

SURFACE TRANSPORTATION BOARD<sup>1</sup>

Finance Docket No. 32760

UNION PACIFIC CORPORATION, UNION PACIFIC RAILROAD COMPANY, AND MISSOURI PACIFIC RAILROAD COMPANY--CONTROL AND MERGER--SOUTHERN PACIFIC RAIL CORPORATION, SOUTHERN PACIFIC TRANSPORTATION COMPANY, ST. LOUIS SOUTHWESTERN RAILWAY COMPANY, SPCSL CORP., AND THE DENVER AND RIO GRANDE WESTERN RAILROAD COMPANY

[Decision No. 62]<sup>2</sup>

Decided: November 27, 1996

In Decision No. 44, we approved the common control and merger of the rail carriers controlled by Union Pacific Corporation (Union Pacific Railroad Company and Missouri Pacific Railroad Company)<sup>3</sup> and the rail carriers controlled by Southern Pacific Rail Corporation (Southern Pacific Transportation

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<sup>1</sup> Proceedings before the Interstate Commerce Commission (ICC) that remained pending on January 1, 1996, must be decided under the law in effect prior to that date if they involve functions retained by the ICC Termination Act of 1995, Pub. L. No. 104-88, 109 Stat. 803. This proceeding was pending with the ICC prior to January 1, 1996, and relates to functions retained under Surface Transportation Board (Board) jurisdiction pursuant to new 49 U.S.C. 11102 and 11323-27. Citations are to the former sections of the statute, unless otherwise indicated.

<sup>2</sup> This decision embraces: Finance Docket No. 32760 (Sub-No. 1), Union Pacific Railroad Company, Missouri Pacific Railroad Company, Southern Pacific Transportation Company, St. Louis Southwestern Railway Company, SPCSL Corp., and The Denver and Rio Grande Western Railroad Company--Trackage Rights Exemption--Burlington Northern Railroad Company and The Atchison, Topeka and Santa Fe Railway Company; Finance Docket No. 32760 (Sub-No. 2), Burlington Northern Railroad Company and The Atchison, Topeka and Santa Fe Railway Company--Petition for Exemption--Acquisition and Operation of Trackage in California, Texas, and Louisiana; Finance Docket No. 32760 (Sub-No. 13), Responsive Application--The Texas Mexican Railway Company; Finance Docket No. 32760 (Sub-No. 14), Application for Terminal Trackage Rights Over Lines of The Houston Belt & Terminal Railway Company--The Texas Mexican Railway Company; Finance Docket No. 32760 (Sub-No. 19), Burlington Northern Railroad Company and The Atchison, Topeka and Santa Fe Railway Company--Trackage Rights Exemption--Union Pacific Railroad Company, Missouri Pacific Railroad Company, Southern Pacific Transportation Company, St. Louis Southwestern Railway Company, SPCSL Corp., The Denver and Rio Grande Western Railroad Company, and The Southern Illinois & Missouri Bridge Company; and STB Finance Docket No. 32760 (Sub-No. 20), The Atchison, Topeka and Santa Fe Railway Company--Trackage Rights Exemption--Southern Pacific Transportation Company.

<sup>3</sup> Union Pacific Corporation is referred to as UPC. Union Pacific Railroad Company and Missouri Pacific Railroad Company are referred to collectively as UP.

Company, St. Louis Southwestern Railway Company, SPCSL Corp., and The Denver and Rio Grande Western Railroad Company),<sup>4</sup> subject to various conditions.<sup>5</sup> Among the conditions we imposed was the *Tex Mex condition*, which requires that The Texas Mexican Railway Company (Tex Mex) be granted the Robstown/Corpus Christi-Houston-Beaumont trackage rights sought in its Sub-No. 13 responsive application and in its Sub-No. 14 terminal trackage rights application, subject, however, to the *prior/subsequent restriction* that provides that all freight handled by Tex Mex pursuant to such trackage rights must have a prior or subsequent movement on Tex Mex's Laredo-Robstown-Corpus Christi line.<sup>6</sup>

