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PUBLIC VERSION

BEFORE THE
SURFACE TRANSPORTATION BOARD

FINANCE DOCKET. NO. 35081

CANADIAN PACIFIC RAILWAY COMPANY, ET AL.

– CONTROL –

DAKOTA, MINNESOTA & EASTERN RAILROAD CORP., ET AL.

COMMENTS OF THE KANSAS CITY SOUTHERN RAILWAY COMPANY AND REQUEST FOR CONDITIONS

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INTRODUCTION AND BRIEF SUMMARY OF ARGUMENT

In accordance with the procedural schedule set forth in Decision No. 4 in above-captioned proceeding, The Kansas City Southern Railway Company ("KCSR") hereby submits these Comments And Request For Conditions ("Comments"). In this proceeding, the Surface Transportation Board is considering under 49 U.S.C. §§ 11321-26 whether to approve, reject, or condition the application filed on December 5, 2007, for Canadian Pacific Railway Corporation ("CP") and Soo Line Holding Company, a Delaware Corporation and indirect subsidiary of CPRC ("Soo Holding"), to acquire control of Dakota, Minnesota & Eastern Railroad Corporation ("DM&E") and Iowa, Chicago & Eastern Railroad Corporation ("IC&E"), a wholly owned rail subsidiary of DM&E.[1] The Transaction has been deemed "significant" for purposes of consideration under §§ 11321-26.

[1] The proposal is referred to as the "Transaction," and CP, Soo Holding, DM&E, and IC&E are referred to collectively as "Applicants." CP and its U.S. rail subsidiaries, Soo Line Railroad Company ("Soo") and Delaware and Hudson Railway Company, Inc. ("D&H") operate a transcontinental rail network over 13,000 miles in Canada and the United States and will be collectively referred to as "CP." DM&E and IC&E operate over 2,500 miles of rail lines serving either U.S. states and will be collectively referred to as "DME."

KCSR does not object to approval of the Transaction as long as the Board imposes certain conditions to preserve the competitive routing options currently available to shippers and receivers located on the lines of DME and KCSR. DME plays a critical role in providing its shippers with direct, single-line service to the major rail gateways of Chicago, Kansas City, and Minneapolis/St. Paul, and, in conjunction with connections to KCSR and others, DME provides shippers with neutral interline access to significant long-haul destination markets in the south-central United States.[2] Indeed, KCSR has an agreement with DME that gives KCSR ratemaking authority for the transportation of grain from origins in Iowa and Minnesota to destinations in Texas, Oklahoma, Kansas, Missouri, Arkansas, Mississippi, Louisiana, and Alabama (i.e., the south-central United States). KCSR has likewise been able to access Chicago via an agreement with DME; access that KCSR did not have prior to the DME Transaction. Additionally, DME and BNSF Railway ("BNSF") have been able to develop an efficient interline market for the transportation of corn to the export markets in the Pacific Northwest ("PNW"). These KCSR/DME or BNSF/DME routings compete with certain CP single-line services and also with joint-line services CP offers with alliance partner, Union Pacific ("UP").

CP's control of DME will insert CP into all of the DME routings for the various markets, eliminating the neutrality of the DME /KCSR or DME/BNSF routings. As these comments and the verified statements of Michael Bilovesky (Exhibit A), Dr. Curtis Grimm

[2] See Dakota, Minnesota & Eastern Railroad Corporation And Cedar American Rail Holdings, Inc. – Control – Iowa, Chicago & Eastern Railroad Corporation, STB Finance Docket No. 34178, slip. op at 8 (STB served Feb. 3, 2003) ("DM&E-IC&E"); see also Iowa, Chicago & Eastern Railroad Corporation – Acquisition and Operation Exemption – Lines of I&M Rail Link, LLC, Finance Docket No. 34177 (STB served Jun. 12, 2002 and Jul. 22, 2002) ("IC&E-IMRL"). The transactions encompassed by DM&E-IC&E and IC&E-IMRL will be referred to as the "DME Transaction."

(Exhibit B), George Woodward (Exhibit C), and Thad Jones (Exhibit D) discuss,[3] CP will, in turn, re-route DME traffic to CP long-haul destinations (or to UP-served destinations), and has incentives to degrade service over the DME/KCSR routings and cancel the agreement governing KCSR's access to Chicago. Such actions will eliminate competition and increase rates for certain shippers and receivers.[4]

To preserve the important neutral role of DME and remedy the competitive harm that will result from the Transaction, the Board needs to impose certain narrowly-tailored conditions. These conditions merely preserve the existing competitive routings that exist today by: - (1) making permanent KCSR's existing ratemaking authority for the origination of corn from DME origins; (2) ensuring that CP takes no action to degrade the transit times over the existing DME/KCSR routing; and (3) ensuring the permanence of KCSR's ratemaking authority to/from the Chicago gateway.

ARGUMENT

I. THE TRANSACTION WILL REDUCE COMPETITION IN THE RAIL TRANSPORTATION OF GRAIN

A. Grain Is An Important Rail-Dependent Commodity

Given its recent Ex Parte No. 665 proceeding, the Board is fully aware of the importance of grain to the U.S. economy. The Board stated it best when it said:

> Throughout this nation's history grain production has been important to our economy. In addition to its vital role in human food consumption, grain has been integral to other industries as feed for poultry and livestock and, more recently, a feedstock in the production of alternative fuel. Production, storage,

[3] Exhibit E contains any evidentiary exhibits gained in discovery and cited in this document or by any of the witnesses. It also contains excerpts of the relevant deposition pages to the extent those pages are noted herein.

[4] For example, CP will divert DME grain to export markets in the PNW and thereby eliminate a primary source of grain for numerous feed mills in the south-central United States. These receivers of DME/KCSR originated corn will be forced to pay more to receive the same product from another origin.

> shipping, and processing locations form a well-established network for delivery of grains, oilseeds and processed products from scattered points of origin to many points of consumption, often separated by great distances. Thus, many grain shippers and processors are captive to the railroads.

Rail Transportation Of Grain, Ex Parte No. 665 (STB served Jan 14, 2008). As relevant to this proceeding and the conditions that KCSR requests, there are three important points made in this statement: (1) grain is heavily dependent upon rail for its transportation (the Board uses the phrase "captive to the railroads"); (2) grain is used in human consumption;[5] and (3) grain is integral as "feed for poultry."

The rail transportation of grain is of such concern that it has been discussed in two recent GAO reports,[6] was the subject of written testimony and an oral hearing in the Ex Parte No. 665 proceeding, and an STB authorized study will examine, in part, the rail transportation of grain.[7] Of course, grain repeatedly has been analyzed and discussed throughout the history of the ICC and STB. There is even a Grain Car Council operating pursuant to this Board's official authorization (STB Ex Parte No 519 (Sub-No. 3)) that advises the Board on rail/shipper grain issues. Such an intense focus on grain transportation is justified because, as the Board noted in the Rail Transportation of Grain proceeding, the grain industry is more sensitive than other industries to rail rates because grain shippers (or

[5] A significant portion of the grain that KCSR and others exports to Mexico is used for human consumption.

[6] On June 21, 2006, United States Government Accountability Office ("GAO") issued a preliminary report entitled "Freight Railroads: Preliminary Observations on Rates, Competition, and Capacity Issues." GAO issued a final report on October 6, 2006, which was entitled "Freight Railroads: Industry Health Has Improved, but Concerns about Competition and Capacity Should Be Addressed." These two documents will be referred to collectively as the "GAO Report."

[7] The Board has awarded a contract to Christensen Associates to conduct an independent study assessing the current state of competition in the freight railroad industry in the United States. The study, entitled "Report to the U.S. STB on Competition and Related Issues in the U.S. Freight Railroad Industry," will be completed and made public later this year.

the receivers/users of that grain) generally directly bear any increase in the transportation costs. Such views are largely consistent with those of the United States Department of Agriculture ("USDA") and as expressed in the GAO Report.

B. The ICC And STB Have Acted To Ensure Adequate Rail Competition For The Movement Of Grain Via The Kansas City Gateway

Given the importance of grain, the Board, and the Interstate Commerce Commission ("ICC" or "Commission") before that, have always carefully scrutinized mergers or other control transactions that could result in the reduction of railroad routing options for grain shippers as well as adversely impact the receivers (or end users) of that grain. Indeed, absent such past scrutiny, and the Board's willingness to impose conditions to preserve competition, the KCSR rail routings that shippers enjoy today for the movement of grain to Mexico and to the poultry markets in the south-central U.S. would not exist.

Prior to 1988, KCSR directly served few grain sources. Almost all of the grain KCSR transported was originated via reciprocal switch or received in interchange from other carriers and was taken either to the Gulf Coast for export or to the south-central U.S. All of that began to change in the late 80's and early 90's. This change was a direct result of the ICC's proactive decisions to preserve important rail routings for grain, especially to preserve competition for those routes that would have been lost as a result of the UP-Missouri-Kansas-Texas Railroad ("MKT") merger.[8] In that decision, the ICC imposed a condition which eventually resulted in KCSR having direct ratemaking authority to certain non-KCSR served origins, including the Omaha/Council Bluffs area (which today represents one of the nation's largest grain origination points). Even that condition was itself the result of a prior condition

[8] Union Pacific Corp., et al. – Control – MO-KS-TX, et al., 4 I.C.C.2d 409 (1988) ("UP-MKT")

that the ICC had imposed in the Union Pacific-Missouri Pacific (MP)-Western Pacific (WP) merger to preserve grain routings.[9]

As the Commission noted in UP-MP-WP, at the time of the proposed UP-MP-WP merger, three rail routes competed for the movement of grain from the Omaha/Council Bluffs area into the Gulf area: MP direct, Burlington Northern ("BN") direct, and UP-MKT interline. UP-MP-WP at 531. The Commission recognized that the proposed UP-MP-WP merger would eliminate parallel competition between UP and MP from Omaha/Council Bluffs to Kansas City. In addition, the Commission was concerned that the UP-MP-WP combination would vertically foreclose MKT from participating in shipments originating in the Omaha/Council Bluffs area and destined for the Gulf Id.

The Commission realized that, after the consolidation, UP would have an incentive to favor the MP line south of Kansas City to maximize its profit on grain movements from Omaha/Council Bluffs to the Gulf. Since MKT at that time handled the largest amount of UP traffic moving to the Gulf via Kansas City, the Commission found that MKT's ability to compete against MP for grain flows south of Kansas City would be directly affected by UP's ability to divert such traffic to the MP line. Id. at 530.[10] Accordingly, the Commission conditioned the UP-MP-WP merger upon a grant of trackage rights to MKT over UP lines from Kansas City to Omaha/Council Bluffs, Lincoln, Atchison, and Topeka so as preserve an independent routing for grain from those origins to the southern markets (the "north-end" rights).

[9] Union Pacific – Control – Missouri Pacific; Western Pacific, 366 I.C.C. 462 (1982) ("UP-MP-WP")

[10] The same situation existed with respect to grain traffic originated at Lincoln, NE, and Atchison and Topeka, KS.

From 1982 until 1988, MKT used its north-end rights to continue to provide competition to the UP system. In 1987, however, UP sought authority to acquire and control MKT. The Commission recognized that the grant of north-end trackage rights to MKT in UP-MP-WP promoted competition among rail carriers (including among UP and MKT) for grain shipments from Omaha/Council Bluffs to the Gulf. UP-MKT at 454. Realizing that a UP-MKT combination would cause a reduction in competition similar to that found in the UP-MP-WP case, the Commission conditioned its approval of the UP-MKT merger upon the transfer of those north-end rights to another carrier in order to preserve competition for grain moving from Omaha/Council Bluffs into the Gulf Coast, Mexico and the south-central states. KCSR was eventually selected to succeed to MKT's rights, and although it had the right to use trackage rights, KCSR chose instead to use haulage rights that could be converted to trackage rights. Since then, KCSR has been originating grain from Omaha/Council Bluffs pursuant to these haulage rights. Of importance, however, was that KCSR had, for the first time, gained a significant source of grain for the Gulf Coast, Mexico and feed mills in the south-central states. Since then, KCSR has competed against UP routings in these very same corridors.

With the advent of NAFTA, KCSR became an even more significant competitor, particularly in the Omaha/Council Bluffs-Kansas City-Laredo corridor. Prior to 1996, however, whatever grain KCSR originated for the Mexican export market was interchanged to Southern Pacific at Beaumont, who in-turn interchanged it to The Texas Mexican Railway Company for export through Laredo. KCSR still did not have single-line route capable of competing against UP for grain moving to Mexican consumers, while UP did have such a single-line route. In 1996, the Board's action in granting Tex Mex's trackage rights to a connection with KCSR at Beaumont in the UP/SP merger proceeding not only preserved competition at the Laredo gateway for all forms of NAFTA traffic (including movements from Detroit and Chicago), but it also for the first time, provided KCSR with single-line pricing authority for grain from the heartland of the grain growing regions of the U.S. to Mexico; thereby enhancing the number of carriers competing in the NAFTA corridor.

Today, as a result of the ICC's and Board's collective actions in the three merger cases to preserve competition in this important corridor, KCSR moves approximately [redacted] carloads of grain [redacted] to Mexico. Grain now represents 12% of KCSR's overall business, 42% of its overall shipments to Mexico, and shippers have a single-line pricing alternative to UP for NAFTA moves. This very important option for shippers and receivers was not possible prior to 1988 and would not be available now if the Board had not acted to preserve competition.

C. <u>DME Is An Important Neutral And Independent Source Of Grain For KCSR Receivers In The Southeast</u>

In 1997, I&M Rail Link, LLC ("IMRL") was formed out of various rail lines that were part of the Soo/CP system.[11] At that time, KCSR entered into an agreement with IMRL providing KCSR with ratemaking authority over IMRL's lines in order to offer a seamless transportation alternative for customers located on both IMRL and KCSR. Among other things, the agreement granted KCSR two major marketing rights: (1) the right to price and market grain from the heart of Iowa and Minnesota via a network of lines known as the "Corn Lines"[12] to any and all KCSR destinations (the "Grain Agreement"); and (2) access to Chicago by granting KCSR with pricing authority between Kansas City and Chicago for

[11] <u>See</u> <u>I&M Rail Link, LLC – Acq. & Oper. Exem. – Canadian Pacific Ry.</u>, 2 S.T.B. 167 (1997).

[12] The "Corn Lines" consist of former Soo, then IMRL, and now IC&E grain-gathering lines in Iowa, including an east-west line from Jackson to Ramsey, and a separate east-west line from Sheldon, through Mason City, to Marquette.

chemical, forest products and other carload customers in order to create alternative routes between Chicago and KCSR territory (the "Chicago Agreement").[13] These agreements provide shippers with competitive options to the UP and BNSF routings against which KCSR competes.

When the DM&E/IC&E Transaction was announced in 2002, KCSR both privately and publicly (through filings at the STB) expressed concern that DM&E not use its control and ownership of the former IMRL lines to cancel the IMRL/KCSR agreements or reduce transit times. Indeed, in its application to control IC&E (which had acquired the IMRL system, including the Corn Lines), DM&E promised that grain receivers would continue to have reliable and long-term access to grain not only from the Corn Lines but also from DM&E *origins in Minnesota and South Dakota.*[14] DM&E *touted the benefits of grain* shippers located on its lines having access to the Kansas City and Chicago markets. The Board highlighted such benefits in its DM&E-IC&E decision at page 6 where it said "applicants maintain . . .that grain shippers will enjoy, for the first time, direct single system service to the major rail gateways of Chicago and Kansas City, new single-system routes to major grain processing plants on IC&E, new direct joint-line routes to processors elsewhere in Iowa – and 'neutral' interline access to significant long-haul destination markets in the south central United States." The Board approved IC&E's acquisition of the IMRL system and, subsequently, DM&E's control of IC&E based in large part upon these representations.

During the DM&E/IC&E proceeding, KCSR sought DM&E's assurance that it would honor the KCSR/IMRL agreement and abide by its representations to the STB. KCSR did in

[13] Selected portions of the Grain Agreement (excluding rates and divisions provisions) and the Chicago Agreement are included in Exhibit E (KCSR HC 00001-00013).

[14] For example, DM&E claimed that "[s]hippers on IC&E will be part of a stable, secure rail system, with truly neutral access to every Class I railroad in the nation, for the first time in many years, if ever." DM&E/IC&E Application at 5.

fact receive such assurances, and the Board's decision noted the importance of DM&E's assurances to keep the DM&E/IC&E system neutral, to maintain existing agreements, and not eliminate any then-existing interchanges. As a result of both private negotiations and the Board's decision, KCSR and DME later amended the original Grain Agreement to expand its scope, add transit time objectives, make other changes, and to extend the term. See Verified Statement of Mr. Michael Bilovesky, Vice President, Sales and Marketing-Agriculture and Minerals Business Unit for The Kansas City Southern Railway Company ("V.S. Bilovesky"), attached hereto as Exhibit A, for a complete discussion of this agreement.

The Grain Agreement effectively linked IC&E-served grain elevators in Iowa and Minnesota with KCSR-served poultry markets. A large portion of the corn handled under this agreement moves in unit trains where [redacted]. These trains supply corn to some 28 feed mills serving the poultry industry in the south-central states of Texas, Oklahoma, Missouri, Arkansas, Louisiana, and Mississippi. KCSR also moves DME corn and soybeans for export under the Grain Agreement. V.S. Bilovesky at 5. As a direct result of the agreement, in 2006, KCSR received [redacted] carloads from DME origins, of which [redacted] moved in domestic grain service to the south-central states. KCSR's total domestic grain business from all origins, including Council Bluffs/Omaha, was [redacted] carloads. As such, DME traffic represents [redacted] of KCSR's total domestic grain volume. V.S. Bilovesky at 4. Grain originating on DME is the primary source of grain for many of the KCSR-served feed mills in the south-central states.[15]

[15] In terms of actual carloads for all commodities interlined with DME, in 2006, KCSR received [redacted] carloads of freight from DME, representing [redacted] million in KCSR revenue. In turn, KCSR forwarded to DME [redacted] carloads worth approximately [redacted] million of KCSR revenue.

The success of the Grain Agreement and the benefits it provides to both the grain farmers and elevators served by the Corn Lines and the poultry producers who receive that grain is shared by DME as well. This is not an agreement that DME would seek to modify or cancel of its own volition. See Exhibit E, (HC DME 00075), email correspondence from Lynn A. Anderson, Senior Vice President – Marketing, Cedar American Rail holdings, Inc. and DM&E/IC&E Railroads to CP official Dave Craig (date January 14, 2008), in which [redacted]

D. CP Control Will Eliminate DME As An Independent Competitor And Neutral Railroad For Movements Of Grain To The Pacific Northwest

As noted, DM&E's acquisition of the former IMRL lines resulted in a financially stronger and relatively neutral railroad system. Indeed, over time, DME used its position as a neutral grain-originating railroad to develop two primary outlets for its grain. Grain originating on DM&E lines in South Dakota and Western Minnesota is interchanged to BNSF for movement to the PNW for export.[16] Such traffic moves pursuant to a marketing agreement that appears to be similar to the DME/KCSR agreement.[17] On the other hand, the vast majority of the grain originating on the Corn Lines is interlined with KCSR at Kansas City pursuant to the Grain Agreement. As previously discussed, this grain goes to KCSR-served receivers (feed mills serving the poultry producers) in the south-central states; many of which rely on DME grain as their primary source.

[16] See Exhibit E, Deposition of Kevin V. Schieffer ("Schieffer Dep."), transcript at 27: 7-24.

