADJUSTMENTS TO CANEXUS' COMPARISON GROUPS

BNSF claims its "Historical PTC Adjustment" is needed "to reflect the impact of BNSF's historical PTC costs on the maximum reasonable rate for movements of TIH," and that its "Liability Risk Adjustment" is needed "to reflect the fact that a substantial portion of BNSF's insurance premiums are due solely to its transportation of TIH traffic."³⁷ BNSF attempts to justify its adjustments based on its unsubstantiated claim that the STB has acknowledged that "URCS does not adequately attribute the PTC [and insurance] costs incurred by BNSF to the TIH traffic responsible for those costs."³⁸ However, the STB's position is that:

It must be remembered that the Three-Benchmark model is designed to approximate the maximum reasonable rate that would be determined under the more rigorous SAC model. The fundamental purpose of the Three-Benchmark approach is not to reflect a snapshot of current market conditions; it is to use

³⁶ *March 12, 2012 Decision*, at 6.

³⁷ BNSF opening, pg. 58

³⁸ *Id.*

the three benchmarks to decide the reasonable maximum contribution to joint and common costs for the issue movement where no cost-based approach is feasible. The R/VC_{Comp} benchmark is used to approximate the maximum reasonable rate that a rail carrier could charge under the SAC constraint.³⁹

Under the stand-alone cost model, a complaining shipper is free to select a traffic group consisting of the issue traffic and other traffic that would use the constructed facilities. One of the fundamental purposes for selecting other traffic is to defray the joint and common costs associated with the construction and operation of the hypothetical stand-alone railroad. Two components of those joint and common costs are PTC installation and operating costs, including insurance premiums. Under the full SAC methodology, those costs are allocated to all traffic that moves on the constructed system.

However, BNSF seeks to allocate all of those costs to the issue traffic (and other TIH traffic) in its Three-Benchmark model. This is a significant and substantial departure from stand-alone cost theory. Rather than using the Three-Benchmark model to “approximate the maximum reasonable rate that a rail carrier could charge under the SAC constraint,” BNSF’s proposed “other relevant factor adjustments” contradict the treatment of joint and common costs under the stand-alone cost constraint.

In its Reply, BNSF applies its four original and the fifth new “other relevant factor” adjustments to only the chlorine movements in the comparison traffic groups selected by Canexus in Opening. BNSF’s development and application of its four original “other relevant factor” adjustments in Reply is mechanically identical to its development and application of its four original “other relevant factor” adjustments in Opening. The only difference is that BNSF applied the adjustments to the maximum R/VC ratio calculated based on application of the Board’s Three-Benchmark methodology, to the chlorine movements of the comparison traffic groups selected by Canexus rather than the comparison traffic group selected by BNSF in Opening. We discussed the

³⁹ *March 12, 2012 Decision*, at 9.

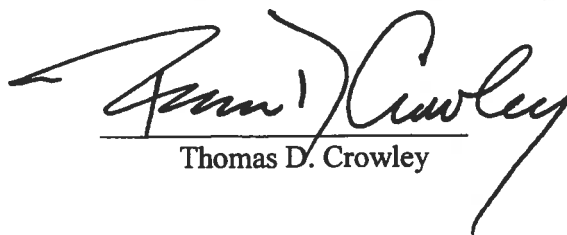
problems associated with BNSF's "Current Rate," "Historical PTC," "Liability Risk," and "Future PTC" adjustments at length in our Reply VS and showed that none of the adjustments are valid.

BNSF's application of its new "Public Current Rate Adjustment" in Reply is mechanically identical to its application of its original "Current Rate Adjustment" in Opening. The only difference is that BNSF applied the adjustments to the maximum R/VC ratio calculated based on application of the STB's Three-Benchmark methodology to the chlorine movements of the comparison traffic groups selected by Canexus rather than the comparison traffic group selected by BNSF in Opening. As discussed in the prior section of this Rebuttal VS, BNSF's new "Public Current Rate Adjustment" is also fatally flawed and should be rejected.

VERIFICATION

COMMONWEALTH OF VIRGINIA)
)
CITY OF ALEXANDRIA)

I, THOMAS D. CROWLEY, verify under penalty of perjury that I have read the foregoing Verified Statement of Thomas D. Crowley, that I know the contents thereof, and that the same are true and correct. Further, I certify that I am qualified and authorized to file this statement.


Thomas D. Crowley

Sworn to and subscribed
before me this 11th day of April, 2012



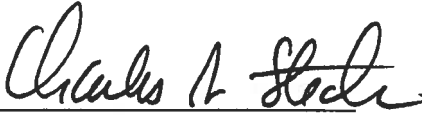
Helen Mary Koch
I was commissioned notary as Helen Mary Lunsford
Notary Public for the State of Virginia

My Commission Expires: May 31, 2015
Registration Number: 7507963

VERIFICATION

COMMONWEALTH OF VIRGINIA)
)
CITY OF ALEXANDRIA)

I, CHARLES A. STEDMAN, verify under penalty of perjury that I have read the foregoing Verified Statement of Charles A. Stedman, that I know the contents thereof, and that the same are true and correct. Further, I certify that I am qualified and authorized to file this statement.


Charles A. Stedman

Sworn to and subscribed
before me this 11th day of April, 2012



Helen Mary Koch
I was commissioned notary as Helen Mary Lunsford
Notary Public for the State of Virginia

My Commission Expires: May 31, 2015
Registration Number: 7507963