

BEFORE THE
SURFACE TRANSPORTATION BOARD

STB Ex Parte No. 657 (Sub-No. 1)

MAJOR ISSUES IN RAIL RATE CASES

**JOINT COMMENTS OF THE
PUBLIC SERVICE COMMISSION OF WISCONSIN
AND THE
WISCONSIN DEPARTMENT OF AGRICULTURE,
TRADE AND CONSUMER PROTECTION**

The Public Service Commission of Wisconsin (Commission) and the Wisconsin Department of Agriculture, Trade and Consumer Protection (Department) submit these comments in response to the Surface Transportation Board's (STB) notice of proposed rulemaking involving the application of STB's standards for large maximum reasonable rate cases under the Stand-Alone Cost Test. The Commission is an independent agency which regulates public utilities and holding companies and is mandated to protect the interests of the state's utility ratepayers. The Department is the state counterpart to the Federal Trade Commission and administers Wisconsin's unfair trade practice act, Wis. Stat. § 100.20, which prohibits unfair trade practices and methods of competition.

The Commission and the Department urge the STB to use its authority to protect rail customers and consumers and make determinations in this proceeding to reform monopolistic railroad practices, curb recent dramatic price increases, and ensure reliable service at just and reasonable rates.

WISCONSIN INTERESTS

The State of Wisconsin's economy depends upon railroad transportation. The State's agriculture, paper and forest product industries use rail to ship many of its products to market. Wisconsin electric utilities depend upon rail for coal deliveries to supply energy to industrial, commercial and residential customers. In 2004, freight railroads handled over 2.5 million cars and 107 million tons of freight in Wisconsin. Current rail service and cost problems are adversely affecting all sectors of Wisconsin's economy.

Over the last 20 years, the railroad industry has consolidated to the point where there are only four Class I railroads providing over 90 percent of the nation's rail transportation. The lack of effective competition or appropriate regulation in the railroad industry has fostered unjustifiably high shipment prices and unreliable shipping service. The recent experience of Wisconsin utilities exemplifies the seriousness of this situation.

Almost 25 percent of railroad freight in 2004 involved the delivery of coal. Wisconsin utilities burned 24,765,000 tons of coal at an estimated cost of over \$541,000,000.¹ Wisconsin produces about 60 percent of its electricity from coal, the majority of which comes from the Powder River Basin in Montana and Wyoming and the Appalachian region. There are only two railroad companies available to ship coal from these areas.

In recent years, once-stable coal costs have increased dramatically despite Wisconsin utilities' attempt to negotiate new, reasonable rates. On a delivered cost per ton basis, rail transportation represents a lion's share of the cost. Powder River Basin coal sold for around \$6 per ton in 2003; today it is selling for more than \$20 per ton. Appalachian coal, a much higher heat rate coal, went from around \$25 per ton in 2003 to as much as \$60 per ton today.

¹ 2005 Wisconsin Energy Statistics, Wisconsin Division of Energy, pages 39, 40, 43, 45.

Without reliable coal transportation, utilities must conserve their coal inventories, using higher priced natural gas-fired generation to produce electricity, adding to the cost of energy in Wisconsin. Last year, Wisconsin utilities incurred nearly \$50 million in costs associated with reduced shipment from Wyoming, the result of a train derailment and resulting rail maintenance.²

The Commission's last biennial Strategic Energy Assessment, docket 05-ES-102, September 2004 (Assessment), discusses the state's electric demand and supply conditions between the years 2000-2010. The Assessment notes that "coal-fired generating units provide the bulk of Wisconsin's generation capacity and will continue to do so for the foreseeable future."³

The cost of coal including rail transport is the largest percentage of the combined cost, typically 70 percent to 80 percent of the variable production cost for coal-fired generation. Railroad deregulation and consolidation and clean-air laws favoring low-sulfur coal have encouraged growth in Western regional coal output.

Restructuring of the electric power industry has promoted competition and cost-cutting measures by electric utilities, such as reductions in plant site coal inventories, increasing the importance of reliable transport...⁴

On March 23, 2006, the Commission initiated a formal inquiry to re-examine the appropriateness of various practices utilized in the natural gas and electric industries for procurement of natural gas and coal and associated cost recovery.⁵ This proceeding will consider coal procurement costs, including transportation costs used for electric generation.

The Commission's action is consistent with concerns raised by other state regulatory agencies. In February 2006, the National Association of Regulatory Utility Commissions Board

² We Energies filed a civil damage action against Union Pacific seeking 23 million dollars in damages related to coal deliveries. *Wis. Electric Power Co. v. Union Pacific Railroad Co.*, U.S. Dist. Court, Eastern Dist. of Wis., No. 06-C-0515 (Complaint, April 2006)

³Strategic Energy Assessment 2004, page 74 (http://psc.wi.gov/apps/erf_share/view/viewdoc.aspx?docid=38772).

⁴Strategic Energy Assessment 2004, page 75.

⁵Docket 5-UI-110 (http://psc.wi.gov/apps/cms_docket/content/DcktList.asp.)

of Directors passed a resolution, entitled “Resolution Urging Legal and Regulatory Reform to Improve Railroad Shipper Rates and Quality of Service.” (A copy of the resolution is attached as Attachment A.)

The Department has heard numerous complaints related to the lack of rail service and exponential increases in shipping rates from producers, manufactures, processors, and suppliers. Rate increases have put them at a substantial disadvantage because their rates are significantly higher than their competitors who are not captive rail customers. U.S. agricultural producers continue to lose U.S. markets to foreign imports due in part to excess U.S. rail rates. Producers have to scramble to find alternative transportation for harvested products when rail service is diminished or completely abandoned.