[17] KCSR is not aware of the details of the DM&E-BNSF agreement. KCSR requested production of this agreement (and others) in discovery, but CP and DME have refused to produce agreements with other railroads. KCSR has filed a motion to compel production of this agreement, as well as other information that was not provided. That motion will not be decided before March 4. As such, KCSR reserves the right to supplement the record based upon any further information provided pursuant to the motion to compel and/or address this agreement and other information as part of its rebuttal.

With respect to the DME/BNSF grain routing to PNW export markets, what is most interesting is what CP did <u>not</u> say about it in the Application, not what it did say. CP would like the Board to believe that the transaction is an end-to-end transaction, and that there will be no reduction in competition at those few points where both CP and DME serve a given station or BEA. Applicants point to two competitive studies from Mr. Williams of Woodside Consulting to reinforce that assertion. The first study examined those specific six-digit SPLC stations where the only two serving railroads are CP and DME, and determined that there will be no "2 to 1" impacts at those locations, because CP and DME do not specifically serve the same shipper at that station or actually compete at that station.[18] The second, submitted in the supplement to the application (CPR-7/DME-7), used a 50/10/10 screen to examine the *impact of the transaction on source or geographic competition.*[19] However, Mr. Williams did not study the presence of parallel competition between CP and DME in conjunction with joint-line or interline service between two common geographic points.[20] As Dr. Grimm's

[18] See Verified Statement of Mr. Williams, CP-2/DME-2. Mr. Williams' analysis is incomplete in that he only examined rail-to-rail competition at a shipper-specific level for each location. He did not examine whether a given shipper at such a location has the benefit of indirect competition between DME and CP, inasmuch as a shipper could – (1) transload its shipment to the other carrier; (2) threaten or undertake a build-in/build-out, or (3) exercise its ability to shift production between facilities located on the other railroad. See Exhibit E, Deposition of John H. Williams ("Williams Dep."), transcript at 44:9-45:22 [redacted]; 81:15-82:3; 137:16-138:9 [redacted]

[19] Mr. Williams'50/10/10 screen examined those locations where CP and DME may transport the same commodity from different origins to a common destination or where CP and DME may transport the same commodity from a common origin to a different destination. Neither this analysis nor the specific station analysis in CP-2/DME-2 analyzed those origins that are served by DME and another railroad (BNSF) to a destination that is served by CP and another railroad (say UP) between a common origin and common destination. See Exhibit E, Williams Dep. 143:9-148:5.

[20] See Exhibit E, Williams Dep. 47:19-48:10 [redacted]

attached verified statement discusses, there are parallel elements to this transaction that were not analyzed and for which Applicants have failed to meet their evidentiary burden to establish that there will not be a substantial lessening of competition in such corridors.

An example of the type of horizontal competition not addressed in either of Mr. Williams' statements can be seen in an examination of the two principal routes for export grain from the grain regions of Minnesota and Iowa to the PNW. As noted, other than the grain covered by KCSR's ratemaking authority on the Corn Lines, DME grain from these areas is interlined with BNSF for movement to Seattle, Spokane, or Portland for overseas export. In 2006, this amounted to [redacted] carloads (standard covered hopper) of DME/BNSF interlined grain. V.S. Grimm at 6. Competing with this DME/BNSF routing is a CP(Soo)/UP routing whereby CP(Soo) originates the grain in the Minneapolis/St. Paul BEA, handles the grain with CP across western Canada to Kingsgate, BC/Eastport, ID, where CP delivers it to UP for export through PNW terminals at Portland and Seattle.[21] This CP/UP routing represented [redacted] carloads (standard hopper) in 2006. Id. The DME/BNSF grain route clearly competes with the CP(Soo)/UP route for the movement of grain from the grain-gathering regions of the Midwest to the export markets of the PNW,[22] yet, neither of Mr. Williams' studies identified the impact on horizontal competition. Obviously, inserting CP into both of these routes will eliminate the independence of the two routing options.

[redacted]

[21] [redacted]% of CP(Soo) originated grain from BEA 107 is routed via a CP/UP routing for export via the PNW ports. Source: 2006 STB Carload Waybill Sample.

[22] See Exhibit E, Deposition of Ray Foot ("Foot Dep."), transcript at 41:11-42:19, 47:13-48:7; Williams Dep. 75: 8-16; 73:18-74:21.

E. CP Control Will Eliminate DME As An Independent Competitor And Neutral Railroad For Movements Of Grain To The South-Central States

There is a similar parallel element with respect to the movement of NAFTA traffic between Chicago, Kansas City, and Mexico, because CP/UP routings compete against DME/KCS routings.[23] As is discussed in a later section of KCSR's Comments, CP's control of DME will eliminate KCSR's ability to effectively compete in the Chicago-Kansas City-Laredo corridor for NAFTA traffic. However, with respect to DME/KCSR grain to KCSR-served poultry feed mills, there are no similar CP(Soo)/UP interline routings that compete directly against the DME/KCSR routings because, as noted, almost [redacted] of the CP(Soo)-originated grain is interlined to UP for PNW export markets in competition with the DME/BNSF routings. However, UP routings of Iowa-originated corn do compete against DME/KCSR routings for movements of that corn to poultry producers in the south-central states.

For corn originated from BEA 100 (Des Moines, IA-IL-MO) and BEA 107 (Minneapolis-St. Paul, MN-WI-IA),[24] UP and DME are competitors. In 2006, UP originated [redacted] carloads of corn from these two BEA's and DME originated [redacted] carloads. The main destinations (via single-line service) for UP grain originated from these two BEA's are the BEA's of Little Rock-N. Little Rock, AR, New Orleans, LA, Fayetteville-Springdale-Rodgers, AR-MO-OK, Davenport-Moline-Rock Island, IA-IL, Los Angeles-Riverside-Orange Co.-CA-AZ, San Francisco-Oakland-San Jose, CA, Portland-Salem, OR-WA, Seattle-Tacoma-Bremerton, WA. For DME-originated grain, the main BEA destinations (via single-line or in interline service with another railroad) are Seattle-Tacoma-Bremerton, WA

[23] See Exhibit E, Williams Dep., 82:20 – 83:4, 89:7-15, 90.6-9, 129:12-19; Foot Dep., 82:8-20 (also attached as Exhibit E).

[24] BEA 107 includes the Corn Lines.

(BNSF), Portland-Salem, OR-WA (BNSF), Dallas-Ft. Worth, TX-AR-OK (KCSR), Davenport-Moline-Rock Island, IA-IL (DME), Fayetteville-Springdale-Rodgers, AR-MO-OK (KCSR), Little Rock-N. Little Rock, AR (KCSR), Jackson, MS-AL-LA (KCSR), and Chicago-Gary-Kenosha, IL-IN-WI (DME). Clearly, DME and DME/BNSF routings compete against UP destinations to the PNW. Just as clearly, DME/KCSR routings compete against UP routings from the same origins to the same destinations of Fayetteville-Springdale-Rodgers, AR-MO-OK and Little Rock-N. Little Rock, AR. DME originations also provide virtually all of the grain destined to the Jackson, MS-AL-LA BEA.

With respect to the destination BEA's served by the DME/KCSR routings, the receivers of this grain (mainly corn) are feed mills which use it as poultry feedstock. Very few of these feed mills, if any, have access to more than one railroad. Most are located either on UP or on KCSR. As such, UP and DME/KCSR compete to deliver grain to their respective feed mill customers.[25] As discussed in the Verified Statement of George C. Woodward, CP's control of DME will give CP the incentive to price DME corn in (or to reduce service levels on the DME/KCSR routing) to promote the flow of DME grain to – (1) the PNW via CP(DME)/UP, CP(DME)/BNSF, or CP(single-line to Vancouver) routes to the PNW, or (2) UP-served feed mills in the south-central states via a CP(DME)-Kansas City-UP

[25] UP and KCSR well know that feed mills that do not receive transportation rates comparable to those offered to other plants in the area will be hindered in their ability to effectively market their products. If such feed mills are stifled in their ability to compete in local markets due to rail rates, then the serving carrier eventually will lose traffic to that facility. Even though either UP or KCSR is usually the only carrier so serve such a facility, neither railroad can increase its rates without regard to the possibility that its customer will lose its business to a customer served by the other carrier. This is a well-recognized economic principle in STB merger and control cases. See e.g. Union Pacific/Southern Pacific Merger, 1 S.T.B. 233, 395-96 (1996) ("UP-SP"), aff'd sub nom. Western Coal Traffic League v STB, 169 F.3d 775 (D.C. Cir. 1999).

route. To understand why this is so, it is important to understand the relationship between CP and UP.

1. UP And CP Are Close Strategic Partners

CP and UP have for nearly a decade built upon, benefited from, and touted the strength of their respective commitments to a multi-faceted strategic relationship, which they have sometimes characterized as a commercial bond just short of a merger. This CP/UP strategic relationship is most evident in three "CanAm" alliances, whereby CP and UP partner in the movement of traffic between – (1) western Canada and points in the west and southwest U.S. (extending into Mexico); (2) midwestern Canada and points in the south-central U.S. (extending into Mexico); and (3) eastern Canada/eastern U.S. and points in the south-central and western U.S. (extending into Mexico). See Canadian Pacific Railway – 2005 Corporate Profile and Fact Book at 50 and 53 and 2006 at 44. These CanAm arrangements are, for example, instrumental in the flow of such commodities as grain from CP origins to points in the U.S. PNW and to south-central U.S. markets.[26] So close is the CP/UP strategic relationship that, in 2001, John Koraleski, UP's Executive Vice President – Marketing and Sales, declared, "We are two railroads thinking of ourselves as one." "Turning a Corner," Railway Age, October 2001.[27]

The impacts of such a CP/UP alliance should not be lost on the Board, as such close inter-carrier relationships have been a point of concern in other Board proceedings. For example, the Board noted that an alliance agreement between the now-merged Canadian National Railway ("CN") and Illinois Central Railroad Company ("IC" – collectively, "CN/IC") and KCSR was an "important … agreement related to this merger, and thus it is

[26] See Exhibit E, Foot Dep. 48:14-15.

[27] Available at http://www.railwayage.com/oct01/CPail.html.

appropriate for us to scrutinize carefully all of the issues relating to it that have been raised in this proceeding," and the Board further observed that the alliance enabled the alliance partners to market their services more effectively via "service coordination among the participants." Canadian National, et al. – Control – Illinois Central, et al., 4 S.T.B. 122, 145-46 (1999) ("CN-IC").[28]

In light of the highly-developed strategic relationship between CP and UP, the Board must recognize that CP's motivations and incentives are also guided by those of UP pursuant to the CanAm alliance. CP will have a strong motivation to avoid (or frustrate the effectiveness of) the pro-competitive inter-carrier agreements forged between DME and KCSR where those agreements serve to compete against CP/UP movements to export markets such as Asia, Mexico, or to feed mills serving poultry producers in the south-central U.S.[29]

2. CP Has Strong Economic And Strategic Incentives To Eliminate DME/KCSR Routings Or Degrade Service Over Those Routes

Having so firmly cemented their strategic relationship, it is entirely likely, indeed probable, that CP and UP will act quickly following CP's acquisition of control of DME to incorporate traffic flows to and from DME's lines into existing and/or supplemental alliances with UP.[30] CP (with DME under its control) will look to adjust and augment its strategic ties

[28] The participants in the CN/IC-KCSR alliance were careful to craft an arrangement that would ensure that the alliance did not extend to points and/or corridors at which the alliance partners can or could compete. That alliance also was so structured to avoid the types of competitive harms that critics of the alliance tried to claim could flow from the arrangement. Id. at 136 ("Restrictions On The Alliance"). No such restrictions or limitations appear to have been placed upon the CP/UP CanAm arrangements.

[29] CP knows it could cause service under the Grain Agreement to suffer. See Exhibit E, Williams Dep. 103:16-20, 104: 12-21, 106: 1-17 [redacted].

[30] See Exhibit E, Schieffer Dep. 88:14-21, 90:10-15; Williams Dep. 108:5-11, 124: 15-20.

with UP and to thwart traffic flows or strategic relationships with other railroads whose services compete with those of CP/UP. Accordingly, at least during the current term of the Grain Agreement, CP would quite likely act to undermine the effectiveness of that agreement by degrading service and reducing transit times.

Indeed, while it is true that CP cannot exercise its control over DME to change KCSR's ratemaking authority for DME originated corn during the term of the DME/KCSR agreement, it certainly could increase transit times for the haulage service it would provide under the DME/KCSR agreement, and would otherwise use its control of DME to frustrate service.[31] In fact, it is precisely because of the ability of a new owner to frustrate service provided under existing ratemaking agreements that KCSR, in connection with its application to acquire control of Tex Mex, voluntarily agreed with the National Industrial Transportation League ("NITL") to specific operational measurements and reporting requirements, and further agreed that, if the operational monitoring showed service deterioration, KCSR would provide the Board with a corrective action plan. See Kansas City Southern – Control – The Kansas City Southern Railway Company, Gateway Eastern Railway Company, and The Texas Mexican Railway Company, __ S.T.B. __, STB Finance Docket No. 34342, slip op. at 19, 42-45 (STB served Nov. 29, 2004)("KCS-Tex Mex"). CP has made no such service guarantees here. Indeed, as will be discussed more below, when KCSR sought, in the course of its negotiations with DME and CP in this proceeding, to amend the existing agreement to add meaningful service penalties for failure to meet the stated transit time goals, CP and DME rejected such proposals. It is critically important that the Board not ignore such service degradation possibilities.

[31] Again, CP is well aware of its ability to so act. See Exhibit E, Williams Dep. 13:17-14:10, 101:17-102:10, 104:22-105.6.

Service issues aside, to the extent DME grain is not covered by either the DME/BNSF agreement or the Grain Agreement, CP will look to adjust DME traffic flows in order to promote its long-standing strategic relationship with UP. When the DME/BNSF agreement and Grain Agreement terminate, CP will seek to add that traffic to the CP/UP alliance by moving it to UP via the Kingsgate interchange for PNW export or to Kansas City for interchange to UP for delivery to UP-served poultry markets. Even in the absence of such a CP/UP alliance, CP will have an incentive to seek to achieve the long haul for itself and route DME-originated grain to the PNW – via either UP or BNSF. Indeed, CP's own witness, Mr. Williams, identified DME/BNSF export grain flows to the PNW as being easily divertible to a CP/UP route, and he has recommended that CP do so. See Exhibit E, Williams Dep. 50:16-53:1; Foot Dep. 41:11-42:19, 47:13-48:7, 48:24-49:4.[32]

It is not simply theory that CP will seek to divert DME grain to its long-haul routes. As George Woodward explains in his verified statement, and as confirmed by Mr. Williams' analysis, it is to CP's economic advantage to immediately seek ways to move DME-originated corn to the PNW.[33] As shown in Exhibit 7 of Mr. Woodward's verified statement, the total per carload freight charges for DME/KCSR grain were approximately [redacted]. Of those per carload receipts, DME received approximately [redacted] and KCSR received approximately [redacted] in a division of the interline revenue. For DME grain forwarded to the BNSF for export through Seattle, the charge is [redacted] per carload. For CP(Soo) originated grain forwarded to UP at Kingsgate, the approximate carload charge is [redacted]. Purely on a revenue-per-car basis, CP has every incentive to route DME grain to a CP/UP-PNW export routing as it is more profitable, on a per carload basis, to do so. V.S. Woodward

[32] Redacted portions of Mr. Williams' traffic diversion analysis is also included in Exhibit E (CPR-DME-HC001532-001543).

[33] See also Exhibit E, Foot Dep. 28:24-29:3, 29:22-25.

at 18. Mr. Woodward's statement also discusses the numerous other economic incentives that exist, and will exist in the future, that would motivate CP to route DME grain either to PNW/export or to UP-served destinations in the south-central U.S. and Gulf Coast/export.

CP's economic incentive to route grain to the PNW is further confirmed in the verified statement of Thad Jones ("V.S. Jones"). His statement discusses the interplay between transportation markets and grain prices. He notes that, currently, most of the grain going to the PNW for export originates in the upper U.S. Midwest (i.e., the Minneapolis/St. Paul BEA and the Omaha/Council Bluffs BEA) or the western Canadian provinces. However, the market is changing, and by the time the DME/KCSR contract expires, the scope of PNW/export grain sources will have expanded to the south and east into markets on the IC&E lines that are now part of DME. V.S. Jones at 14-15. Because there will be a strong demand for DME grain to move to the PNW, CP will have an economic incentive to move it via its long-haul route to the PNW, and it will have no incentive to continue to move that grain to KCSR.

The analyses of Mr. Woodward, Mr. Jones, and CP's own expert, Mr. Williams, all highlight CP's incentive to seek to price its service in to encourage flows to the PNW and away from a KCSR interchange at Kansas City. CP's public statements also confirm that focusing upon such PNW export hauls is part of their long-term economic and strategic plan. In the Ex Parte No. 665 proceeding, Ms. Judy Harrower, CP's Vice President, Marketing and Sales – Bulk, discussed CP's grain markets and routings. She noted that strong Asian demand for U.S. corn and soybeans has significantly increased the demand for rail transportation of grain to the PNW and remarked that CP had responded to that demand. She also noted that CP has invested over $40 million in additional infrastructure to accommodate

CP/UP grain routings to the PNW; expand yard capacity, purchase locomotives; and help its short line connections to upgrade their lines to handle export grain volumes.

CP's Ex Parte 665 comments hint at CP's dedication to, and strategic focus on, growing its Pacific Rim grain traffic flows. In fact, KCSR's concerns about this Transaction stemmed from its own assessment of CP's strategic focus on PNW trade flows, particularly for grain, and its possible impact on KCSR customers. [redacted] See Exhibit E, McQuade Dep. 17: 6-11. PNW export grain is very likely to be among CP's chief targets for its added capacity. As Mr. Foot observed, [redacted] See Exhibit E, Foot Dep. 28:24-29:3, 29:22-25. Given CP's level of investment, the returns these investments have yielded with respect increased PNW export grain volumes, and CP's stated strategic goal to increase commodities moving via the PNW, CP has tremendous incentive to seek ways to route DME originated corn to the PNW.

3. CP Has Shown That It Has Different Strategic Goals Than DME

The theory that CP will have different incentives and strategic plans than DME with respect to the Grain Agreement and grain routings to the south-central poultry markets is not just a theory, it has already proven itself in reality. CP has already intervened in DME-KCSR negotiations which had commenced due to KCSR's concerns about the proposed Transaction. CP's intervention clearly demonstrates that CP's goals are not the same as DME's.

Upon learning of the proposed Transaction, KCSR approached DME to discuss modifications to the terms of the existing Grain Agreement (by adding certain service standards and penalties and by extending its terms) and to the Chicago Agreement, which would take effect upon consummation of the Transaction. See V.S. Bilovesky at 12. KCSR understood that DME was entrusted under the terms of the CP-DME Agreement and Plan of Merger (dated as of September 4, 2007 – the "APM"), which has been appended to the Application, to take whatever action might be appropriate and in the best interest of DME.

Understanding that CP would not obstruct DME's negotiating an extension and/or other modification of the Corn Agreement and the Chicago Agreement, KCSR advanced proposals to DME, which DME encouraged. Specifically, to progress such negotiations, KCSR's Mr. Bilovesky contacted his counterpart at DME, Mr. Steve Milligan. Mr. Milligan advised Mr. Bilovesky that DME was willing to discuss extending and/or modifying the Grain Agreement, and welcomed proposals to modify the Chicago Agreement to make it more remunerative to DME.[34] Mr. Milligan added that, despite DME's receptiveness to a proposal for extending or replacing the Kansas City-Chicago haulage terms, DME would

[34] See Exhibit E, E-mails from Steve Milligan to Mike Bilovesky and Lynn Anderson (HC DME 00044, HC DME 00056-57).

need to consult with the Trustee for further input and guidance.[35] See V.S. Bilovesky at 12. A flurry of contact between KCSR and DME continued from late December 2007 until roughly mid February 2008, during which time the two individuals discussed the particulars of the agreements.