Tex Mex, which wants the prior/subsequent restriction removed, has filed a petition (TM-44) to reopen Decision No. 44. Replies have been filed by: UP/SP (UP/SP-283); BNSF (BN/SF-69);<sup>7</sup> the Railroad Commission of Texas (RCT-9); Dow Chemical Company (DOW-30); The National Industrial Transportation League (NITL-23);<sup>8</sup> and The Society of the Plastics Industry, Inc. (SPI-26). We have also received a number of letters supporting the Tex Mex petition. See also TM-46 and TM-47 (letters of shippers and public officials supporting the Tex Mex petition); BNSF's "Progress Report and Operating Plan" filed October 1, 1996 at 20-22 (more discussion of the matters raised in the TM-44 petition); and TM-48 at 8-10 (same).

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<sup>4</sup> Southern Pacific Rail Corporation is referred to as SPR. Southern Pacific Transportation Company, St. Louis Southwestern Railway Company, SPCSL Corp., and The Denver and Rio Grande Western Railroad Company are referred to collectively as SP.

<sup>5</sup> Common control was consummated on September 11, 1996, when SPR was merged with and into UP Holding Company, Inc., a direct wholly owned subsidiary of UPC. See UP/SP-277 at 1. UPC, UP, SPR, and SP are referred to collectively as applicants. See Decision No. 44, slip op. at 7 n.3.

<sup>6</sup> See Decision No. 44, slip op. at 30-33 and 147-51. See also Decision No. 47 (addressing certain details respecting the Tex Mex trackage rights).

<sup>7</sup> Burlington Northern Railroad Company and The Atchison, Topeka and Santa Fe Railway Company are referred to collectively as BNSF. See also Decision No. 44, slip op. at 12 n.15 (description of the BNSF agreement, which we also imposed as a condition in Decision No. 44).

<sup>8</sup> See also the TFI-3 reply filed by The Fertilizer Institute.

**BACKGROUND**

Tex Mex contends that imposition of the prior/subsequent restriction was material error for several reasons.

*First.* Tex Mex contends that the prior/subsequent restriction leaves uncorrected a serious competitive harm that the merger will cause to many shippers, including particularly shippers located in Houston. Before the merger, Tex Mex notes, those shippers were served by three line-haul railroads; after the merger, they will be served by only two line-haul railroads (except with respect to traffic having a prior or subsequent movement on Tex Mex's own line). Unique aspects of the Houston rail market, Tex Mex claims, make the loss of a third competitive outlet in that rail market significantly more harmful than it would be in most other rail markets. Tex Mex claims: that very little of the 3-to-2 traffic to or from Houston is intermodal or automotive; that 50% of the Houston 3-to-2 traffic is chemical traffic; that, of the Houston 3-to-2 traffic, 75% moves more than 600 miles and 50% moves more than 1,200 miles; and that, for these reasons, very little of the 3-to-2 traffic in the Houston market is subject to substantial truck competition. Tex Mex further claims: that SP is a much more significant competitor in the Houston market than in most other 3-to-2 markets; that, for much of the traffic in Houston, BNSF has a small share; and that, for these reasons, the competitive situation in Houston is closer to 2-to-1 than to 3-to-2.<sup>9</sup>

*Second.* Tex Mex maintains that the prior/subsequent restriction will *both* impose unnecessary costs and operating inefficiencies *and* seriously impair Tex Mex's ability to compete effectively for the traffic it is permitted to carry. The principal difficulty presented by the prior/subsequent restriction, Tex Mex claims, arises from the fact that shippers (e.g., plastics manufacturers) often deliver cars to a railroad before the ultimate destination of the car is known. For example, if a Houston shipper initially routes a group of 100

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<sup>9</sup> Tex Mex adds that the competitive situation respecting traffic moving from/to Houston is analogous to the competitive situation respecting traffic moving across the U.S.-Mexico border: it may be a 3-to-2 situation in some theoretical way, but, on account of BNSF's "extremely limited" pre-merger presence, it is effectively a 2-to-1 situation. See Decision No. 44, slip op. at 148 & n.182.