Clearly, the economic welfare, and vitality of not just Wisconsin, but also the nation, is affected by the present status of the rail transportation system. It is imperative that the STB, in this rulemaking process, make a thorough examination of current railroad operations and their effects upon captive customers. The transportation of coal deserves particular attention.

In conclusion, the Commission and the Department urge the board to carefully and thoroughly examine railroad market power and recent pricing actions and adopt regulatory rate protections to ensure reliable service at just and reasonable rates.

Dated at Madison, Wisconsin, _____

Public Service Commission of Wisconsin



Daniel R. Ebert
Chairperson

Wisconsin Department of Agriculture,
Trade and Consumer Protection



Rodney J. Nilsestuen
Secretary

Attachment
DRE:RJN:DJG:LMS:hms:ash:sp:k:\dgj\cases\major issues in rail cases\comments(2)

Resolution Urging Legal and Regulatory Reform to Improve Railroad Shipper Rates and Quality of Service

WHEREAS, The Staggers Rail Act of 1980 provided for the deregulation of competitive rail traffic and directed the Interstate Commerce Commission (now superseded by the Surface Transportation Board under the Department of Transportation) to continue to maintain reasonable rates where there is an absence of effective competition for rail traffic within the Board's jurisdiction; *and*

WHEREAS, Today, 25 years after passage of the Staggers Rail Act, over half of the electric energy in the United States is generated using coal, the majority of which is transported to electric utilities under non-competitive conditions, by no more than two railroad companies serving any coal region, which charge unjustifiably high monopoly prices for unreliable service, even though they are presumably subject to regulatory supervision by the Surface Transportation Board; *and*

WHEREAS, This body, the National Association of Regulatory Utility Commissioners (NARUC), passed a resolution in March of 1984, almost 22 years ago, voicing similar concerns about the lack of appropriate regulatory standards and alternatively the lack of competitive market conditions within the rail industry; *and*

WHEREAS, Today, 20 years after the last NARUC resolution on this issue, the railroad industry has consolidated to such a great extent that there are only 4 Class I railroads providing over 90% of the nation's rail transportation; *and*

WHEREAS, Today, in 2006, the nation is experiencing record high prices for natural gas, which has dramatically increased the cost of both natural gas and electricity service to the millions of business and residential customers in this country; *and*

WHEREAS, The cost of producing electricity with a gas-fired plant is several times higher than the cost of producing electricity with a coal-fired plant; *and*

WHEREAS, This economic statistic means that existing coal-fired electric generation should be used as much as possible in lieu of gas-fired generation in order to produce electricity more economically and to avoid upward pressure on natural gas prices; *and*

WHEREAS, Many coal plants in the United States are dependent on the low-sulfur coal supplies coming out of the Powder River Basin in Montana and Wyoming and the Appalachian region, yet only two railroad companies are available to ship coal out of each of these regions; *and*

WHEREAS, The Burlington Northern and Union Pacific in the west and the Norfolk Southern and CXS System in the east, have had significant reliability problems and have reduced their coal deliveries to firm contract customers in numerous States by 10 - 25%, thereby dramatically reducing the amount of coal inventory available for electricity production; *and*

WHEREAS, These reduced coal shipments have resulted in a substantially diminished ability of many electric utilities to rely on lower-cost electricity production from their existing coal plants, thereby necessitating the substitution of much higher-priced gas-fired production or market purchases of gas-fired generation to make up the difference; *and*

WHEREAS, These higher costs of substitute gas-fired electricity have resulted in significant rate increases to customers of rural electric cooperatives, public power authorities, and investor-owned utilities all across the country, totaling billions of dollars, and have placed upwards pressure on natural gas market prices; *and*

WHEREAS, These billions of dollars in higher energy bills have contributed to a higher manufactured product cost for many industries, lower net business earnings, less disposable household income, and diminished economic productivity across the country; *and*

WHEREAS, This problem could be alleviated through legislative and regulatory reform at the federal level that would ensure more reliable rail service, more railroad capacity, more rail carrier options for shippers, and more equitable rates for affected rail shippers; *now therefore be it*

RESOLVED, That the Board of Directors of the National Association of Regulatory Utility Commissioners (NARUC), convened in its February 2006 Winter Meetings in Washington, D.C., urges Congress to immediately address and resolve these issues by enacting legislation which would empower the Surface Transportation Board to develop and enforce quality of service standards and implement a more equitable rate-setting process, and to interpret the existing deregulation law to promote competition as well as ensure reasonable rates in a competitive market, and to also remove the railroad industry's exemption from the federal antitrust laws; *and be it further*

RESOLVED, That the National Association of Regulatory Utility Commissioners urges the development of specific federal legislation that would create mandatory reliability standards for the nation's railroad system, enforced by the Surface Transportation Board, along with rate reform to ensure just and reasonable rates, particularly in the absence of true competition, since this nation is no less dependent on a reliable and reasonably-priced rail system than we are on a reliable and reasonably-priced electric transmission system; *and be it further*

RESOLVED, That the National Association of Regulatory Utility Commissioners calls upon the members of the Surface Transportation Board to exercise their existing regulatory authority to protect rail customers and consumers in this country, and to support Congressional efforts to pass the additional legislation necessary to ensure reliable rail service at just and reasonable rates; *and enhance additional competition within the rail industry.*

Sponsored by the Electricity Committee

Passed by the NARUC Board of Directors February __, 2006