As constructive negotiations were taking place between DME and KCSR, KCSR expressed to CP KCSR's hope that CP would not frustrate those negotiations or otherwise undermine the process now well underway. In that vein, David C. Reeves, KCSR's Associate General Counsel, wrote to Mr. Paul A. Guthrie, Q.C., CP's Vice President – Law and General Counsel. Given the positive tone of discussions between DME and KCSR, Mr. Guthrie's response was a shock. Mr. Guthrie advised that CP was unwilling to discuss or to agree to modifications to either of the agreements, and stated that, as far as CP was concerned, discussions on the subject were over. See Guthrie Letter, V.S. Bilovesky at Appendix 1. The Guthrie Letter reflects that, in CP's more recent view, the Grain Agreement and Chicago Agreement were matters entirely within CP's discretion, and that DME had no latitude to separately explore modifying them at this time. The Guthrie Letter also evidences CP's abject reversal of opinion on whether it should have a hand in the negotiations, and its subsequent influence on DME. By letter dated February 21, 2008, Mr. Lynn Anderson, DME's Senior Vice President – Marketing, notified Mr. Bilovesky that DME was also no longer willing to discuss the Grain Agreement and Chicago Agreement with KCSR. See V.S. Bilovesky Appendix 2. Interestingly enough, in contrast to DME's constructive tone to that point, Mr. Anderson's letter mimicked the style, tone, and message of the Guthrie Letter. CP

[35] The Trustee, Mr. Richard Hamlin, is a close personal friend of Ms. Kathryn McQuade, CP's Executive Vice President and COO. They have been co-workers at two previous places of employment, KPMG and Norfolk Southern, and they spend personal vacation time together. See Exhibit E, McQuade Dep 46:22-48.4.

had obviously signaled to DME that DME's strategic plans and goals were at odds with CP's, and so DME changed course.

This turn of events suggests that CP may have exercised a form of unauthorized control over DME by pressing DME to terminate discussions on both agreements.[36] It is not entirely clear from the evidence now available to KCSR the extent to which DME and the Trustee and/or CP conferred on the subjects of the agreements, but it is clear that DME's Mr. Milligan had for some time conveyed DME's interest modifying the agreements. In fact, upon discovery, KCSR has learned that [redacted] See Exhibit E, (HC DME 00075) (Anderson-Craig email exchange). Also in that contact, [redacted]

At about the time of the Anderson-Craig exchange, it appears that CP took up the matter as within its province, and terminated the KCSR-DME dialogue by informing KCSR that CP was unwilling at that time to take further action on either agreement. There is no evidence that DME had contractually bound itself not to undertake the extension of such strategic and commercial arrangements with its partner carriers,[37] and so it is unclear how CP

[36] Pursuant to the governing statutes and Board precedent, the acquisition of control of a rail carrier by any number of rail carriers requires advance Board approval under 49 U.S.C. 11323(a)(3). Control includes the power or authority to manage, direct, superintend, restrict, regulate, govern, administer, or oversee. Colletti Control – Cornet Freight Lines, 38 I.C.C. 95, 97 (1942).

[37] The APM, appended to the Application, contains numerous limitations upon DME's

properly could have inserted itself in the process and designated for itself matters that are eminently within the realm of DME's day-to-day management. Indeed, a careful review of the APM shows that it contains an "additional agreements" section (Article VI) which purports to limit DM&E's and IC&E's respective abilities take certain actions or to obligate themselves during the term of that agreement, including, among other things, restrictions on negotiating coal transportation contracts, contracts with customers if over one year in length, and leases among DM&E and/or ICE and third-party railroads. DM&E and IC&E are not, however, expressly prohibited under Article VI of the APM from entering into new, or modifying existing, agreements with other railroads. Rather, DME is prohibited under the APM from making "any changes in the customary methods of operations... including, without limitation, practices and policies relating to purchasing, inventories, <u>marketing</u>, selling and <u>pricing, other than in the ordinary course of business consistent with past practice</u>." APM, Article VI, Section 6.01(b)(iv). The extension or modification of an existing arrangement between KCSR and DME, which DM&E's President and Chief Executive Officer, Kevin V. Schieffer has said [redacted][38] clearly is consistent with the ordinary course of DME's marketing and pricing business practices.

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ability to enter into various kinds of agreements or arrangements, but KCSR cannot find any provision that ties DME's hands in negotiating (or extending the terms of) commercial arrangements with connecting carriers. In fact, were the APM to contain such limitations upon DME's ability to act in its own self-interest, then the APM would contain clear evidence of CP's unlawful control of DME.

[38] See Exhibit E, Schieffer Dep., 52:7-53:14. Mr. Schieffer maintained at his deposition that DME was unwilling from the outset to explore an extension of the Grain Agreement beyond its current term. Mr. Schieffer was not directly and actively engaged in such KCSR-DME discussions. See Exhibit E, Schieffer Dep. 61:3-9. Mr. Bilovesky was directly involved in such discussions, and his testimony reflects that DME was receptive to the idea of such an extension. See V.S. Bilovesky at 12-14.

The evidence now available to KCSR shows that CP clearly intervened in DME's efforts to reach a negotiated settlement with KCSR notwithstanding that the APM would have allowed DME to resolve KCSR's concerns. Whether CP's intervention constituted unlawful control is not for KCSR to investigate or decide. Rather, the evidence indicates that, but for CP's intervention in DME's affairs, KCSR and DME might by now have concluded modifications to the two agreements. DME's abrupt rejection of further negotiations with KCSR following CP's clear expression of intent with respect to those agreements shows that CP's economic interests differ from DME's, and reflects that CP has no intention to maintain DME's neutrality, especially in working with KCSR to resolve service and rate concerns arose as a result of the proposed Transaction.

F. <u>Elimination Of The DME/KCSR Grain Routings Will Harm Shippers and Receivers</u>

Pursuant to the Grain Agreement, KCSR has ratemaking authority to source DME grain from the Corn Lines and other DME(IC&E) origins. On the Corn Lines alone, there are approximately 44 elevators providing grain for KCSR's 28 receivers (feed mills). As noted previously, DME-sourced grain, mainly from the Corn Lines, represents [redacted] of KCSR's total domestic grain volume. [redacted] of this DME sourced grain is moving to KCSR served feed mills in the South Central U.S. V.S. Bilovesky at 5. Every day, these feed mills seek grain at the lowest delivered cost. The delivered cost of grain is composed of two elements – the price per bushel paid at a given rail served elevator and the cost of freight from that elevator to the feed mill. The elevator and railroad that can deliver the grain at the lowest price will win the move. Id. at 6; V.S. Jones at 3-5.

KCSR receivers (feed mills/poultry producers) analyze the per-bushel price from KCSR-served grain origins and the KCSR freight rate to determine their final cost.[39] As previously discussed, KCSR really only originates grain from two main sources – the Omaha/Council Bluffs area via its ICC/STB granted rights and from Iowa and Minnesota via its agreement with DME. Thus, the KCSR served feed mills are actually competing against other potential users of the grain from these KCSR origins. For example, because Omaha/Council Bluffs is served by KCSR, UP, and BNSF, there are many potential receivers of this grain against which KCSR feed mills will bid if they seek to procure the grain from that origin. Although DME-originated corn can move to the PNW, to Mexico, to the Gulf Coast for export, or to the poultry markets in the south-central U.S., the price per bushel from the Corn Lines is lower and the delivered price to the south-central poultry markets is less than KCSR originated grain from Omaha/Council Bluffs. V.S. Bilovesky at 11; V.S. Jones at 18.[40] As a result, in 2007, KCSR handled almost 12,000 carloads on average of DME originated corn to 28 feed mills. Those cars represent almost one quarter of KCSR's total business unit's carloads. The weekly demand at those 28 feed mills is over [redacted] carloads. Id. at 5.

As has been discussed, CP's control of DME will eliminate DME's neutrality and impose CP's corporate and marketing strategies on DME traffic flow preferences. CP will naturally favor long-haul movements over its expanded network. Indeed, CP's Application touts the benefit of new single-line service to DME's shippers. Single-line service can be a pro-competitive benefit under certain circumstances, but for shippers (grain elevators) on the

[39] These receivers also examine other sources of grain that are not originated on the KCSR but which would have to be interlined to KCSR. V.S. Bilovseky at 7-8.

[40] On the flip-side, from the grain elevator's perspective, the more outlets (receivers) there are for the grain, the more bidders there are, which in turn results in a higher per-bushel price. Id. at 7-8.

Corn Lines shipping to KCSR poultry markets or even to the PNW, the transaction offers no benefit, because CP does not serve those markets in single-line service (with the exception of Vancouver, which CP itself admits is used primarily for the export of Canadian wheat).[41]

It is possible that CP could adjust its rates to move DME corn via single-line service to Vancouver. V.S. Woodward at 19. If so, CP would likely gain more revenue from such a haul, and the distance is certainly no less efficient than the DME/KCSR move to the south-central poultry markets. Id. More likely, however, is that CP, like it plans to do with the DME/BNSF export grain, will seek to move Corn Lines corn to its Kingsgate interchange with UP pursuant to the CP/UP alliance and routing protocols, so that this grain may go to export terminals in Portland and Seattle, or could be routed in CP a long-haul service to PNW export facilities served by BNSF. *Id.* at 14-18. Because the delivered price of grain is a combination of the per-bushel price at the source plus the freight rate, CP has significant ability to adjust its rates to influence the ultimate destination of Iowa/Minnesota corn.[42] Likewise, while KCSR's rates in the Grain Agreement are protected for ten more years, there are no volume or service guarantees. CP has no obligation to ship one carload pursuant to that agreement, and CP will have an incentive to downgrade service and increase transit times during that ten year period. As noted, CP has already rejected KCSR's efforts to put in service standards and penalties.

[41] Likewise, CP would not serve the Mexico markets in single-line service and would have to rely upon interline service with either UP, BNSF, or KCSR to move CP(Soo) and CP(DME) grain to those markets.

[42] The spread between the per-bushel price to the PNW and the per-bushel price to the Gulf Coast or the south-central states is significant, which gives CP significant rate flexibility so as to influence the ultimate destination. V.S. Jones at 12-13.

CP's manipulation of the freight rate to divert DME corn to a CP single-line service to Vancouver or to CP/UP or CP/BNSF interline service through Portland and Seattle,[43] while good for CP's revenues, will be detrimental to both the DME grain shippers, especially those on the Corn Lines, and KCSR served feed mills. The grain elevators on the Corn Lines could see a reduction in the number of end users as CP markets this grain for export; which could reduce (to some unknown degree) the per-bushel price. V.S. Jones at 14. KCSR served feed mills will be forced to look to other sources of grain. Of course the only other KCSR direct source is via the ICC/STB rights granted to KCSR to serve the Omaha/Council Bluffs market. Alternatively, These receivers may be able to obtain grain via a joint line move from a non-KCSR served origin. Regardless, on a delivered cost basis, corn will cost more for many of our feed mills in a post-transaction environment. V.S. Bilovesky at 11-12. Clearly, lower prices for the grain elevators and higher prices for the feed mills reflects reduced competition that the Board should prevent by imposing appropriate conditions.

II. THE TRANSACTION WILL RESULT IN REDUCED COMPETITION IN THE NAFTA CORRIDOR BETWEEN CHICAGO AND LAREDO

The Board often has often noted the importance of promoting efficient and competitive rail service in the movement of freight traffic among the United States, Canada, and Mexico under the North American Free Trade Agreement ("NAFTA"). In one of its most definitive (and prophetic) statements concerning the nexus of NAFTA trade flows and the Board's responsibilities, the Board remarked as follows:

> We are particularly sensitive to our responsibility to ensure that this [UP/SP] merger will foster the goal of North American economic integration embodied

[43] As previously discussed, to the extent the economics still favor a routing via the Kansas City gateway to south-central poultry markets, CP is likely to interchange such grain with UP, not KCSR. V.S. Woodward at 20-23. While this would maintain multiple outlets for Corn Line shippers, KCSR served feed mills would be required to obtain corn from other sources at higher prices. V.S. Bilovesky at 11.

> in NAFTA. After all, our regulatory powers are derived from the "Commerce Clause" of our nation's constitution [Article I, Section 8], which, in a very real sense, has resulted in the creation of a "free trade zone" within these United States, leading to our emergence in this century as an economic superpower.
>
> NAFTA now has the potential to contribute to the economic growth and prosperity of the United States, Mexico, and Canada. Mexico, in particular, holds great promise as a market for our agricultural and other products. As USDA explained, "under NAFTA, Mexico is expected to be an important growth market, especially for grains and oil seeds produced in the Midwest and plains states. Affordable rail rates and access to service are critical."

UP-SP, 1 S.T.B. at 421 (footnotes omitted).

Indeed, in granting Tex Mex trackage rights over UP to a connection with KCSR at Beaumont in UP-SP, the Board intended to carry out this policy in order to preserve competition for NAFTA traffic flowing through the Laredo gateway. See UP-SP, 1 S.T.B. at 421-26. Later, when KCSR acquired control of Tex Mex, the Board noted that:

> [T]he evidence demonstrates that the end-to-end configuration of the KCS/TM control transaction will benefit shippers by enabling KCS to offer expanded single-line service and to provide the benefits of efficient use of a NAFTA route connecting the Central United States with Mexico.

KCS-Tex Mex, slip op. at 17. In other transactions not involving KCSR, the Board has also noted the importance of maintaining competition for NAFTA traffic.[44] Consequently, it is a matter of Board policy that robust rail competition in the movement of NAFTA-oriented traffic is decidedly in the public interest and should be maintained.

The Board's policy in preserving competition at the Laredo gateway and for NAFTA rail trade has paid off. A large part of KCSR's market share constitutes grain from

[44] In approving the acquisition of control of the Wisconsin Central rail system by the Canadian National Railway Company ("CN"), the Board noted that the transaction would benefit shippers because it would permit CN to improve the efficiency of its "NAFTA route connecting Western Canada and the Central United States." Canadian National, et al. – Control – Wisconsin Central Transp. Corp., et al., 5 S.T.B. 890, 901 (2001) ("CN-WC").

In approving the CN/IC control transaction, the Board stated that the "merger should significantly intensify competition for the north-south traffic that has achieved greater significance due to NAFTA." CN-IC, 4 S.T.B. at 142.

Omaha/Council Bluffs and other locations served via KCSR's STB-granted rights. KCSR also transports NAFTA traffic via a Chicago – Kansas City – Laredo route in competition with CP/UP routings in that same corridor. V.S. Grimm at 8-9. Indeed, as a result of this Board's policies, KCSR is now an extremely important resource in the flow of NAFTA commerce; a fact that former Chairman Morgan, who now sits on CP's Board of Directors, had, in her prior position, noted.[45]

The Transaction proposed here by CP, however, threatens to limit NAFTA shipper options and erode competition in important NAFTA rail service corridors. In particular, as will be shown below, CP will be able to enhance its position, and the position of its chief ally in NAFTA traffic flows, UP, by undercutting the competitive position of KCSR through cancelling KCSR's ratemaking authority to Chicago or otherwise re-routing DME/KCSR flows to CP(DME)/UP routes, thereby reducing competition.

A. <u>DME And KCSR Have Worked Together To Form A Competitive Alternative To CP/UP Routings</u>

As the Board's <u>UP-SP</u> decision intended, and as CP has acknowledged in other proceedings, UP and KCSR are rigorous competitors for NAFTA rail traffic. To meet the competition KCSR faces from UP and its strategic ally, CP, in the flow of traffic between

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> [KCSR is a] historical Class I railroad situated in the Nation's heartland [which] serves a number of important markets and provides significant competitive routes and connections not only for North-South traffic but for East-West traffic as well. Indeed, as the self-styled NAFTA railway with its substantial ownership interest in the Texas Mexican Railway Company and Grupo Transportacion Ferroviaria Mexicana [now Kansas City Southern de Mexico, S.A. de C.V. – "KCSM"], as well as its control of Gateway Western …, [KCSR] is of such strategic importance that any merger between it and another Class I railroad could well trigger the next round of major rail mergers resulting in two transcontinental railroad systems.

<u>Major Railroad Consolidation Procedures</u>, 5 S.T.B. 539, 605 (2001) ("<u>Major Railroad Consolidation</u>") (separate expression of Chairman Linda Morgan).

Laredo to the important U.S. gateway of Chicago, KCSR has built a strategic relationship of its own with DME.[46] Such a relationship is central to KCSR's ability to offer a competitive counterbalance to UP's dominant status at U.S.-Mexico rail gateways.

Because of the importance of Chicago as a gateway for NAFTA traffic, and particularly in light of the CP/UP CanAm alliance, which focuses, in part, on NAFTA flows via Chicago, KCSR has in place the aforementioned Chicago Agreement, whereby DME has agreed to provide certain haulage services to KCSR between Kansas City and Chicago. In particular, through the Chicago Agreement, KCSR can offer a competitive alternative to UP single-line service between Laredo and Chicago.[47] More importantly, the Chicago Agreement represents a first step in what KCSR anticipated would become a stronger KCSR-DME alliance responsive to competition from UP and CP in NAFTA corridors. In some respects, KCSR had come to view its relationship with DME as similar to the one between

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[46] In fact, over ten years ago, when KCSR was deep into its efforts to forge its current NAFTA system, observers noted that DME's Kansas City-Chicago line could be an important northern outlet for KCSR. For example, Railway Age noted that KCSR could "reach Chicago from Kansas City, depending on agreements with the Washington Group [DME's predecessor], which is in the process of acquiring controlling interest in the former Soo Line Kansas City-Chicago line..." "Mexico's Railway Privatization: KCS Maps the 'NAFTA Railroad,'" Railway Age, January 1997 (available at http://www.encyclopedia.com/doc/1G1-19077893.html).

[47] Although not currently used, the KCSR-DME Chicago Agreement is nevertheless a competitive counterbalance to UP's Chicago-Laredo service, and thus is a beneficial influence on UP rates and services in this corridor. See, e.g., Southwest Railroad Car Parts Company v. Missouri Pacific Railroad Company, No. 40073, slip op at 3 (STB served Feb. 20, 1998) ("We consider potential, as well as actual, competition in determining whether effective alternatives exist. The question is whether an alternative is feasible, not whether it has been used in the past") (footnotes omitted); cf. Major Rail Consolidation, 5 S.T.B. at 617 (promulgating new rules requiring applicants in major and significant transactions to provide a market analysis, including the applicant's marketing plan and "existing and potential competitive alternatives")(emphasis added).

CP and UP, but CP's proposed acquisition of DME will change the competitive landscape significantly and in ways that the Applicants have neglected to discuss.[48]

B. The CP/UP Alliance Would Benefit From Undercutting KCSR's Ability To Compete For Mexico-Chicago NAFTA Traffic Flows

It should come as no surprise that CP refuses to discuss modifying the Chicago Agreement and that it has openly and publicly conveyed its views on the subject to the DME Trustee and DME management. As discussed above, CP has no incentive to promote, much less preserve, the strategic relationships that KCSR and DME have developed and that KCSR had been further developing In fact, CP, which admits to competing alongside UP for KCSR's NAFTA traffic flows,[49] has considerable incentive to deprive KCSR of effective access to the Chicago gateway and thereby secure new alliance flows with UP.[50] Thus, the foundation upon which KCSR planned to solidify and improve upon its Chicago gateway

[48] As KCSR has mentioned elsewhere in these Comments, KCSR was aware that DME felt that the Chicago Agreement did not provide it with enough revenue. DME had threatened to cancel that agreement unless KCSR was willing to change it. KCSR was amenable to such discussions and had begun pursuing with DME an expanded and modified Chicago-Kansas City haulage agreement even prior to the announcement of the CP/DME transaction. Even after the Transaction was announced, KCSR was interested in resolving DME's concerns, but unfortunately, DME abruptly terminated discussions, apparently to accommodate CP's interests. See V.S. Bilovesky at 13-14.