cars to Tex Mex and later sells 90 of the carloads to buyers in Mexico and 10 of the carloads to buyers in Kansas City, Tex Mex notes that, in this situation, it could carry the 90 cars to Laredo but, even though it will be operating a regular train from Houston to Beaumont consisting of freight having a prior movement on Tex Mex's own line, it could not carry the 10 cars to Beaumont for interchange with its KCS affiliate<sup>10</sup> and would have to switch these cars to UP/SP or BNSF in Houston. This switching, Tex Mex claims, will entail costs and additional transit times that would not be incurred by UP/SP or BNSF if the cars were delivered to them. Tex Mex adds that shippers will be discouraged from routing via Tex Mex any carloads whose ultimate destination is not known at the time of initial delivery, and that this will seriously impair Tex Mex's ability to compete even for traffic that would ultimately traverse its Laredo-Robstown-Corpus Christi line.

*Third.* Tex Mex contends that we were under a misimpression that Tex Mex conceded the correctness of UP/SP's objections to Tex Mex's carrying traffic not having a prior or subsequent movement on its own line. This argument concerns a concession Tex Mex made in its TM-34 rebuttal submission (filed May 14, 1996):

An incidental competitive benefit of granting the rights Tex Mex seeks is that Tex Mex could carry some shipments between Beaumont and Houston that had no prior or subsequent rail movement south of Houston. This, however, would be a relatively minor benefit, and it was certainly not a central purpose of the application. Tex Mex submits that there is no reason to deny a remedy that is appropriate to mitigate anticompetitive effects of a merger merely because the remedy has other incidental competitive benefits, or to perform some Procrustean operation on that remedy just to prevent it from being too beneficial. *However, if the Board concludes that providing those shippers with this modicum of additional competition is not competitively justified, it could limit the rights granted to exclude Tex Mex from carrying shipments between Houston and Beaumont that have no prior or subsequent movement by rail south of Houston. Such a limitation would not undermine the purposes for which the rights are being sought. Nor would it significantly*

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<sup>10</sup> The Kansas City Southern Railway Company is referred to as KCS. See Decision No. 44, slip op. at 31 & n.41.

affect Tex Mex's ability to provide essential services for customers local to its line.

TM-34 at 7 (emphasis added). Two days later, Tex Mex filed an "Errata By Way Of Clarification" arguing that it had made no concessions or amendments to its applications, and did not support or endorse any limitation of the trackage rights sought in those applications. TM-35 at 1-2 (filed May 16, 1996). Tex Mex insists that it has never conceded the correctness of UP/SP's arguments respecting Houston-Beaumont traffic, it has never believed that the rights it has sought should be limited in any way, and it has never suggested that the right to carry traffic having no prior or subsequent movement south of Houston was unimportant to Tex Mex or was not justified.<sup>11</sup>

*Fourth.* Tex Mex contends that removal of the prior/subsequent restriction is extremely important to Tex Mex's ability to function as a viable competitor to a merged UP/SP. Approval of the Tex Mex applications in their entirety, Tex Mex claims, will produce \$822,000 more in revenues and \$250,000 more in net income to Tex Mex in the first year of operation than approval of such applications subject to the prior/subsequent restriction. The first year net income calculation, Tex Mex notes, is especially important--\$269,000 net income with unrestricted rights, but only \$19,000 net income with restricted rights. Tex Mex acknowledges that the \$19,000 calculation represents net income and not net loss, but insists that it would provide Tex Mex with little margin for weathering business cycles and, more importantly, little incentive to compete aggressively. Tex Mex concedes that it can survive without the traffic made unavailable by the prior/subsequent restriction, TM-44 at 16, but claims that its survival without this traffic will be extremely tenuous.

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<sup>11</sup> We think it appropriate to observe that we did not ignore or misconstrue Tex Mex's argument that we should not restrict its access to Houston. Although we noted Tex Mex's TM-34 concession (Decision No. 44, slip op. at 149-50), we also explicitly noted its TM-35 "clarification" (Id., slip op. at 32 n.42).