[49] In connection with KCSR's successful efforts to assemble a truly NAFTA-oriented system in KCS-Tex Mex, CP stressed that "nearly 90 percent of the rail traffic to and from Mexico in which [CP] participates moves via Laredo (virtually all in conjunction with UP...)," and later expressed its concern that the "NAFTA Rail system" could potentially impair the "competing services offered by [CP] and others (in conjunction with UP)" via the Laredo gateway. CP Comments in KCS-Tex Mex, filed on September 2, 2003, and CP Additional Comments in KCS-Tex Mex, filed on September 30, 2004 (emphasis added); Foot Dep. 62.24-63:12; 82:8-20; Williams Dep. 75:17-76:2.

[50] For example, because approximately [redacted] of the existing CP(Soo)-originated grain is interlined with UP at the Kingsgate gateway for PNW export, CP will likely seek to route most of the DME grain via this same routing, although CP will also have the option of moving that grain to Mexico via UP routings or to the Gulf Coast; thus effectively depriving KCSR grain consumers of access to source markets from which they have traditionally procured such grain.

access with DME would be lost post Transaction, a victim of the CP/UP alliance. KCSR anticipates that CP, out of its strategic commitments to UP, would act swiftly to cancel the existing Chicago Agreement and reject all KCSR proposals to obtain enhanced KCSR access to Chicago via the DME route on mutually beneficial terms.[51] As a result, shippers moving traffic in the Chicago-Laredo corridor would experience reduced post Transaction competition in this corridor. In short, the Transaction would enable CP and UP to affect NAFTA corridor competition by handicapping a competitor (KCSR), rather then through any competitive enhancements that would result from the Transaction.

Not only does CP have an overriding incentive to obstruct the flow of KCSR traffic to Chicago in competition with UP's NAFTA traffic to and from this gateway (by either canceling the Chicago Agreement or by severely degrading service and transit times) but CP also is likely to view capacity on DME's Kansas City – Chicago route as a means to enhance the length of CP hauls for traffic that CP currently interchanges with other carriers at Chicago and at other gateways to the north of Kansas City. In other words, where CP may get a short-haul today because it has to interchange its shipments at Chicago with other carriers, it will get a long-haul post Transaction by moving the interchange point with the other carriers to Kansas City utilizing DME's Kansas City-to-Chicago line.

[51] Although UP possesses independent rail routes between Kansas City and Chicago (via Des Moines or St. Louis), those routes are far less efficient and direct than those of BNSF, UP's largest competitor. To compensate for this weakness in UP's system, UP has (and uses) trackage rights over BNSF-owned lines between Kansas City and Chicago. Due to the close ties between CP and UP, CP's acquisition of DME would extend to UP a "friendly" route between Chicago and Kansas City that is far more direct than UP's independent routes and would not require dependence upon trackage rights over BNSF lines. It is likely that UP views the opportunity to avail itself of DME's Chicago-Kansas City route as a potential strategic benefit of the transaction and one upon which new alliance accords with CP may be struck. Conversely, CP in all likelihood views UP's interest in a more favorable and direct route between Chicago and Kansas City as a factor in negotiating future, favorable adjustments in CP/UP alliance agreements. Such circumstances would only make successful CP-KCSR haulage or trackage rights negotiations over this same line even more unlikely.

Where traffic is flowing between points on CP east of Chicago and points in the south-central and western U.S. and in Mexico (including traffic currently moving with UP pursuant to the Eastern CanAm Alliance), CP is likely to use its new DME route to Kansas City (and its newly-gained access to this interline gateway), rather than turn over traffic to other carriers at Chicago, as CP does today. Indeed, the Application touts the benefits of CP shippers gaining single-line access to the Kansas City gateway. In so extending the length of its interline traffic hauls (and its share of revenue) in conjunction with western carriers, CP doubtlessly would view KCSR haulage as an unwanted constraint on existing and/or future capacity on DME's Kansas City-Chicago route. Thus, for this reason also, it is very likely that CP would find KCSR's Kansas City-Chicago haulage as an impediment.

Unless appropriately conditioned, the Transaction will enable CP to adversely affect KCSR's ability to compete with UP and CP in NAFTA traffic flows moving between Chicago and the critically important Laredo gateway. Although there may be some efficiencies that CP and UP might gain by incorporating DME's Kansas City-Chicago line into the carriers' alliance route structure, these efficiencies will come at the expense of the shippers who currently depend upon the KCSR route to Laredo as a viable competitive alternative to UP or those shippers who have used the rate provided to them by KCSR (which rate was calculated pursuant to the Chicago Agreement) as a means to obtain concessions from UP or CP for movements via the Chicago-Kansas City-Laredo corridor. KCSR will also be harmed because it will no longer have DME as an ally in marketing service to Chicago. Where DME and KCSR had a foundation upon which aggressively to pursue mutually beneficial arrangements to enhance KCSR's NAFTA service options, CP, by virtue of its ties to UP will want no part of any arrangements that favor UP's NAFTA competitor. Thus, without appropriate conditions, NAFTA shippers moving traffic between Mexico and the Chicago gateway would experience a reduction in competition in this corridor if the transaction is approved.

III. THE PROPOSED CONDITIONS ARE NECESSARY TO PRESERVE COMPETITION AND ARE NARROWLY TAILORED

The types of competitive harm set forth above are not easily categorized within the contexts of previous merger cases. To be sure, there are elements of all types of STB-recognized harms in this case, including parallel, vertical, source, geographic, direct, and indirect competition impacts. But even though the adverse impacts of this Transaction cannot be labeled easily or conveniently, KCSR nevertheless has shown that competitive harm will result from this Transaction, and the Board should likewise recognize that the Transaction threatens harms to shippers and receivers for which remedial conditions are warranted. Having observed substantial changes in the rail industry due to the numerous rail mergers that have occurred over the past several years, the agency has concluded that each new consolidation could uniquely impact competition, and the Board has determined that the competitive harms of any further industry consolidation would be difficult to remedy.

In light of the increased challenges in reviewing and acting upon future railroad consolidations, the Board specifically has rejected the notion that conditions must be "direct and proportionate," because the agency must have the flexibility in addressing the various types of competitive harm that it might encounter.[52] The Board also recognizes that even a so-called "end-to-end" railroad consolidation (which is how Applicants prefer to describe the subject Transaction) presents the prospect for competitive harms that cannot be fixed

[52] Major Railroad Consolidation, 5 S.T.B. at 555 ("[W]e believe the carriers underestimate the difficulties we could face in attempting to remedy, in a direct and proportionate manner, losses of both direct and indirect competition ").

easily.[53] Despite the difficulty of addressing the types of harms that would occur in future transactions, including the one at issue here, the Board noted that its policy would be to "strive to remedy every competitive harm that would stem from any proposal that we decide to approve."[54] KCSR agrees with that general policy and requests the Board to undertake its best efforts to remedy the competitive harms which KCSR and its experts have identified.

A. Applicants Have Avoided Customary Competition-Preserving Commitments

In adopting its new merger rules in the Major Railroad Consolidation proceeding, the Board generally conveyed a policy preference that merger applicants offer certain standard competition-preserving conditions. This policy preference has manifested itself in a set of commitments that merger applicants in proceedings both large and small routinely have made *to substantiate their respective assertions that the subject transaction would not have* anticompetitive impacts. Generically speaking, merger applicants, post Major Railroad Consolidation, have typically committed to do the following: (1) maintain "open gateways" (to address questions of possible vertical foreclosure), (2) maintain contract commitments (under which applicants promise not to modify or cancel contracts with shippers and or other carriers), (3) adhere to a bottleneck waiver pledge, and (4) submit to periodic post-transaction reporting and Board monitoring.[55] Such commitments are commonplace even though, until now, all post Major Railroad Consolidation applications have been for transactions that were deemed "minor" under the Board's merger rules.

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[53] Id.

[54] Id. at 557.

[55] The oversight commitment could be said to be generally directed to preserve service levels on the merged rail network. If so, this is still a highly relevant consideration here, where the Applicants could target interline traffic flows with KCSR for deteriorated service so as to evade nominal commitments under the Grain Agreement.

Such routine commitments, or pledges, are usually self-imposed, but, in limited instances, one may be imposed upon the merger applicant by the Board. The very first formal rail consolidation application approved by the Board following the adoption of its new rules in Major Railroad Consolidation was Canadian National Railway's ("CN") acquisition of control of the Wisconsin Central railroad system ("CN-WC") – a minor transaction. In CN/WC, decided roughly three months after Major Railroad Consolidation, the applicants volunteered an open gateways pledge[56] and a "bottleneck waiver" pledge,[57] even though such pledges were not explicitly required under the Board's rules. In addition, CN/WC committed to be bound by transportation service contracts in specific instances where shippers had expressed concern about CN's commitment to such agreements.[58] Finally, that transaction, as approved, was subjected to Board operational monitoring and oversight, for which the applicants acknowledged there was a need.[59] The same pledges or commitments have been offered in all such formal consolidation applications involving a Class I carrier which have filed since then, including Canadian National Railway Company and Grand Trunk Corporation – Control – Duluth, Missabe & Iron Range Railway Company, Bessemer and Lake Erie Railroad Company, and The Pittsburgh & Conneaut Dock

[56] CN/WC promised not to engage in "vertical foreclosure" by closing efficient gateways, but, rather committed to "keep all existing active gateways affected by the [t]ransaction open on commercially reasonable terms." CN-WC, 5 S.T.B. at 918.

[57] CN/WC committed to waive any defenses they might otherwise have as a result of the transaction, under the Board's general rule not to regulate separately bottleneck rates, in circumstances where a shipper prior to the transaction would have been entitled to regulation of a bottleneck rate under the Board's 'contract exception' to the general rule. Id.

[58] As an example, CN gave Wisconsin Public Service Corporation ("WPS") specific written assurances that it would continue to be bound by, and would fulfill its obligations under, a contract previously negotiated between WPS and WC. Id. at 937.

[59] Id. at 909.

Company, __ S.T.B. __, STB Finance Docket No. 34424 (STB served Apr. 9, 2004); and KCS-Tex Mex.[60]

The Applicants have chosen to ignore these four competition-preserving commitments, never explaining why these commitments would be inapplicable or inappropriate here. Indeed, CP's apparent rejection of the standard commitments is especially curious because CP insisted upon such protections in CN-WC (again, involving a minor transaction)[61] and elsewhere.[62] In fact, in CN-WC, CP argued (unsuccessfully) that the applicants' "gateway pledge" did not go far enough. Here, CP does not offer any sort of gateway pledge at all, much less offer a pledge that goes further than the one offered by applicants in CN-WC. CPR's stance is puzzling. Despite the fact that all minor transactions involving a Class I carrier have, since the Major Railroad Consolidation decision, contained such standard commitments, the CPR-DME Application – involving the first and only

[60] Most recently, CN has embraced the same basic pledges in its application to acquire control of the majority of the current Elgin, Joliet & Eastern Railway Company in the ongoing proceeding in Canadian National Railway Company and Grand Trunk Corporation – Control – EJ&E West Company, STB Finance Docket No. 35087.

[61] CPR advocated rather persuasively for the universal application of the "major merger" rules in the CN-WC transaction, which argument the Board paraphrased as follows:

> CP argues that the Board's new "major merger" rules provide that, because even an essentially end-to-end merger can generate anticompetitive effects (including the elimination of product and source competition) if the merging carriers take steps to thwart the effectiveness of competing interline routes, consolidation transactions will henceforth be conditioned to ensure that major existing gateways are kept open... CP further argues, in essence, that, even though the CN/WC control transaction is not a "major merger" [it was deemed minor], the logic of the new "major merger" rules requires that the CN/WC control transaction be conditioned to ensure that major existing CP/WC gateways are kept open.

CN-WC at 938.

[62] Dakota, Minnesota & Eastern Railroad Corporation and Cedar American Rail Holdings, Inc. – Control – Iowa Chicago & Eastern Corporation, STB Finance Docket No. 34178 slip op. at 16 (STB served Feb 3, 2003).

significant transaction since then – includes none of them. Because the Transaction has been deemed significant, the Board should expect more of the Applicants here.

By excluding any of these usual commitments from the Application, CP appears to be repudiating the position it has taken at least twice previously that the "logic" of the new "major merger" rules should apply to all formal control applications, regardless of the category of the transaction. Such repudiation is patently self-serving and counterproductive. CP should not be permitted to bypass the customary commitments, nor should the Board disregard of the valid merger policy arguments that CP has made in recent minor transactions. KCSR agrees with CP's position prior to this Transaction – the policies underlying the Major Consolidation merger rules should apply equally to all merger applications. In short, the Board should view positively any application for a non-major transaction that actively adheres to the policies behind the Major Railroad Consolidation rules,[63] and eye with suspicion those, like the subject Application, that do not.

B. The Grain Agreement Should Be Made Permanent And Should Contain Service Standards And Penalties

But even if CP were to change course and offer the pledges usually made by merger applicants, such steps would not be enough to remedy the adverse impacts of the Transaction that KCSR has described in detail here. Rather, KCSR has demonstrated that grain consumers on its lines will be harmed by the Transaction unless specific remedies are imposed, and KCSR has also shown that CP would have a strong incentive post Transaction to diminish KCSR's ability to offer competition to UP in critical NAFTA traffic flows to and

[63] The Board has clearly been welcoming of non-major transactions structured to reflect the policy considerations of Major Railroad Consolidation. In the KCS-Tex Mex proceeding, for example, the Board noted with approval the five pledges that KCS had made to assure that its acquisition of Tex Mex would not result in anticompetitive impacts.

KCS-Tex Mex, slip op. at 18-19.

through the Chicago gateway. In both cases, a remedy is apparent and could be imposed within the context of existing KCSR-DME agreements. To protect KCSR-served grain receivers, the Board should condition its approval of the Transaction upon – (1) CP agreeing to make permanent the terms of the Grain Agreement, and (2) CP's further commitment to negotiate rigorous service protection provisions for the Grain Agreement to ensure against possible targeted deterioration of service for traffic handled under that agreement.

As discussed in Section I-B, above, Board precedent supports such a remedy for KCSR-served corn receivers. In particular, in UP-MP-WP, the ICC responded to competitive concerns regarding certain grain flows from the combined UP/MP/WP system, and acted to protect competition for grain traffic by imposing a permanent trackage rights remedy in favor of MKT to serve grain sources in the Omaha/Council Bluffs area, at Lincoln, NE, and at Topeka, KS. As further discussed in preceding sections of these Comments, the grain condition imposed in UP-MP-WP was so important to ensure competitive grain options that it was revisited in connection with UP's application to acquire control of MKT, and the rights originally conveyed to MKT were ultimately acquired by KCSR.

While the Grain Agreement may have roughly 10 years remaining, such a time frame is not particularly long when considered in terms of the economic commitments that KCSR must make to ensure that service under the Grain Agreement is adequate. Specifically, to support grain hauls in connection with the Grain Agreement, KCSR must commit a fleet of locomotives and covered hopper cars for the purpose of this service – equipment that has a far longer than 10-year useful life and potential for return on investment. See V.S. Woodward at 12-13. In addition, KCSR has undertaken physical plant improvements on its lines with this traffic flow in mind, and such track improvement costs may take decades to fully recoup. In light of the long-term planning and investment capital considerations that related to KCSR's provision of service in connection with the Grain Agreement, 10 years is not a long time. In the CN-WC, for example, CP requested that an existing (but unused) intermodal haulage agreement with WC be preserved for 20 years, maintaining that such a condition was thoroughly reasonable. CN-WC at 908.

Of course, the question of the appropriate term of the Grain Agreement post-Transaction is largely irrelevant if CP can, without significant penalty, cause its handling of the traffic to deteriorate to the point that the service becomes prohibitively expensive for KCSR to provide on its end, and unattractive for KCSR-customers as would be the case without appropriate contract modifications. See V.S. Woodward at 16-17, 20, 22. For this reason, the terms of the Grain Agreement should not only be extended (made permanent), but the agreement must also be revised to add adequate transit time and related service protections to deter CP from ever designing purposely to allow service to decline to levels unacceptable to KCSR and its customers. Moreover, as added security, the Board should require CP to report on its service and transit times for Grain Agreement haulage traffic as part of the Board's post Transaction oversight (or as an independent report in the unlikely event that no post Transaction operational monitoring is ordered).

The Grain Agreement condition set forth above is a narrowly-tailored remedy that fits within the basic parameters of the existing contract, and merely preserves the form and function of the haulage service upon which KCSR customers have come to depend. The requested remedy would not expand the reach of the haulage agreement, extend the Grain Agreement to other commodities, or require CP to accept less economically advantageous terms than those that DME enjoys under the Grain Agreement today. The requested Grain Agreement condition, being narrowly focused on the harms that it is designed to address, ensures needed stability for KCSR-served corn customers without imposing any significant restriction on CP post Transaction. In fact, the condition would not unduly interfere with the Applicants' implementation of the Transaction or impede Applicants' objectives in undertaking it. The condition is therefore in keeping with the Board's general expectation that a requested condition be carefully designed to address harms, and not a serve merely as a mechanism to confer a benefit upon a carrier or shipper.

C. KCSR's Haulage Access To Chicago Must Be Made Permanent

As KCSR has discussed in the preceding sections of these Comments, the Board has long recognized the important trade policy objectives of NAFTA, and its decisions in prior proceedings reflect the Board's commitment to ensuring that its actions to not impede this agreement's goal of advancing North American commerce. KCSR has described how NAFTA policy considerations, as embraced by the Board, have shaped the reach and function of KCSR's current system and how NAFTA has affected, and will affect, traffic flows accommodated by the KCSR system and by rail networks, such as the UP/CP alliance network, which competes with KCSR. Finally, KCSR has explained how a currently unused haulage agreement between itself and DME serves as an important competitive factor in the Mexico-Chicago gateway rail transportation marketplace. As KCSR has demonstrated, the elimination of the Chicago Agreement only further bolsters UP's dominance in such traffic flows and benefits CP, which is an ally in UP's NAFTA services.

To maintain a modicum of competition in the Chicago-Laredo corridor in particular, the Chicago Agreement must be preserved as a permanent constraint on UP and CP's designs to further dominate traffic in this lane. KCSR had viewed this agreement as the foundation upon which closer KCSR-DME traffic partnerships could be developed which ultimately would expand upon and make more effective KCSR's service alternatives to UP. Indeed, as these Comments reflect, KCSR had begun pursuing such expanded (and mutually advantageous) arrangements with DME, which discussions appear to now have been terminated due to CP intervention. Though currently unused, the Chicago Agreement nevertheless affects competition in the Chicago-Laredo corridor, and CP, quite naturally aware of this, would much prefer to do away with the Chicago Agreement, and bar any other agreement that might evolve from it.

KCSR has clearly established that, unlike DME, who had been receptive to developing a more comprehensive arrangement to replace or supplement the Chicago Agreement, CP will be hostile to any such arrangements and will have a vested interest in thwarting any such KSCR objectives with respect to Chicago access.[64] Accordingly, the harm to shippers that currently benefit from KCSR's role as a counterbalance to UP dominance in the Chicago-Laredo corridor is a direct result of the proposed Transaction; it would be a competitive harm that would flow directly from actions that would not likely occur if not for CP's acquisition of the DME lines.

As with the Grain Agreement, the Board should, at a minimum, grant KCSR permanent access to the Chicago gateway in order to ensure robust competition in the movement of NAFTA-oriented traffic. In addition, such a remedial condition should also require the good faith negotiation of service commitments and penalties to ensure that CP does not undermine the effectiveness of the haulage agreement purposely by providing poor service. In the event such service is not maintained, KCSR should be granted the right to

[64] The circumstances here are quite different from those in CN-WC, where CP asked for, but was denied, a Board-imposed extension of an unused haulage agreement with WC. In that case, the Board concluded that the combined CN/WC system was no more likely to cancel the agreement than WC would be acting on its own. The Board also added that the competition-preserving pledges volunteered by CN, and a related agreement with NITL also should mitigate and adequately address CP's concerns over the haulage agreement. CN-WC, 5 S.T.B. at 908. Here, KCSR has shown that CP is more likely to cancel the agreement and CP has made no competition preserving pledges.

convert this agreement to trackage rights. Negotiations over the finalization of such terms and conditions could be structured similar to those that the parties were direct to undertake in connection with the UP-MKT proceeding (regarding the terms of KCSR's permanent access to grain sources in Lincoln, Council Bluffs, and Topeka), and, more recently, in the DM&E-IC&E proceeding (concerning DME's negotiation of operating rights over a segment of line that UP owned, and that DME operated, in Owatonna, MN). KCSR is confident that, if pursued in good faith on both sides, CP and KCSR could reach a mutually acceptable arrangement to govern KCSR's haulage access to Chicago via Kansas City. But, if for some reason the parties cannot agree, then the Board should make clear that it stands ready to intervene to ensure that its condition is effectively implemented.

Just as with the Grain Agreement condition, the condition that KCSR seeks here is based upon the framework of an existing KCSR-DME agreement, and is not designed to enable KCSR to access other markets or to secure for shippers certain benefits that they do not already enjoy. Thus, the remedy that KCSR requests is not only appropriate in light of the Board's dedication to the principles of NAFTA but it is properly tailored to address specific Transaction-related harms.

CONCLUSION

As it has stated from the outset, KCSR does not object to the proposed Transaction, provided that Board approval is conditioned to protect KCSR-served grain shippers who depend upon DME grain moved pursuant to a KCSR-DME haulage agreement, and to protect NAFTA traffic flows through the Chicago gateway by preserving KCSR's haulage access from Kansas City to Chicago in keeping with the basic framework of the Chicago Agreement (described in detail above). As KCSR has shown in its Comments, and as supported by the testimony of George Woodward, Thad Jones, Michael Bilovesky, and Dr. Curtis Grimm, the Transaction would result in competitive harm if not so conditioned.

KCSR has demonstrated herein that DME is a "neutral" regional carrier, whose traffic flows are not dictated by any one particular Class I carrier's agenda. This has been good for shippers and connecting rail carriers alike, as the discussion above and attached verified statement testimony shows. As noted, DME's effective neutrality and route structure has enabled KCSR to pursue (and to continue to pursue until recently) mutually advantageous arrangements with DME that enhance KCSR's competitive position, and, more importantly, gives shippers important choices in traffic routings. Among other things, KCSR has been able to achieve a relationship with DME that strengthens KCSR's ability to provide a more effective competitive alternative to UP in NAFTA traffic lanes through the Laredo gateway. All of this will change, to the detriment of competition, if the Transaction is approved as currently proposed.

KCSR has made clear that receivers of grain on KCSR's lines depend heavily upon access to DME grain by way of KCSR service provided under the Grain Agreement (also described in detail above). Absent appropriate assurances from CP, such essential grain sources are likely to be lost to KCSR's customers, due to CP's natural preference to find other markets for this grain that allow longer CP hauls and/or promote CP's strategic alliance with UP. For similar reasons, CP will have every motivation to abolish KCSR's haulage rights access to Chicago via Kansas City, as such access does not comport with CP's participation in a competitive traffic routing that would compete directly with KCSR's service in the same corridor.

As KCSR has made clear, the conditions it seeks are directly tied to the demonstrated harms, are proportional to the anticompetitive impact, and are narrowly tailored to conform to the framework of the KCSR-DME contracts that KCSR is seeking to preserve. For these reasons, it is imperative that the Board adhere to the principles of the Major Railroad Consolidation decision ins this, the first "significant" transaction to be considered in the "modern era" of railroad consolidations, and in so doing impose the conditions that KCSR requests.

Respectfully submitted,

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Dated: March 4, 2008

CERTIFICATE OF SERVICE

I have this day served a copy of the foregoing Comments And Requests For Conditions Of The Kansas City Southern Railway Company's upon all parties of record by depositing a copy in the U.S. mail in a properly addressed envelope with adequate first-class postage thereon prepaid, or by other, more expeditious means.

Dated: March 4, 2008

William A. Mullins

Attorney for The Kansas City Southern
Railway Company

**BEFORE THE
SURFACE TRANSPORTATION BOARD**

FINANCE DOCKET. NO. 35081

CANADIAN PACIFIC RAILWAY COMPANY, ET AL.

– CONTROL –

DAKOTA, MINNESOTA & EASTERN RAILROAD CORP., ET AL.

COMMENTS OF THE KANSAS CITY SOUTHERN RAILWAY COMPANY AND REQUEST FOR CONDITIONS

EXHIBIT A

VERIFIED STATEMENT OF MICHAEL R. BILOVESKY

**BEFORE THE
SURFACE TRANSPORTATION BOARD**

FINANCE DOCKET. NO. 35081

CANADIAN PACIFIC RAILWAY COMPANY, ET AL.

– CONTROL –

DAKOTA, MINNESOTA & EASTERN RAILROAD CORP., ET AL.

COMMENTS OF THE KANSAS CITY SOUTHERN RAILWAY COMPANY AND REQUEST FOR CONDITIONS

VERIFIED STATEMENT OF MICHAEL R. BILOVESKY

My name is Michael R. Bilovesky. I am Vice President, Sales and Marketing-Agriculture and Minerals Business Unit of The Kansas City Southern Railway Company ("KCSR"). The Ag & Minerals Business Unit represents 22% of KCSR's total revenue and 14% of the total carloads. Grain is the largest segment of the business unit and it represents over half of the revenue for the business unit (56%) and 48% of the carloads. Domestic grain, in particular, is the largest carload segment of the business unit.

My business mailing address is P.O. Box 219335, Kansas City, MO 64121-9335. I have been employed by KCSR for 15 years. Prior to that, I was employed by SooLine/CPR Rail. In total, I have spent 28 years of my career working in the rail industry with the last 21 years in the field of grain transportation.

The purpose of my statement is two-fold: (1) To address the likely effects of the proposed Transaction on both the grain elevators and feed mills who currently utilize an IC&E/KCSR grain agreement to ship grain from IC&E origins to KCSR-served feed mills that provide feed to the poultry markets in the south-central United States; and (2) to address the negotiations that have occurred between DME, CPR, and KCSR to resolve KCSR's concerns with the Transaction.[1]

I. THE TRANSACTION WILL ADVERSELY IMPACT SUPPLIERS AND BUYERS OF IC&E GRAIN DESTINED TO KCSR-SERVED CUSTOMERS

A. The Sources Of KCSR Originated Grain

Prior to 1988, KCSR directly served two grain elevators located in Kansas City. There were four other grain elevators in Kansas City that KCSR could access through reciprocal switch charges. The feed mills that KCSR served were almost totally reliant on carriers other than KCSR to originate their shipments of corn, either directly or through reciprocal switching. At that time KCSR served a total of 19 feed mills located in Texas, Oklahoma, Missouri, Kansas, Arkansas, and Louisiana.

Over the next ten years, beginning in 1988, KCSR's ability to provide direct service to grain suppliers and grain consumers grew dramatically. In 1988, as a condition to the merger of Union Pacific ("UP") and the Missouri-Kansas-Texas Railroad ("KATY"), KCSR was awarded rights to serve the origins of Atchison, KS, Topeka, KS, Omaha, NE/Council Bluffs, IA, and Lincoln, NE. That opened up 14 grain elevators north of Kansas City that KCSR could access through haulage fees and reciprocal switch charges, increasing the number of grain origins open to KCSR by 350%.

[1] I will refer to DM&E and IC&E, collectively, as "DME." All of the DME originated grain comes from IC&E origins.

In 1993, KCSR gained access to a number of additional feed mills and more grain elevators through its acquisition of the MidSouth companies. That acquisition added an additional 13 feed mills to our system and seven grain elevators, bringing our total feed mills to 32, adding additional demand for corn, but also adding additional sources as well.

In 1996, KCSR acquired the Gateway Western Railway Company ("GWWR"). That acquisition added ten grain elevators to our system. At the time of that acquisition there was only one grain elevator on the GWWR system that was capable of loading 25-car units. All other facilities were small country elevators with limited loading capacity. Shortly after KCSR's acquisition of GWWR, a 100-car shuttle train origination elevator/facility was built in Slater, MO. We were also able to upgrade other elevator facilities to load a minimum of 25 cars.

Notwithstanding the expanded capacity of our elevators and the added origination points gained through ICC conditions and the GWWR and MidSouth transactions, KCSR struggled to originate enough corn to keep the feed mills that we served fully supplied. KCSR simply could not supply enough corn. Between 2000 and 2005, four feed mills on our system closed. One, Simmons Industries, which closed its facility in Anderson, MO on KCSR in late 2000, built a new feed mill in Fairland, OK on the BNSF to replace their KCSR facility.

In 1997 KCSR entered into an agreement with I&M Rail Link, L.L.C. ("IMRL," now Iowa, Chicago & Eastern – "IC&E"). That agreement was a renewable one year agreement that gave KCSR the ability to publish tariff rates or write contracts for movements where the routing contained either KCSR or GWWR and IMRL. That agreement opened up 44 country elevators located in Iowa and Minnesota, on what is known as the Corn Lines,[2] as sources of grain

[2] The Corn Lines are generally those two former Soo, then IMRL, now IC&E grain-gathering lines in Iowa and Minnesota. One is an east-west line from Jackson to Ramsey in Minnesota. The other is an east-west line from Sheldon, through Mason City, to Marquette in Iowa.

origination to serve feed mills on the KCSR system. Eighteen of these 44 elevators were located in Minnesota and 26 in Iowa.

In 2002, that agreement was amended to expand its scope, add transit time objectives, make other changes, and to extend the term until December 31, 2017. The agreement has no volume commitments and lists transit times as objectives and goals, but the service guarantees are fairly loose, and the penalties for failing to meet the stated transit times are almost non-existent. .

B. KCSR's Relationship With IC&E

As a direct result of the agreement with IMRL, in 2006, KCSR received 15,014 cars from the DME origins. Ninety-nine percent of that - 14,898 carloads - moved in domestic grain service to the south-central states.

KCSR treats the DME origins as our own, supplying the covered hoppers for loading and publishing rates for shipments originating at those points in our KCS 4032 tariff. The agreement allows KCSR to price shipments from origins on DME, fixes the amount DME will be paid for certain movements, and provides for KCSR to absorb car hire responsibility on cars it provides for use under the agreement.

KCSR's total domestic grain business from all origins, including Council Bluffs/Omaha, was 41,509 carloads. As such, traffic originating on DME lines constitutes over 36% of KCSR's total domestic grain volume. Considering origins on DME as a single source makes DME the single largest source of grain to serve domestic feed mills on the KCSR system. Omaha/Council Bluffs is our number two origination point for grain to domestic or export destinations, but almost [redacted] of the grain that KCSR originates in Omaha/Council Bluffs ends up in markets in Mexico.

Today, KCSR serves directly, or through our short-line partners, 28 feed mills in the states of Kansas, Arkansas, Oklahoma, Texas, Louisiana, Mississippi, and Alabama. We normally handle close to 40,000 carloads of corn annually to those feed mills. Those shipments represent about one fourth of the Ag & Minerals Business Unit's total carloads. The weekly demand at those 28 feed mills is over 1100 carloads.

KCSR now originates corn that potentially could go to feed mills in the south-central U.S. from 91 grain elevators, which includes our access at Omaha/Council Bluffs. Of the 91 elevators, nearly half - 44 - are located on the lines of DME. Twenty-one of the remaining elevators are located directly on KCSR lines, where we do not have to pay any additional reciprocal switch charges, haulage fees, or divisions of revenue to other carriers. Those 21 elevators have total track capacity to load 520 cars of grain at one time, less than half of the weekly requirements of feed mills on our system. Seven of those twenty-one facilities are located in Louisiana and Mississippi and almost exclusively serve feed mills in that area. Of the remaining 26 elevators, KCSR serves these via its haulage rights to Omaha/Council Bluffs.

Even though 99% of the corn that KCSR originates from the Corn Lines pursuant to its grain agreement is delivered to our feed mills in the south-central U.S., this source still does not provide enough corn to meet the demand. To meet this demand, we must also provide corn from other origins not directly served by KCSR and must rely on our haulage rights access gained in 1988 or on agreements to reach origins on other carriers. At Omaha/Council Bluffs, we compete directly against UP for corn originations from that point to many of the same general destinations served by KCSR (Mexico and the poultry markets in the south-central U.S.), but we have to pay

UP an $85 per car switch fee plus haulage charges.[3] In Kansas City, we must pay the UP a $400 per car reciprocal switch charge to originate grain from one of their local elevators. Thus, in trying to compete with UP on grain shipments originating in Kansas City, we start out at a $400 per car (11 cents per bushel) disadvantage. Similarly, we pay UP a switch charge of $85 per car, on top of the applicable haulage fee for grain, at originations at Atchison, Topeka, and Lincoln. While we have been able to compete for grain origination under these conditions, the grain originated from these locations, and others, is generally more expensive than DME sourced grain. That is why the DME originated grain has become the primary source of grain for our feed mills in Kansas, Oklahoma, and Arkansas, and why it is so important to our customers.

C. The Impact Of The Transaction On The IC&E/KCSR Grain Business

Unlike many other commodities that railroads handle, the grain business is a true market-driven business based solely on supply and demand and ultimately price. There will be times that outside factors can influence movements. If those factors remain constant over an extended period, the market will react and correct for that outside factor. An example of this would be when the recent hurricanes hit the Gulf Coast. The lowest priced option at the time moved grain to that area first, even though that option historically would not have moved grain into that area under normal market conditions.

Price is the main factor in the movement of grain. That price is composed of two parts: the price of the grain at the origin and the transportation cost to get the grain from origin to destination. What seems like a small increase or decrease in a per-bushel price makes a large difference in the overall price of the product because of the huge volumes of grain that are

[3] UP competes directly with KCSR at Omaha/Council Bluffs and other locations. While UP doesn't directly serve the Corn Lines, UP does serve other elevators and sources nearby, and delivers that corn to feed mills in many of the same destinations served by KCSR, feed mills that compete against KCSR served feed mills.

moved. For example, as mentioned above, KCSR-served feed mills need in excess of 1100 carloads of corn a week to operate. There are 3,500 bushels of corn loaded in a standard covered hopper car. That equates to a demand of 3,850,000 bushels of corn per week at KCSR-served feed mills. In November 2007, corn was selling at $3.82/bu. Today it is selling for $5 38/bu. That alone is costing the KCSR-served feed mills $6 million *per week* in added costs. In addition to the per-bushel price, transportation costs must be added to determine the ultimate delivered price to the buyer of the grain.

In the context of rail mergers and takeovers, to the extent a transaction can increase the number of destination markets a grain elevator can reach, there may be a net benefit to the elevator.[4] But if a consolidation in any way limits the elevator's choice of destination by closing or impeding service to existing gateways or routings, encouraging diversions to different markets, a consolidation can result in a reduction of markets, a reduction in demand and a net negative to the elevator. In this respect, what may be profitable to the consolidating carriers, such as increasing the length of haul on their lines to the detriment of other connecting carriers, may not be good for the elevators.

From the feed mill side, the actual user and buyer of the grain, the more sources they have to choose from for purchasing corn, the better chance they have of finding a lower delivered price. For a poultry company, which uses the corn bought by the feed mill, corn in Iowa is the same as corn in Illinois or any other state. If the per bushel price plus freight (i.e., the delivered price) is lower from Iowa than from Illinois, or vice versa, the origin offering the lowest delivered price wins the business. A rail consolidation can expand the scope of sources

[4] Supply and demand-driven price changes affect each specific grain elevator. The more destinations that an elevator's corn can reach economically, the greater the chance that the elevator can charge more for its product. More demand means a higher selling price to the origin elevator, and a higher cost to the consumer.

for that buyer, but likewise, a transaction can limit the choices by closing or impairing access to existing sources of grain. A consolidation can be a net negative if a grain buyer's traditional sources are no longer available and it is forced to obtain grain from other sources at higher prices.

While price is the ultimate deciding factor on where a feed mill will buy their grain, service is also a key important factor. If a rail consolidation reduces service, even if there is no change in rates, there can still be a negative impact. The feed mill must produce feed. Without ingredients (corn being the major one), the feed mill is forced to cease operation until the corn arrives. In most instances a feed mill will purchase higher-priced corn delivered by truck to remain operational, rather than shutting down. The ultimate delivered price of corn to the feed mill is thereby *significantly* increased by *adding to the normal cost of grain and rail* transportation the extremely high price of trucking corn on short notice to keep the feed mill operational. When you take into account the added cost factor of trucking the corn, the feed mill will change origination source if service interruptions or unreliability continues. The new source may not have previously been the lowest priced option, but when you have to add in the service failure price of high cost trucking, a new source with greater service reliability becomes the lowest price option. The bottom line is that the poor service forced the feed mill to purchase higher priced corn.

Today, for our feed mills in Kansas, Arkansas, and Oklahoma, the Corn Lines grain represents the primary source of grain.[5] CPR's proposed acquisition of DM&E/IC&E will change these dynamics. Indeed, when CPR owned the IC&E Corn Lines previously, CP did not originate any corn that terminated at our feed mills. KCSR is concerned that return of CPR

[5] Our feed mills in Mississippi also receive DME originated corn but such corn is not their primary source of corn.

ownership will again alter the current marketplace dynamics to be more like they were when CPR owned the Corn Lines before CPR will have every incentive to route IC&E originated corn to other destinations.

CPR will have more incentive to target its resources to generating a long haul on CPR than it will to fostering a short haul on CPR coupled to a movement on KCSR. CPR can make more money on its own long hauls by encouraging movement of DME grain to other CPR or UP destinations than by collecting revenue for moving the grain to KCSR. Although our agreement with DME will protect the rail rate structure for another ten years, that agreement has no volume guarantees, and the penalties connected to violating the service standards are extremely weak. Thus, CPR can develop policies to ensure that no volume moves pursuant to that agreement so as to encourage movements to CPR.

CPR can also downgrade service and allow transit times to increase during the remaining term of the agreement because the down side of failing to maintain service standards under the KCSR-IMRL 2002 agreement (i.e., the penalty for service failure) is minimal. Indeed, as I will discuss later, when KCSR suggested, as part of its negotiations related to this proceeding, that the agreement be modified to include service standards and penalties, as well as be extended, DME rejected our efforts outright on almost identical grounds to those earlier articulated by CPR's general counsel. That rejection indicates to me that CPR wants to minimize the risk to it of failing to comply with service standards in the KCSR-IMRL 2002 agreement.

CPR ownership will create different financial considerations than now exist in routing shipments from current IC&E origins. Those financial considerations are not likely to favor maintaining access to KCSR-served feed mills in the south-central United States. As it stands now, IC&E has no direct economic interest in what carrier handles its traffic once that traffic leaves its lines; that is, IC&E is effectively neutral with respect to its connections. As pointed out in the U.S. Department of Agriculture's February 28 comments in this proceeding, DME is the only regional railroad having interchanges to all seven U.S. major railroads Under CPR ownership, however, IC&E's neutrality disappears. CPR/IC&E's goal is to bring as much revenue as possible to the consolidated system so as to cover more of CPR's fixed costs. They will do this, among other means, by encouraging long-haul routings and focusing available assets on movements via the CPR system to the Pacific Northwest.