**DISCUSSION AND CONCLUSIONS**

A proceeding may be reopened, and reconsideration granted, upon a showing of material error, new evidence, or substantially changed circumstances. 49 CFR 1115.3(b) (1995). See also Burlington Northern Inc. and Burlington Northern Railroad Company--Control and Merger--Santa Fe Pacific Corporation and The Atchison, Topeka and Santa Fe Railway Company, Finance Docket No. 32549 (ICC served Nov. 27, 1995) (Decision No. 43, slip op. at 2). Tex Mex has asserted material error and, to a limited degree, new evidence; it has not asserted substantially changed circumstances. As a practical matter, however, the TM-44 petition rests entirely upon the assertion of material error, because the new evidence that has been presented is only tenuously "new" and is certainly not material.

The TM-44 petition will be denied. The merger, as presently conditioned, will have no significant adverse competitive effects on Houston traffic or at the Laredo border crossing into Mexico. Thus, there is no reason to grant Tex Mex unrestricted access to Houston traffic.

The purpose of the trackage rights given to Tex Mex was to address the possible loss of competition at the Laredo gateway into Mexico and to protect the essential services provided by Tex Mex to its shippers. There is no nexus between the potential difficulty we discerned with regard to Laredo, which we have ameliorated with our partial grant of the Tex Mex applications, and the Houston transportation market.

Our grant of trackage rights was premised on our concerns "that the merger will diminish [Tex Mex's] traffic base to the point where it is unable effectively to preserve a second competitive routing at Laredo, and that the merger might endanger the essential service it provides to the more than 30 shippers located on its line." Decision No. 44, slip op. at 148. Although BNSF's settlement agreement with applicants anticipated that BNSF would replace SP as an independent interline partner for Tex Mex traffic bound to and from Laredo, we explained that "[t]his does not mean that BNSF will be able to retain all the traffic now carried by SP." Id. at 148.

BNSF also received enhanced access to Mexico at Eagle Pass. This created an additional concern that BNSF might favor its new, efficient, single-line movement into Eagle Pass over its new interchange with Tex Mex into Laredo. Thus, our analysis led to the conclusion that only a partial grant of the Tex Mex applications was required to ensure the continuation of an effective competitive alternative to UP's routing into the border crossing at Laredo.

Our partial grant of the Tex Mex applications was not directed at mitigating any supposed competitive harm arising at Houston. Despite the continued assertions of Tex Mex, the 3-to-2 situation at Houston is not unique, and is much the same as at other 3-to-2 points. In addition, there is very little of the Houston traffic that was served by all three Class I railroads operating there prior to this merger.<sup>12</sup> The merger should actually strengthen competition in Houston by replacing SP with a stronger BNSF.<sup>13</sup> BNSF has been granted additional routes into and out of Houston that preserve and will reinforce competition for Houston rail traffic.

A significant amount of the traffic at Houston points served directly or by reciprocal switching by three rail carriers before the merger, but by only two carriers after, is truck-competitive intermodal traffic. Intermodal shippers have broadly supported this merger, and we have found that this traffic will not suffer any merger-related harm. See, e.g., Decision No. 44, slip op. at 269. Further, as applicants have explained:

Whereas Tex Mex's petition relies on the fact that much Houston traffic is chemicals rather than intermodal, the traffic gains that Tex Mex expects if the prior/subsequent movement limitation is removed relate almost entirely to intermodal traffic and not chemicals traffic. Of the 3,510 units of traffic that Tex Mex believes its [sic] would gain if the limitation were removed, over 88% (3,100 units) is intermodal. TM-44, p. 15.

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<sup>12</sup> Tex Mex has measured 3-to-2 flows using BEAs (Business Economic Areas), which we have found to be an overly broad definition of origins and destinations. See Decision No. 44, slip op. at 106 n.102 and 123 n.130.

<sup>13</sup> "SP is a constrained, not a full competitor, with limited impact on the pricing actions of other western carriers." Decision No. 44, slip op. at 121.

UP/SP-283 at 11 n.4 (emphasis in original). We have carefully examined the role of rail transportation for chemicals and plastics shippers in the Gulf area, and determined that the merger, as we have conditioned it, is unlikely to have any significant adverse competitive effects. See Decision No. 44, slip op. at 151-54. And, the monitoring condition we have imposed will ensure that we can detect and remedy any unforeseen competitive harm.