Access to the PNW for Corn Line elevators may be good for the grain elevators if it provides them with an additional market, assuming of course that CPR does not change other market conditions in order to drive grain shipments away from current destinations. But as I've noted, because CPR's policy will be to encourage long-haul movements to the export markets in the PNW, it is unlikely that CPR will price its rail rates so as to encourage routings to Kansas City. Thus, simply replacing one destination (the PNW), while closing, de-emphasizing or impairing access to existing destinations, would not be a net benefit for the grain elevators on the IC&E lines.

Nonetheless, even assuming that the acquisition of IC&E by CPR opens up new markets to grain elevators on IC&E and assuming CPR does not foreclose current routings to KCSR, the Transaction will still result in harms to the *buyers* of the Corn Lines grain. Those buyers will now be competing against additional buyers for this same corn, driving up the prices for grain. Either the feed mills will lose their access to IC&E grain because it is diverted to PNW destinations, or the price of grain from those origins will go up due to increased demand. Either way, the feed mills will be negatively impacted; having to pay more for the same product.

If, as I expect, CPR diverts IC&E-originated corn to new destinations, those bushels will not be available to move to KCSR destinations, forcing KCSR-served feed mills to fill that void through other sources of grain. Such alternative sources are available, such as Omaha/Council Bluffs, Illinois, or Indiana, but on a delivered cost basis to our feed mills in Kansas, Oklahoma, and Arkansas, such grain will be more expensive.[6] Furthermore, over the past few years, KCSR has *averaged* over 12,000 carloads of corn that originated on the DME and terminated at feed mills that we serve. If those additional 12,000 carloads (42,000,000 bushels) of corn are shifted from DME origins to another source, such as Omaha/Council Bluffs,[7] the price of corn will rise there.

If corn from the Corn Lines is routed to other CP or UP destinations, KCSR served feed mills will need to buy their corn from Omaha/Council Bluffs or other sources, where the delivered cost basis is already higher than DME originated corn for a substantial number of our feed mills.[8] For these feed mills, grain sourced from Omaha/Council Bluffs will cost more than what the feed mills pay today for DME originated corn, and while other sources of grain are also available, such as Illinois and Indiana corn, those sources are likewise generally more expensive today on a delivered cost basis than DME/KCSR originated corn.

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[6] Indeed, today, most of our feed mills do receive some corn from these alternative sources. However, for our feed mills in Kansas, Arkansas, and Oklahoma, the primary source or corn is from the DME origins, which means it is the lowest cost corn on a delivered price basis when compared to all other sources.

[7] Almost [redacted] of the KCSR sourced corn from Omaha/Council Bluffs is already going to Mexico, and on a delivered price basis to the south-central markets, is already more expensive, on average, than IC&E/KCSR sourced corn.

[8] If all of the corn demand shifted to Omaha/Council Bluffs, that itself would add substantial demand for corn at that location, raising the price. Our Mexican customers, who already are sourced via Omaha/Council Bluffs originations, would be faced with higher-priced corn. These price increases, on top of the already increased prices resulting from the overall increase in market demand for corn, despite record production, will make our customers less competitive in the overall marketplace.

As I stated earlier, grain trades solely on price - lowest delivered price on the destination side and highest paid price on the origin side. The fact that KCSR-served feed mills are today consistently buying DME originated corn shows that is their lowest priced option An unconditioned Transaction, however, will increase the delivered cost of corn for KCSR-served feed mills in the south-central United States.

II. KCSR'S EFFORTS TO DISCUSS ITS CONCERNS WITH DME AND CPR

My belief that CPR will have different incentives and strategic plans than DME with respect to the IC&E/KCSR agreement and will seek to change DME's existing policy of working smoothly with KCSR is not just a theory, but has already proven itself in reality. Upon learning of the proposed transaction, I was asked to approach DME to determine if DME would be willing, upon consummation of the transaction, to modify the terms of the existing IC&E/KCSR grain agreement by adding certain service standards and penalties and to extend its term. KCSR was also interested in discussing modifications to an agreement that KCSR has with IC&E that provides KCSR with ratemaking authority to Chicago. I made this contact on the understanding that DME remained independent of CPR during the STB's processing of the Transaction, and would be entrusted to make whatever decisions might be appropriate as between DME and KCSR.

I contacted my counterpart on the DME, Mr. Steve Milligan. Mr. Milligan advised me that DME was amenable to discussing an extension and modification of the grain agreement and welcomed any ideas regarding modifying the Chicago Agreement so as to make it more remunerative to DME. Mr. Milligan added that, any long term agreement would need to go to the Trustee for final approval.

Discussions between KCSR and DME continued from late December 2007 until roughly mid February 2008. At the time, I believed those discussions were constructive. During this time, others in KCSR management were asked to respond to inquiries from CPR about KCSR's concerns. What followed was a letter from David C. Reeves, KCSR's Associate General Counsel, to Mr. Paul A. Guthrie, Q.C., CP's Vice President – Law and General Counsel. Given the positive tone between DME and KCSR, it was a surprise to me when Mr. Guthrie advised, via reply letter dated January 29, that CPR was unwilling to discuss or to agree to modifications to KCSR's agreements with DME, not because such matters were between KCSR, DME, and the Trustee, but rather because CPR saw no need for any modifications or changes to the agreements.

Notwithstanding CPR's rejections, it was my belief that DME might still be open to negotiation. I and others sought to continue such discussion with DME. KCSR sought to extend the current grain agreement indefinitely. We also had a concern that the current transit penalties needed to be modified to address our concerns of the possibility of deteriorated service. DME originally told us that they would not agree to anything that would extend the agreement indefinitely. In the end, we were told that if we changed the term to expire twenty-five years from the current agreement they would take it to the Trustee. Again, we were told that we could negotiate a long term agreement but that the Trustee would ultimately have to approve the agreement.

Mr. Guthrie's letter to Mr. Reeves was put into the public record at the STB on February 14. By including the letter in its February 14 filing, CPR had obviously clearly signaled to DME that its strategic plans and goals were different than those of DME and that CPR had no desire to reach any agreement with KCSR. By letter dated February 21, 2008 by Mr. Lynn Anderson, DME's Senior Vice President - Marketing to me, I was advised that DME was no longer willing to continue discussions with KCSR. Interestingly enough, in contrast to their earlier position and constructive tone, Mr. Anderson's letter mimicked Mr. Guthrie's position that DME had no desire for further discussions. DME had obviously gotten the message.

In my opinion, but for CP's intervention in DME's affairs, KCSR and DME might by now have concluded modifications to the two agreements. Mr. Anderson's letter practically mirrors Mr. Guthrie's letter to Mr. Reeves. Both urge that it is premature to talk about changes to the 2002 agreement given that "there are too many variables that could come into play in the future" or in light of "facts that might be highly relevant to such renegotiations in 10 years." Both took the position that our agreement with IC&E regarding access to Chicago had been *utilized little or not at all, 'so why change it?" My overall impression of reading the two letters* (both of which are attached hereto) was that they were almost identical in tone and substance, and represented a sharp turn away from the constructive discussions I had with other DME personnel with whom I have dealt on business matters over a number of years. The similarity of the two letters and the fact that Mr. Anderson's letter departed so dramatically from my prior discussions with his subordinates and followed the lines of CPR's letter, reinforces my concerns that CPR's reacquisition of the Corn Lines will impair access for KCSR's customers to IC&E-originated grain.

CANADIAN PACIFIC RAILWAY

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January 29, 2008

Mr. David C. Reeves
Associate General Counsel
The Kansas City Southern Railway Company
P. O. Box 219335
Kansas City, MO 64121-9335

David·

Thank you for your letter dated January 25, 2008 setting out your client's position vis-à-vis CP's proposed acquisition of the Dakota Minnesota & Eastern Railroad Corp ("DM&E") and its affiliate Iowa, Chicago & Eastern Railroad Corporation ("ICE"). While CP is always interested in exploring cooperative arrangements with our interline partners, we are not, at this time, agreeable to extending or modifying the two existing KCS-ICE agreements referenced in your letter. Candidly, we are somewhat confused as to why your client believes that this is an appropriate time to address these issues. As you know, CP does not yet have authority to control ICE, or to enter into agreements that bind ICE contractually. Moreover, while CP has some understanding of the nature of the agreements between your client and ICE, we do not have access to certain details of those agreements, including their history and the possible commercial implications of your client's requests for ICE.

We understand that the agreement described in your letter as the "grain agreement" has an initial term that runs until December 31, 2017 and will automatically renew thereafter for one-year terms unless it is terminated in writing by either party Given these facts, why is it necessary even to consider a further extension of this agreement at this nascent stage? Assuming the STB approves the proposed transaction, CP will discuss renewal of this agreement on such terms and conditions as are appropriate at a time closer to the expiration of the initial term At this time, neither party can possibly be aware of facts that might be highly relevant to such renegotiations 10 years from now. In any event, we do not believe that it would be prudent to commit ICE (or CP) to an essentially permanent (99 year) agreement as your letter requests

We further understand that the other agreement described in your letter – the "Kansas City-Chicago agreement" – is, in essence, a one-year haulage agreement that contains an "evergreen" renewal provision. We also understand that little (if any) traffic has moved under this agreement in the years since ICE acquired the Kansas City-Chicago line from IMRL. For the same reasons discussed above in connection with the "grain agreement," CP is not willing at this time to enter into discussions regarding modification or expansion of an essentially dormant agreement between KCS and ICE.

With all due respect, we do not see how the proposed transaction implicates either of these agreements Both are pre-existing voluntary arrangements between KCS and ICE. We do not believe that the STB can or will, as a condition upon its approval of the proposed transaction, require CP (or ICE) to renegotiate or to extend indefinitely commercial arrangements that were negotiated on a voluntary basis between sophisticated parties. Nor do we agree with your suggestion that the proposed transaction can in any way be characterized as "major" in nature, or that the STB will require the applicants to comply with the vague provisions regarding "enhanced competition" set forth in the Board's rules governing "major" transactions.

As always, we look forward to continuing our commercial relationship with your client to our mutual benefit and the benefit of the industry as a whole.

Yours truly,

Paul Guthrie
Vice-President, Law & General Counsel

DM&E
Dakota, Minnesota & Eastern Railroad Corporation

Cedar American Rail Holdings, Inc.

IC&E
Iowa, Chicago & Eastern Railroad Corporation

Lynn A. Anderson
Senior Vice President - Marketing

February 21, 2008

Mr. Michael R. Bilovesky, Vice President – Marketing and Sales
Kansas City Southern
P.O. Box 219335
Kansas City, MO 64121-9335.

Dear Mike,

This is in response to your requests to ICE for extension and modification of the KCS and IMRL Divisions and Equipment Agreement, dated July 18, 2002, pertaining to grain movements from ICE origins to KCS destinations, as well as extension and modification of the May 20, 1997 IMRL-KCS Marketing Agreement, containing haulage provisions between KCS at Kansas City, MO and points on and beyond the IMRL system,

First, the KCS-IMRL Divisions and Equipment Agreement is currently scheduled to expire December 31, 2017. We believe the provisions of this Agreement have been very beneficial to our railroads, as well as our customers, and feel they should continue to be beneficial for the foreseeable future. However, it is nearly impossible to anticipate what market and economic conditions will be, beginning ten years from now, in 2018. It seems that the prudent approach for both of us would be to not change the terms of the existing Agreement at this point in time, but wait until we approach the current expiration date and then determine what course of action makes the most sense for both of our companies. There are just too many variables that could come into play in the future and affect the economics of these movements, and which could have a significant impact on this Agreement for both parties. Accordingly, we choose to not extend the Agreement at this time, but will certainly consider it at some point in the future when many of these variables begin to crystallize for both parties.

Second, on the IMRL-KCS Marketing Agreement, this Agreement was entered into in 1997 by IMRL and subsequently adopted by ICE at its startup in 2002. This Marketing Agreement has not been utilized since it has been in existence, and ICE does not feel its terms and conditions are favorable to its financial performance. ICE continues to handle large volumes of carload business with KCS under normal railroad rate and division negotiation methodology with KCS and believes this is the appropriate method for developing acceptable freight rates and divisions between the parties.

ICE is willing to consider haulage arrangements on specific movements and in specific corridors with KCS, however, it is not willing to provide and expand unlimited authority to KCS to price over its system to the detriment of ICE's existing business. Each movement needs to be considered on its own merits. Further, for your information the Trackage Rights Agreement ICE has with CP for movement of its trains between La Crescent, MN and St. Paul, MN contains a provision prohibiting ICE from providing haulage for another rail carrier. Thus, ICE is not able to even consider haulage in this corridor.

Finally, your request to us was made at a time when CP is seeking authority to acquire control of DME/ICE. The STB is scheduled to rule on this application in September. That KCS has indicated to CP that resolution of your issues would cause KCS to not oppose the transaction is not a sufficient reason for ICE to extend these agreements now.

Mike, ICE values its relationship with KCS and sees no reason to alter its arrangements for doing business with your company. As new potential movements are identified and developed, please contact us and we will do all reasonably possible to work with you to capture these new opportunities.

Sincerely,

Lynn A. Anderson
Senior Vice President - Marketing

VERIFICATION

I, Michael Bilovesky, declare under penalty of perjury that the foregoing statement is true and correct. Further, I certify that I am qualified to file this Verified Statement. Executed this 3rd day of March, 2008.

Michael Bilovesky

V.S. Grimm
Public Version

BEFORE THE
SURFACE TRANSPORTATION BOARD

FINANCE DOCKET. NO. 35081

CANADIAN PACIFIC RAILWAY COMPANY, ET AL.

– CONTROL –

DAKOTA, MINNESOTA & EASTERN RAILROAD CORP., ET AL.

COMMENTS OF THE KANSAS CITY SOUTHERN RAILWAY COMPANY AND REQUEST FOR CONDITIONS

EXHIBIT B

VERIFIED STATEMENT OF CURTIS M. GRIMM

**BEFORE THE
SURFACE TRANSPORTATION BOARD**

FINANCE DOCKET. NO. 35081

**CANADIAN PACIFIC RAILWAY COMPANY, ET AL.
– CONTROL –
DAKOTA, MINNESOTA & EASTERN RAILROAD CORP., ET AL.**

**COMMENTS OF THE KANSAS CITY SOUTHERN RAILWAY COMPANY AND
REQUEST FOR CONDITIONS**

VERIFIED STATEMENT OF CURTIS M. GRIMM

I. Introduction

My name is Curtis M. Grimm, and I am Dean's Professor of Supply Chain and Strategy, Robert H. Smith School of Business, University of Maryland at College Park. I have been a member of this College since 1983. I received my B.A. in economics from the University of Wisconsin-Madison in 1975 and my Ph.D. in economics from the University of California-Berkeley in 1983. My Ph.D. dissertation investigated competitive impacts of railroad mergers.

In my background, I have extensively addressed public policy issues regarding transportation, including those examined in Interstate Commerce Commission ("ICC") and Surface Transportation Board ("STB") merger and control proceedings. I have previously been employed by the Wisconsin Department of Transportation, the United States Interstate Commerce Commission, and the Australian Bureau of Transport and Communication, and I have provided consulting services to several other government agencies and private firms regarding transportation issues.

My research has involved deregulation, competition policy, competitive interaction and management strategy, with a strong focus on transportation. This research has resulted in over 80 publications, including articles in leading journals such as *Journal of Law and Economics, Transportation Research, Transportation Journal, Logistics and Transportation Review, Academy of Management Journal, Management Science, Strategic Management Journal, and Journal of Management*. More than two dozen publications have dealt specifically with the railroad industry, focusing mainly on deregulation, mergers, and competition issues. I have also co-authored four books or monographs. Further details may be found in the attached vita.

In summary, I have extensively researched and evaluated the competitive effects of railroad mergers, and I have participated directly in several ICC/STB merger and control proceedings. Specifically, I have provided testimony regarding the competitive consequences of these transactions. In preparing my testimony, I have drawn on this experience.

II. The STB Should Consider Applying A "Structural Approach" To Analyzing The Competitive Harms From This Transaction

The STB, in having moved towards a policy emphasizing preserving and enhancing competition in rail mergers, has in fact moved towards a more structural approach with respect to reviewing rail mergers and consolidations. I have long supported such an approach and believe the Board should apply such a policy here. Such a structural approach evaluates transactions in broader economic and strategic terms and provides a more refined assessment of the impact of a rail merger on market structure, as opposed to simply counting the number of railroads before and after a merger, and would go well beyond merely delineating "2-1" shippers at a specific station or even a specific shipper facility. Such an approach is commonplace for assessing mergers in other industries and other countries.

The first step in such a structural approach would be to define relevant markets, for example, rail traffic in origin-destination corridors. The second step is to analyze market structure prior to the merger as indicated by the market shares of participants. Commonly, a measure of market concentration, such as the share held by the leading firm or firms or the Herfindahl Index (HHI) is used in evaluating market concentration. The third step is to analyze the change in market structure in a given market from the merger. If the structure is substantially more concentrated following the merger, there is a strong presumption of competitive harm.

The U.S. Department of Justice's Horizontal Merger Guidelines provide a prominent example of this methodology and how it is implemented for mergers under the purview of the DOJ Antitrust Division. Indeed, many in the industry desire to remove merger authority from the STB and place it under DOJ. However the STB already has the tools necessary to review transactions pursuant to a structural approach and apply policies and approaches similar to those applied by DOJ. The most relevant portion of the Merger Guidelines that could be applicable here states:

> Post-Merger HHI Above 1800. The Agency regards markets in this region to be highly concentrated. Mergers producing an increase in the HHI of less than 50 points, even in highly concentrated markets post-merger, are unlikely to have adverse competitive consequences and ordinarily require no further analysis. Mergers producing an increase in the HHI of more than 50 points in highly concentrated markets post-merger potentially raise significant competitive concerns, depending on the factors set forth in Sections 2-5 of the Guidelines. Where the post-merger HHI exceeds 1800, it will be presumed that mergers

> producing an increase in the HHI of more than 100 points are likely to create or enhance market power or facilitate its exercise. The presumption may be overcome by a showing that factors set forth in Sections 2-5 of the Guidelines make it unlikely that the merger will create or enhance market power or facilitate its exercise, in light of market concentration and market shares.

III. Applying Such An Approach In This Case Reveals Horizontal Competitive Effects Not Yet Analyzed By The Applicants

It is immediately clear that viewing the instant transaction through the lens of the guidelines reveals horizontal competitive issues which have not been discussed by the Applicants.[1] The Applicants have provided two studies regarding competitive effects. The first examined specific 6-digit SPLC stations where the only two serving railroads are CP and DME. The conclusion was that there would be no "2 to 1" impacts at the station level. The second study, submitted in the supplement to the Application, used a 50/10/10 screen to examine the impact of the transaction on source and geographic competition. While the Applicants have provided these studies regarding the competitive impact of the merger, an appropriate and complete structural analysis of potential anticompetitive impacts goes well beyond this.

Railroads compete with each other in many cases not only when both serve the same point, or station, but also when both provide service in the same geographic area or in the same origin/destination corridor. Customers can gain from such competitive rail options in their transportation buying decisions. Also, with the possibility of truck transloading, build-ins/build-outs, product substitution, plant production shifts, plant relocation, and source and geographic

[1] I will refer to DM&E and IC&E, collectively, as "DME," just as was done in the subject railroad control Application ("Application") filed with the Board in STB Finance Docket No. 35081. In addition, I intend in my statement to employ terminology in a manner consistent with the Application filed in this proceeding, except that I prefer to use "CP" to refer collectively to CPR and SOO.

competition, railroads may be effective competitors even where they do not both serve the same station. Thus, one cannot reach a conclusion that there are no horizontal competitive effects without a careful and systematic analysis of whether the instant merger eliminates independent rail routings between broader geographic areas, such as counties or Business Economic Areas ("BEAs"). The market and competitive analysis provided by the Applicants does not investigate these important dimensions of competitive harm

For example, applying the DOJ's structural approach as discussed above with a market definition of BEA-BEA shows that there are horizontal effects of the merger in the Twin Cities (BEA 107) to Chicago (BEA 64) market CP competes directly with ICE and DME in this rail market, and a structural approach would examine carefully these horizontal effects. The market shares of the various routings are provided in Table 1, attached hereto as an Appendix.

We calculate a Herfindahl index based alternatively on Cars, Tons and Freight Charges based on the pre-merger structure.[2] Based on cars, the pre-merger Herfindahl is [redacted]; tons is [redacted]; freight charges is [redacted]. Any of the three measures provides a market concentration well above the DOJ Guideline threshold of 1800 for a "highly concentrated" market. We next calculate the post-merger structure, by combining the market shares for DME and CP, and again calculating the Herfindahl, we find that for cars, the post-merger Herfindahl is [redacted], tons is [redacted]; freight charges is [redacted]. All of the three measures have increased more than 100 points. According to the Guidelines, "[w]here the post-merger HHI exceeds 1800, it will be presumed

[2] We take a conservative approach and assign ICE/CP interline traffic to CP. UP/EJE traffic is assigned to UP. CN/CSXT/CN traffic is assigned to CN. BNSF/EJE and BNSF/CSS traffic is assigned to BNSF. The small amount of interline traffic between BNSF and CN or UP is assigned to BNSF. UP/CN interline traffic is assigned to UP.

that mergers producing an increase in the HHI of more than 100 points are likely to create or enhance market power or facilitate its exercise." Based upon application of this approach, the Transaction will presumably create a substantial lessening of competition for rail transportation between Chicago and the Twin Cities.

IV. Applicants Also Compete Directly With Each Other With Regard To Alternative Routings For Grain Traffic

Another area which has not been explored by the Applicants is direct competition between DME and CP on movements of export grain from the grain regions of Minnesota and Iowa to the Pacific Northwest. DME originates grain from these origins that is then interlined with BNSF for movement to Seattle and the export markets. In 2006, this represented [redacted] carloads and [redacted] million of DME/BNSF interlined grain revenue. This DME/BNSF routing competes with a CP (SOO) UP routing whereby SOO originates grain in the Minneapolis BEA area, interchanges it with CP, and then CP interchanges it to UP for export through Portland. This CP/UP routing represented [redacted] carloads in 2006. Clearly the DME/BNSF routing competes against the CP/UP routing for the movement of grain from the heartland of the grain region to the export markets of the Pacific Northwest. Thus, inserting CP into each of these routes will eliminate the independence of these two routing options, thus representing another horizontal effect of the transaction.

V. There Are Additional Competitive Effects Of The Transaction Given The Alliance Of CP And UP

I have reviewed the verified statements of other witnesses and the information gathered in discovery and through public sources, based upon this review, I note that UP and CP have a strong strategic relationship. CP and UP have worked together for almost a decade in numerous alliances, most of which are particularly important for the flow of grain. Pursuant to such arrangements, CP, where possible, will seek to route DME originated traffic to favor UP as a connecting carrier. In this context, and given the Board's prior policy of reviewing the competitive effects of alliance arrangements, the STB should also examine potential diminution of competition where DME and UP are currently key competitors. An important area of concern is for corn traffic originating from BEAs 100 and 107. DME originates over [redacted] tons annually from these locations. UP originated over [redacted] from these same two BEAs. Given the close linkage of CP and UP, it could be expected that competition between UP and DME (post merger) would be less intense than currently for corn traffic to many different markets.

The main destinations (via single-line service) for UP grain originated from these two BEA's are to the BEA's of Little Rock-N. Little Rock, AR, New Orleans, LA, Fayetteville-Springdale-Rodgers, AR-MO-OK, Davenport-Moline-Rock Island, IA-IL, Los Angeles-Riverside-Orange Co.-CA-AZ, San Francisco-Oakland-San Jose, CA, Portland-Salem, OR-WA, Seattle-Tacoma-Bremerton, WA. For DME originated grain the main BEA destinations (via single-line or in interline service with another railroad) are Seattle-Tacoma-Bremerton, WA (BNSF), Portland-Salem, OR-WA (BNSF), Dallas-Ft. Worth, TX-AR-OK (KCSR), Davenport-Moline-Rock Island, IA-IL (DME), Fayetteville-Springdale-Rodgers, AR-MO-OK (KCSR), Little Rock-N, Little Rock, AR (KCSR), Jackson, MS-AL-LA (KCSR), and Chicago-Gary-Kenosha, IL-IN-WI (DME).

As the data shows, DME/KCSR routings are competing against UP routings from the same origins (BEAs 100 and 107) to the same destinations of Fayetteville-Springdale-Rodgers, AR-MO-OK and Little Rock-N. Little Rock, AR. The grain that is involved in these routings is corn destined to feed mills in Arkansas, Missouri, and Oklahoma. DME originations also provide a significant amount of the grain destined to the Jackson, MS-AL-LA BEA. In a post-transaction environment and to the extent UP requires additional corn for these markets, I would fully expect CP to use its control of DME to route DME originated corn to an interchange with UP at Kansas City, rather than interchanging this corn to KCSR. CP also has an incentive to downgrade service for KCSR routings so as to encourage shifting this volume from KCSR feed mills to UP feed mills.

Another area of potential loss of competition involves rail movements between Chicago and Laredo pursuant to North American Free Trade Agreement ("NAFTA"). KCS plays an important role in NAFTA trade. The Transaction here threatens to limit NAFTA shipper options and erode competition in important NAFTA rail service corridors. In particular, due to CP's relationships with UP, CP will likely seek to undercut the competitive position of KCS. One way they could do this would be to cancel KCS's existing ratemaking authority to Chicago. From what I have learned, KCSR has in place an agreement with DME that allows KCS to provide certain haulage services between Kansas City and Chicago. Through this agreement, KCSR can offer a competitive alternative to UP single-line service between Laredo and Chicago. Although I understand that this agreement has never actually been used, that does not mean that it plays no competitive role. An agreement can constrain rates simply because of the potential for its use as a competitive counterbalance. Cancellation of this agreement would remove the KCS routing from Chicago and would lessen competition.

Given the existing traffic flows between CP and UP, it is apparent that CP utilizes UP for the movement of NAFTA traffic. Some CP originated traffic destined for Mexico is interchanged to UP at Chicago for movement to the Mexican gateways. In theory, the DME/KCS routing between Chicago and Laredo provides a competitive option to CP/UP routings. In addition, given CP's natural desire to want to extend its haul in a post-merger environment, I would expect CP to seek ways to move its interchange with UP from Chicago to Kansas City. CP would not want KCS traffic competing over that very same route. CP therefore has several incentives to cancel the DME/KCS agreement in a post-transaction environment. In light of my structural analysis, in order to ensure continued competition in the NAFTA corridor, I would recommend that the Board ensure that KCS's access to the important Chicago gateway be maintained.

VII. The Board Needs To Also Take Into Account The Loss Of DME As A Neutral Railroad

Another area of potential anticompetitive effects regards vertical aspects of the transaction. Indeed, in the instant transaction, which is predominantly end-to-end, vertical impacts need to be carefully addressed before reaching a conclusion that the transaction is not anticompetitive. The STB's revised rail merger guidelines appropriately place greater emphasis on vertical effects, for example, that gateways remain open in the context of end-to-end mergers. Consistent with these guideline revisions, a number of STB cases over the past ten years have involved careful analysis of vertical impacts and, in a number of instances, monitoring conditions and other safeguards to address potential vertical anticompetitive effects have been put in place. For example, in the STB deliberations regarding creation of the NAFTA Railway by Kansas City Southern, the STB conducted an extensive evaluation of concerns raised by UP and BNSF regarding vertical foreclosure at the Laredo gateway. The STB then imposed certain requirements that existing gateways, routings, and interchanges remain open pursuant to various representations put forth by KCS. CP has not put forth any such representations in this proceeding, which indicates to me that CP desires to use the Transaction as a means of changing the commercial arrangements and routings agreed to by DME.

In particular, DME currently serves as a neutral connection to a number of Class I railroads, including KCS. After the merger, this friendly connection will be lost. CP will have an incentive to route originating traffic so that it receives the longest haul. It is well established that railroads have both the ability and incentive to do so[3] and the statement of Mr. Woodward confirms that CP would do so here. As discussed by other witnesses, particularly Mr. Bilovesky, the loss of DME grain through such efforts by CP to seek the long-haul for movements of this grain to the Pacific Northwest will cause adverse competitive impacts to the feed mills served by KCSR in the south-central United States. While I am not an expert in the grain markets, the effects put forth by Mr. Bilovesky (and Mr. Jones) are logical outcomes of the Transaction and would constitute a reduction of competition and harm to consumers. Therefore, to the extent

[3] Indeed an empirical study of the railroad industry I co-authored supports the presence of this behavior (Grimm, C. and R. Harris, "A Qualitative Choice Analysis of Rail Routings: Implications for Vertical Foreclosure and Competition Policy," <u>Logistics and Transportation Review</u> Vol. 24, No. 1, March 1988, pp. 49-67)

possible, I would recommend the Board undertake efforts to alleviate these competitive effects as part of any approval of the Transaction.

VIII. The STB Should Address Competitive Effects Of This Transaction In A Comprehensive And Thorough Fashion.

The rail industry environment in 2008 is dramatically different from initial years following the Staggers Act. Following extensive industry consolidation, most recently in the mid-1990s, the rail industry is highly concentrated, both with regard to aggregate U.S. market shares and options available in specific markets. The STB has recognized these fundamental changes with its merger moratorium in the late 1990s and subsequent new merger guidelines, which enunciate a much greater concern for competitive harms in evaluating mergers. At the same time, there has been a strong shipper backlash with regard to rail consolidation, with attempts for legislative relief commonplace year in and year out. Excess capacity, once a prime motivation for rail consolidation, has been largely eliminated in the industry, and railroads have achieved record profits in recent years. Clearly, the current railroad environment suggests that the STB should ensure a careful and detailed evaluation of competitive impacts in this transaction. Based upon the record in this proceeding, one cannot conclude that Applicants have met their burden of proving that the Transaction does not result in a substantial lessening of competition.

TABLE 1 - REDACTED

VERIFICATION

I, Curtis M Grimm, declare under penalty of perjury that the foregoing statement is true and correct. Further, I certify that I am qualified to file this Verified Statement. Executed this 3rd day of March, 2008

Curt Grimm

Curtis M. Grimm

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PRESENT POSITION

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EDUCATION:

Institution	Degree	Date	Field
University of California, Berkeley	Ph.D.	6/83	Economics

Major Areas: Industrial Organization, Transportation and Econometrics/Statistics.

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Institution	Degree	Date	Field
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Economist, Office of Policy and Analysis, Interstate Commerce Commission, Washington, D.C., January 1981 - December 1981.

Assistant to the Chief of Intercity Transport Development, Planning Division, Wisconsin Department of Transportation, Madison, October 1977 - August 1978 and November 1975 - July 1976.

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80) Grimm, C. and R. Windle, "Regulation and Deregulation in Surface Freight, Airlines and Telecommunications," in Regulatory Reform and Labor Markets, J. Peoples, ed., Kluwer Academic Publisher, Boston, 1998.

81) Grimm, C. and C. Winston, "Competition in the Deregulated Railroad Industry: Source, Effect and Policy Issues," in S. Peltzman and C. Winston, editors, Deregulation of Network Industries: The Next Steps, Brookings, Washington, D.C. 2000, pp. 41-72.

82) Dresner, M. and C. Grimm, "Public Policy and Logistics," in Handbook of Logistics and Supply-Chain Management, edited by A.M. Brewster, K.J. Button, and D.A. Hensher, Pergamon, Amsterdam, 2001.

83) Ferrier, W., K. Smith and C. Grimm, "The Role of Competitive Action in Market Share Erosion and Industry Dethronement: A Study of Industry Leaders and Challengers," published in Selected Collection of Award Winning Papers in Academy of Management Journal, Anne S. Tsui, ed., Peking University Press, 2006. (This book is a collection of papers which had received a best paper award in AMJ or AMR.)

84) Grimm, C. "Merger Analysis in the Post-Staggers Railroad Industry," chapter in Competition Policy and Merger Analysis in Deregulated and Newly Competitive Industries, P. Carstensen and B. Farmer, eds., Edgar Elgar Publishing, Northampton, MA (forthcoming).

Articles in Journals with Internal Review Boards

85) Grimm, C. and R. Harris, "The Financial Performance and Prospects of Railroads in the South and Southwest," Texas Business Review 56 (6), November/December 1982, pp. 257-262.

86) Grimm, C. and R. Harris, "Vertical Foreclosure in the Rail Freight Industry: Economic Analysis and Policy Prescriptions," ICC Practitioners' Journal 50 (5), July/August 1983, pp. 508-531.

87) Corsi, T. and C. Grimm, "Transportation Education in the 1980's: An Examination of Teaching Materials," Transportation Practitioners' Journal 52 (1), Fall 1984, pp. 27-39.

88) Grimm, C. and J. Kling, "Integrating Microcomputers into a Transportation and Logistics Curriculum," Defense Transportation Journal Vol. 44, No. 5, October 1988, pp. 14-22.

Articles in Proceedings (other than those listed above)

89) Grimm, C., "Public Interest Evaluation of Recent Rail Mergers," 1981 Eastern Transportation Law Seminar Papers and Proceedings, Association of ICC Practitioners, Washington, D.C., pp. 171-176.

90) Grimm, C., "Promoting Competition in the Railroad Industry: A Public Policy Analysis," Transportation Research Forum Proceedings, 1984, pp. 222-227.

91) Grimm, C. and K. Smith, "Impact of Deregulation on Railroad Strategies and Performance," Transportation Research Forum Proceedings, 1985, pp. 540-544.

92) Corsi, T., C. Grimm and R. Lundy, "ICC Exemptions of Rail Services: Summary and Evaluation," Transportation Research Forum Proceedings, 1985, pp. 86-92.

93) Corsi, T., C. Grimm and R. Smith, "Motor Carrier Strategies in a Changing Environment: An Empirical Analysis," Transportation Research Forum Proceedings, 1986, pp. 177-180.

94) Grimm, C., K. Smith and R. Blankinship, "Railroad Strategies and Performance: An Exploratory Study," 1987 Eastern Academy of Management Proceedings, pp. 25-28.

95) Smith, E., M. Gannon, C. Grimm and G. Young, "Competitive Advantage in Diverse Industries," Proceedings of the Second Biennial High Technology Conference, University of Colorado, Boulder, Colorado, January 1990.

96) Grimm, C., "The Impact of Entry and Concentration in Australian Aviation: A Test of Contestability Theory," Transportation Research Forum Proceedings, 1992.

97) Sapienza, H. and C. Grimm, "The Importance of Founder, Start-Up Process, and Structural Variables in Entrepreneurial Firms: A Study of the Shortline Railroad Industry," Frontiers of Entrepreneurship Research, 1994.

Other Publications, Reports and Monographs

Grimm, C., "Combining Scholarly Research with Public Policy Evaluation," ITS Review, Vol. 5, No. 2, Institute of
Transportation Studies, University of California, February 1982.

Grimm, C., "Strategic Motives and Competitive Effects in Railroad Mergers: A Public Policy Analysis," Dissertation Series, Institute of Transportation Studies, University of California, August 1983 (UCB-ITS-DS-83-1).

Grimm, C., "Preserving and Promoting Rail Competition," Report to the National Industrial Transportation League, 1984.

Grimm, C., "Econometric Techniques to Estimate Rail Costs," Report to the Railroad Accounting Principles Board, General Accounting Office, Washington, D.C., October 1985.

Roberts, M., T. Corsi and C. Grimm, "Benefit-Cost Analysis of Weight Limit Exemption for Vehicles Carrying International Freight in the Route 50 Corridor," Study Prepared for the State Highway Administration, State of Maryland, February 1988.

Deregulation of Domestic Aviation: The First Year, Bureau of Transport and Communication Economics, Australian Government Publishing Service, Canberra, Australia, 1991 (lead author).

Cambridge Systematics; Leeper, Cambridge and Campbell; T. Corsi, and C. Grimm, "A Guidebook for Forecasting Freight Transportation Demand," NCHRP Report 388, National Academy Press, Washington, D.C. 1997.

CONTRACTS AND GRANTS:

Co-Principal Investigator, U.S. DOT Federal Motor Carrier Safety Administration cooperative research agreement, 2005-present.

Course Development Grant, Joint MS Program in Telecommunications.

University of Maryland Center for International Education and Research (CIBER) Research Award, 1991.

University of Maryland Dingman Center for Entrepreneurship Research Award, 1990.

Small Business Administration, Small Business Development Center, University of Maryland. From 1985 - 1989, Ken Smith, Martin Gannon and I received funding to establish Center for the counseling and training of small business managers. We also conducted research on strategic management of small businesses, including travel agencies and electronic firms. (Amount: $200,000)

Department of Education Business and International Education Program. During 1988 and 1989, I was part of a team which received a two-year grant for curriculum development, research and professional outreach. The program involves collaboration with the Maryland Port Authority on research, outreach and internships. (Amount: $110,000).

Maryland Department of Transportation. During 1987/88 I worked with Tom Corsi and Merrill Roberts on a contract to study the impact of exempting Eastern Shore export container traffic from the 80,000 pound highway weight limitation. (Amount: 35,000).

University of Maryland Grant to Integrate Computer Use into the Classroom, 1985.

University of Maryland General Research Board Summer Research Award, 1984.

CONFERENCE PAPER PRESENTATIONS:

"Public Interest Evaluation of Recent Rail Mergers," presented at the 11th Association of ICC Practitioners' Eastern Transportation Law Seminar, October 1981.

"Stand-Alone Costs: Use and Abuse in Railroad Maximum Rate Determination," presented at the Eastern Economics Association Annual Meeting, March 1984 (with Philip Fanara).

"Promoting Competition in the Railroad Industry," presented at the Transportation Research Forum Annual Meeting, October 1984.

"The Politics of the Budget Deficit and the Role of Political Interest Groups," presented at the Annual Meeting of the Association for Public Policy Analysis and Management, October 1984 (with John Holcomb).

"Impact of the Staggers Act on Rates and Shipper Quality: Role of Shipper Size and Competition," presented at the American Economics Association/Transportation and Public Utilities Group Annual Meeting, December 1984 (with Ken G. Smith)

"The Effects of Railroad Mergers on Industry Performance and Productivity," Transportation Research Board Conference on Rail Productivity, University of Illinois, June 1985, (with Robert G. Harris).

"Environmental Variation, Strategic Change and Firm Performance: A Study of Railroad Deregulation," presented at the Annual Meeting of the Academy of Management, August 1985 (with Ken G. Smith).

"Management Characteristics, Strategy, and Strategic Change," presented at the Strategic Management Society Annual Meeting, Barcelona, Spain, October 1985 (with Ken G. Smith).

"Impact of Deregulation on Railroad Strategies and Performance," presented at the Transportation Research Forum Annual Meeting, November 1985 (with Ken G. Smith).

"ICC Exemptions of Rail Services: Summary and Evaluation," presented at the Transportation Research Forum Annual Meeting, November 1985 (with Thomas M. Corsi and Robert Lundy).