In addition, Tex Mex offered a comparison of rates for certain Houston shippers that attempts to quantify the asserted harm when the number of carriers is reduced from three to two. This study purports to show that rates for three-carrier shippers are over 20% lower than those for two-carrier shippers at Houston. But applicants have shown certain fundamental flaws in this study, and it cannot support the conclusions Tex Mex has drawn from it. The most important of the flaws is linked to the significantly longer lengths of haul for the three-carrier traffic group. The study merely shows that route distance and revenue per ton-mile are inversely related. Average rail transport costs per mile decrease as the length of haul increases, and this has caused the rate differences observed in the study, not the number of railroads serving the shippers. See UP/SP-283 at 12-13.

Finally, the circumstances surrounding the 3-to-2 situation at Houston are altogether different from those for the Mexican traffic. We determined that, absent our partial grant of the Tex Mex applications, the merger could lead to competitive problems at Laredo in part because BNSF would begin interlining with Tex Mex while also being able to use its own new, efficient, single-line routes to other Mexican gateways, in particular Eagle Pass. At Houston, BNSF will not face the impediments faced by Tex Mex at Laredo. We are confident that BNSF will emerge as a strong and effective replacement at Houston for the competition lost through the merger. BNSF will have its own single-line routes throughout the West and to all the major Eastern gateways. Thus, BNSF's position at Houston is completely different from the predicament that Tex Mex was facing at Laredo.

Restricting Tex Mex's use of these trackage rights to traffic having a prior or subsequent movement on Tex Mex's lines will not have the profound adverse effect alleged by Tex Mex on

the efficiency of its trackage rights or on its ability to compete for traffic. Applicants have effectively rebutted Tex Mex's contention that the requirement of some plastics shippers that they be able to use storage-in-transit facilities will unduly limit Tex Mex's ability to compete for Houston traffic moving into Mexico. Plastics comprise only 3% of the Houston traffic bound for Mexico, and none of this traffic requires storage-in-transit. See UP/SP-283, Peterson V.S. at 11-12. The inefficiencies that are asserted by Tex Mex will, at worst, apply to a very small subset of the traffic that would be available to Tex Mex without the restrictions we have imposed. That this traffic might not be available, with restrictions, should not overly burden Tex Mex's use of its new trackage rights. And, our concern in granting those rights continues to rest solely on the ability of Tex Mex to be able to generate sufficient density and efficiencies on its own lines to remain a competitive force at Laredo, which is attainable through the trackage rights that have been granted to Tex Mex by the Board.

As to the financial effects of the restrictions, they also were argued previously by Tex Mex. No new information has been presented here. Tex Mex continues to project that it will earn a small profit of \$19,000 if the restrictions on its trackage rights at Houston remain in place. TM-44 at 15. We are confident that Tex Mex is adequately positioned to be competitive for traffic flowing through Laredo. As is pointed out by applicants, both applicants' and Tex Mex's traffic analyses were undertaken when U.S.-Mexican traffic levels were depressed due to the Mexican peso devaluation. In the interim, there has been a strong recovery in traffic volumes between the two countries. See UP/SP-283, Peterson V.S. at 12-14. Also, Tex Mex's analysis of its trackage rights gains focused only on existing traffic that could be diverted to Tex Mex. This ignores the traffic increases that should be generated by NAFTA (the North American Free Trade Agreement) and Tex Mex's prospect for new traffic as a result of its being able to connect with its affiliated carrier, KCS, via its trackage rights. Applicants note that the addition of a single additional grain train every other week would generate more additional net income for Tex Mex than the total net income it projects if we were to remove the restrictions on its trackage rights. See UP/SP-283 at 18.

This action will not significantly affect either the quality of the human environment or the conservation of energy resources.

It is ordered:

1. The TFI-2 motion for leave to file the TFI-3 reply is granted.
2. The TM-44 petition is denied.
3. This decision shall be effective on November 27, 1996.

By the Board, Chairman Morgan, Vice Chairman Simmons and Commissioner Owen.

Vernon A. Williams  
Secretary