"Excess Branchline Capacity in the Railroad Industry," presented at the Transportation Research Board Annual Meeting, January 1986.

"The Economics of Coal Transportation: Implications for Railroad Shipper Strategies," presented at the Transportation Research Board Annual Meeting, January 1986 (with Les Selzer and Kent Phillips).

"The Organization as a Reflection of its Top Managers: An Empirical Test," presented at the Annual Meeting of the Academy of Management, August 1986 (with Ken G. Smith).

"Motor Carrier Strategies in a Changing Environment: An Empirical Analysis," presented at the Transportation Research Forum Annual Meeting, September, 1986 (with Thomas M. Corsi and Raymond Smith).

"Shifts in Use of Owner-Operators Among LTL General Freight Carriers Since the Motor Carrier Act of 1980," presented at the Transportation Research Forum Annual Meeting, September, 1986 (with Thomas M. Corsi).

"Environmental Variation, Decision Comprehensiveness and Performance," presented at the Strategic Management Society Annual Meeting, Singapore, October, 1986 (with Ken G. Smith, Martin Gannon, and Terence Mitchell).

"Gambit and Repartee: A Theory of Competitive Action and Responses," presented at the Annual Meeting of the Academy of Management, August 1986 (with Ken G. Smith).

"The Impact of the Environment on Personnel Policies: Management Characteristics in the U.S. Railroad Industry," presented at the Annual Meeting of the Academy of Management, August 1987 (with James Guthrie and Ken G. Smith)

"Mobility Barriers in the Motor Carrier Industry," presented at the Transportation Research Forum Annual Meeting, November 1987 (with Thomas M. Corsi).

"Railroad Cost Structure - Revisited" presented at the Transportation Research Forum Annual Meeting, November 1987 (with Tony Barbera, Kent Phillips and Les Selzer).

"The Impact of Rail Rationalization on Traffic Densities: A Test of the Feeder Line Theory," presented at the Transportation Research Board Annual Meeting, January 1988 (with Les Selzer and Kent Phillips).

"Porter's Generic Strategies and Organizational Size," presented at the Strategic Management Society Annual Meeting, October 1988 (with Ken Smith).

"Predictors of Competitive Responses in the Domestic Airline Industry," presented at the Strategic Management Society Annual Meeting, October 1988 (with Ken Smith and Martin Gannon).

"ATLFs: Driving Owner-Operators into the Sunset," presented at
the Transportation Research Forum Annual Meeting, November 1988 (with Thomas M. Corsi).

"Competitive Strategic Interaction: Action Characteristics as Predictors of Response," presented at the Annual Meeting of the Academy of Management, August 1989 (with Ming-Jer Chen and Ken G. Smith).

"Strategies and Performance in the Truckload General Freight Segment Before and After Deregulation," presented at the Transportation Research Forum Annual Meeting, October 1989 (with Thomas M. Corsi).

"Rivalry in the U.S. Domestic Airline Industry," presented at the Strategic Management Society Annual Meetings, October 1989 (with Ken Smith and Martin Gannon).

"Building Competitive Advantage in Diverse Industries," presented at the Boulder, Colorado Conference on the Management of the High Technology Firm, January 1990 (with Greg Young, Ken Smith, and Martin Gannon).

"Economic Effects of Surface Freight Deregulation," presented at the Transportation Research Board Annual Meeting, January 1990 (with Cliff Winston and Thomas Corsi).

"Strategies of Challenging Airlines at Hub-Dominated Airports," presented at the Transportation Research Forum Annual Meeting, October 1990 (with James Kling and Thomas M. Corsi).

"Size, Strategy, and Performance: LTL Motor Carriers," presented at the Transportation Research Board Annual Meeting, January 1991 (with Raymond Smith and Thomas Corsi).

"The Role of Firm Reputation in Competitive Interaction," presented at the Annual Meeting of the Academy of Management, August 1991 (with Leith Wain, Martin Gannon and Ken G. Smith).

"The Advantage of Size in the U.S. Trucking Industry," presented at the Transportation Research Forum Annual Meeting, November 1991 (with Carol Emerson and Thomas M. Corsi).

"The Impact of Entry and Concentration in Australian Aviation: A Test of Contestability Theory," presented at the Transportation Research Forum Annual Meeting, October 1992.

"Reevaluating Returns to Scale in Transportation," presented at the Transportation Research Forum Annual Meeting, October 1993 (with K. Xu, R. Windle and T. Corsi).

"Access and Competition Policy in the US Rail Freight Industry: Potential Applications to Telecommunications," presented at a conference on <u>Sustaining Competition in Network Industries through Regulating and Pricing Access</u>, CITI, Columbia University, November 1993 (with R. Harris).

"Engaging Competitors," presented to the Whitmore Conference, Dartmouth College, New Hampshire, September 1994, (with G. Young and K. Smith).

"Engaging a Rival for Competitive Advantage: Firm Resources and the Competitive Environment as Predictors of Competitive Firm Activity," presented at the Annual Meeting of the Academy of Management, August 1994 (with G. Young, A. Schomburg and K. Smith).

"David and Goliath: Strategies for Challenging the Dominant Rival," presented at the Annual Meeting of the Academy of Management, August 1994 (with K. Smith, T. Corsi and J. Kling)

"Wealth Effects of New Product Rivalry," presented at the 14th annual international conference of the Strategic Mangement Society, Paris, September 1994 (with H. Lee, K. Smith, and A. Schomburg).

"Business Distress and a Firm's Propensity to be Rivalrous," presented at the 14th annual international conference of the Strategic Mangement Society, Paris, September 1994 (with C. MacFhionnlaoich and K. Smith).

"Industrial Organization Economics, Resource-Based Theory, and Schumpeterian Perspectives on Competitive Advantage: Toward an Action-Based Model of Advantage," presented at the Annual Meeting of the Academy of Management, August 1995 (with K. Smith).

"Strategic Groups and Rivalrous Firm Behavior: Towards a Reconciliation," presented at the Annual Meeting of the Academy of Management, August 1995 (with K. Smith and G. Young).

"Shareholder Wealth Effects of New Product Rivalry," presented at the Annual Meeting of the Academy of Management, August 1995 (with H. Lee and K. Smith).

"Creative Destruction and Competitive Dynamics: An Action-Based Study of Industry Dethronement and Market Share Erosion," presented at the Annual Meeting of the Academy of Management, August 1996 (with W. Ferrier and K. Smith).

"The Rate of International Alliance Formation: The Role of Firm Resources, Strategy, and Industry Structure," presented at the Annual Meeting of the Academy of Management, August 1996 (with G. Young and K. Smith).

"An Assessment of the Validity of Competitive Dynamics Research," presented at the Annual Meeting of the Academy of Management, August 1996 (with G. Young, M. Becerra and K. Smith).

"The Rate of International Alliance Formation: The Role of Firm Resources, Strategy, and Industry Structure," presented at the 16th annual international conference of the Strategic Management Society, Tempe, Arizona, October 1996 (with G. Young and K. Smith).

"Performance Implications of Market and Non-Market Actions," presented at the Annual Meeting of the Academy of Management, August 1997 (with T. Quasney and B. Shaffer).

"Multimarket Contact, Resource Heterogeneity, and Rivalrous Firm Behavior," presented at the Annual Meeting of the Academy of Management, August 1997 (with G. Young and K. Smith).

"Performance Implications of Market and Non-Market Actions," presented at the Annual Meeting of the Academy of Management, August 1997 (with T. Quasney and B. Shaffer).

"Techniques of Transportation Analysis: Costs," discussant at Transport Policy and Economics Conference in Honor of John R. Meyer, Kennedy School of Government, Harvard University, September 1997.

"A Conceptual Model of Supplier-Reseller Satisfaction Perceptions in Distribution Channels," Academy of Marketing Science, Coral Gables, Florida, 1997 (with C. Emerson and R. Krapfel).

"The Impact of Financial Condition on Competitive Behavior: Towards a Reconciliation of Competing Views," presented at the Annual Meeting of the Academy of Management, August 1998 (with C. MacFhionnlaoich, W. Ferrier and K. Smith).

"Competitive Effects of Railroad Mergers," Transportation Research_Forum Annual Meetings, Philadelphia, October 1998 (with J. Plaistow).

"The Canadian Experience with Competitive Access, " Transportation Research Board Annual Meeting, January 1999.

" Predicting Order and Timing of New Product Moves: The Role of Top Management," presented at the Annual Meeting of the Academy of Management, August 1999 (with A. Srivasta, H. Lee and K. Smith).

"Competition in the Deregulated Railroad Industry: Source, Effect and Policy Issues," presented at the AEI-Brookings conference on Deregulation of Network Industries, December, 1999.

"Future of Rail Regulation," presented at the Alliance for Rail Competition Second Annual Rail Customer Forum, Washington, D.C., March 1, 2000.

"The State of Railroad Research," presented at the Transportation Research Forum Annual Meeting, Annapolis, November 2000.

"Investigating the Action Dilemma: Untangling the Relationships Between Firm Activity, Rival Activity, and Firm Performance," presented at the Annual Meeting of the Academy of Management, August 2001 (with P. Derfus and K. Smith).

Discussant, Workshop on Airline and National Strategies for Dealing with Airport and Airspace Congestion, College Park, March 2001.

Participant, Federal Railroad Administration and Surface Transportation Board Joint Roundtable on Rail Freight Industry, June 2002.

"A Schumpeterian Perspective on Innovation," presented at the Leading Through Innovation Research Conference, College Park, January 2003.

"The Role of Conduct in the Structure, Conduct, Performance Relationship," presented at the Annual Meeting of the Academy of Management, August 2003 (with P. Maggitti, P. Derfus and K Smith).

"The Impact of Market Actions on Firm Reputation," presented at the Annual Meeting of the Academy of Management, August 2003 (with D. Baseo, V. Rindova, P. Derfus and K. Smith).

"Merger Analysis in the Post-Staggers Railroad Industry," presented at a conference on Competition Policy and Merger Analysis in Deregulated and Newly Competitive Industries, Madison Wisconsin, June 2005.

"Firm Action, Rival Action and Firm Performance: Understanding the Effect of Competitive Interdependence," presented at the Annual Meeting of the Academy of Management, August 2005 (with P. Maggitti, P. Derfus and K. Smith).

RESEARCH AWARDS:

Journal of Management 2004 best paper award, for the paper determined to be the best published in 2003 in the *Journal of Management.*

Academy of Management 2000 best paper award, for the paper determined to be the best published in 1999 in the *Academy of Management Journal.*

Award for best paper, marketing channels track, Academy of Marketing Science conference, Coral Gables, Florida, 1997.

Award for the best airline paper and best paper overall, 1990 Transportation Research Forum Conference.

Plowman Award for the best paper, 1987 Transportation and Logistics Educators Conference.

Regular Common Carrier Conference Award for the best motor carrier paper, Transportation Research Forum Annual Meeting, September, 1986.

EDITORIAL AND REVIEWING ACTIVITIES:

Consulting Editor (1991-1993) Journal of the Transportation Research Forum.

Editorial Review Board, Journal of Transportation Management (1993-present).

Editorial Review Board, Transportation Research – Part E (2001-present).

Editorial Review Board, Journal of the Transportation Research Forum (2001-present).

Frequent referee activity for numerous journals.

PROFESSIONAL AFFILIATIONS:

American Society of Transportation and Logistics; Transportation Research Forum; American Economics Association & Transportation and Public Utilities Group; Academy of Management; Strategic Planning Society.

TEACHING AND ADVISING:

Courses Taught

BMGT 370 (Introduction to Transportation: also served as course coordinator)
BMGT 372 (Introduction to Logistics Management)
BMGT 476 (Computer Models in Transportation and Logistics)
BMGT 495 (Business Policy)
BMGT 670 (Economic Environment of Business)
BMGT 671 (Managerial Economics)
BMGT 683 (Global Economic Environment)
BMGT 770 (Transportation Theory and Analysis)
BMGT 798 (Field Studies in Industry and Competitor Analysis)

BMGT 808 (Seminar in Industrial Organization and its Application to Strategic Management; Seminar in Supply Chain Management Research)

ENTS 631 (Telecommunications Policy)

Teaching Awards

Allen J. Krowe Award for Teaching Excellence, College of Business and Management, 1988.

Selected as one of the top 15% teachers in the College of Business and Management (13 times, most recently in 2006)

Member of the Following Ph.D. Dissertation Committees:

Pamela Donovan (co-chair)
David Cantor (co-chair)
Victor Cheng (co-chair)
Tom Quasney (chair)
Kirk Patterson (co-chair)
Wally Ferrier (co-chair)
August Schomburg (co-chair)
Greg Young (co-chair)
Hun Lee (co-chair)
Carol Emerson (chair)
Cormac Mac Fhionnlaoich (co-chair)
Pam Derfus (co-chair)

Ayesha Malhotra
Ming Zhou
Stephanie Head
Chris Lin
Constantinos Christou
Chul Moon
Deborah Lyons
Jane Feitler
Laura Power
Ming-Jer Chen
Harry Sapienza
Jack Scarborough
James Kling
Robert Trempe
George Rubenson
Ven Sriram
Raymond Smith
Ritu Lohtia
Jason Chang
Douglas Meade
Barbara Houchen
Leith Wain
John Burgess
Douglas LaBahn
Ker-Tsung Lee
Yeon Myung Kim
Steven Chien
Chad Syverson

Eungcheol Kim
Helena Schweiger

SERVICE:

Department Chair, Transportation/Logistics, Business and Public Policy (December 1994-July 2003).

Chair, Teaching Enhancement Committee, 2004-present.

Member, APAC (Campus level committee, chaired by the Provost, charged with advising the Provost on strategic and programmatic matters) 2000-2003.

Member, Vice President for Administrative Affairs search committee (2002-2003).

Member, Committee to Critique MBA Program Report, 2005.

Member, Ad Hoc committee to design an EMBA program (2001-2002).

Member, MBA director search committee (2001)

Member, Provost's Committee to conduct five year review of Dean Howard Frank (2001).

Chair of Search Committee, Executive Director of the Center for Knowledge and Information Management, 1999.

Member, CRC T&P Committee, Don Riley (1998), Samer Faraj (2004), and Josh Newberg (2004); Gil Souza (2005).

Chair, Extra Merit Step for Non-Exempt Employees Committee, 1999.

Member, MBA 4th Track Committee (subcommittee of executive committee) (1996-1998).

Member, Strategic Planning Committee (subcommittee of executive committee). (1996-present).

College Workload coordinator (responsible for attending meetings with Provost and reps re: workload requirements and taking lead on filling out compliance forms).

Member, Executive Committee, Middlestates Accreditation Committee, University (Dan Fallon/Nelson Markley, Chair), Dec. 1995-1997.

Member, Faculty Composition and Development Section, AACSB Accreditation committee (1995).

Lead College Member on Campus Committee to form and fund a Global China Institute (1995).

Chair of Search Committee, Transportation, Business and Public Policy Faculty Positions (1994-5, 1995-6, 1996-7, 1997-8, 1998-9, 1999-2000).

Member, College Strategic Planning Committee (drafted section on MBA program), 1994-5.

Chair, MBA Oversight Committee, College of Business and Management (May 1994-Jan. 1995).

Member, MBA Oversight Committee, College of Business and Management (1992-1994).

Chair, ELM Coordinator's Committee, College of Business and Management, (1993-1994).

Member, External Communications Committee, College of Business and Management, 1994.

Chair, PR on Academic Quality Committee, 1993.

Member Technology Advancement Program Business Screening Panels (1986-1990).

Member, Faculty Grievance Hearing Board, College Park Campus (1991).

Member, College Budget Committee (1990-1991).

Member, Strategic Planning Steering Committee, and Chair, MBA Subcommittee, College of Business and Management (1989-1990).

Member, General Committee on Faculty Affairs, College Park Campus Senate (1984-1986, 1987-1988).

Elected Representative to the College Park Campus Senate (1988-1991).

Member, Graduate Committee, College of Business and Management (1987-1988).

Chairman, MBA Case Competition Subcommittee of the Graduate Committee (1987).

Faculty Assistant Coordinator, MBA/Rutgers Invitational Case Tournament (1986-1987).

Faculty Judge, MBA Case Competition, College of Business and Management (1989).

Member, Undergraduate Committee, College of Business and Management (1987-1988).

Faculty Co-Advisor, University of Maryland Transportation and Logistics Club (1985-1990).

Member, International Task Force, College of Business and Management (1986-1987)

Member, Dean's Computer Integration Task Force, College of Business and Management (1986-1988).

Participant in Planning Session for External Activities, College of Business and Management, Wye Woods (Sept. 1987).

Member of Multiple Faculty Search Committees (1985-present).

In November 1995, I presented testimony before the United States Senate and House Committees on Small Business at a joint hearing on "Railroad Consolidation: Small Business Concerns."

In March 2004, I presented testimony to the U.S. House of Representatives Committee on Transportation and Infrastructure regarding railroad competition legislation.

In October 2005, I provided testimony to the Surface Transportation Board on the 25th Anniversary of the Staggers Rail Act of 1980.

**BEFORE THE
SURFACE TRANSPORTATION BOARD**

FINANCE DOCKET. NO. 35081

CANADIAN PACIFIC RAILWAY COMPANY, ET AL.

– CONTROL –

DAKOTA, MINNESOTA & EASTERN RAILROAD CORP., ET AL.

**COMMENTS OF THE KANSAS CITY SOUTHERN RAILWAY COMPANY AND
REQUEST FOR CONDITIONS**

EXHIBIT C

VERIFIED STATEMENT OF GEORGE C. WOODWARD

**BEFORE THE
SURFACE TRANSPORTATION BOARD**

FINANCE DOCKET. NO. 35081

CANADIAN PACIFIC RAILWAY COMPANY, ET AL.

– CONTROL –

DAKOTA, MINNESOTA & EASTERN RAILROAD CORP., ET AL.

**COMMENTS OF THE KANSAS CITY SOUTHERN RAILWAY COMPANY
AND REQUEST FOR CONDITIONS**

VERIFIED STATEMENT OF GEORGE C. WOODWARD

My name is George C. Woodward. I am an independent management consultant From 1991 until 2001, I was Senior Vice President-Chief Commercial Officer at ALK Technologies, Inc. ALK is the repository of the STB rail waybill sample and has developed information systems that enable rail carriers to analyze traffic flows. Prior to joining ALK, I was Executive Vice President-Distribution Services at Southern Pacific Transportation Co. from 1987-91, and Vice President-Marketing with Conrail from 1978-87. I have a B.S. in Physics from the Georgia Institute of Technology and an MBA with a major in Finance from the Wharton School of the University of Pennsylvania. Further qualifications are noted in the attached professional biography.

The purpose of my verified statement is to provide testimony regarding the likely adverse impacts of the proposed CPR-DME Transaction[1] upon The Kansas City Southern Railway Company ("KCSR") and its shippers. As I will explain in detail below, my analysis indicates that there are two wholly avoidable adverse consequences of the Transaction. First, the Transaction would harm certain KCSR-served grain shippers and receivers, and, second, it would undermine KCSR's ability to compete in an important NAFTA corridor. Specifically, without appropriate concessions from CPR or conditions from the STB, KCSR-served consumers of grain would lose currently efficient access to exceedingly important DME-served grain sources. In addition, due to its strategic relationship with the Union Pacific Railroad Company ("UP"), CPR would eliminate KCSR's haulage rights access to Chicago from Kansas City, and would not negotiate what would be, in the absence of CPR's overriding interests in its strategic CPR/UP alliance, mutually advantageous modifications to that haulage arrangement. As I have indicated and will explain below, my analysis of the Transaction confirms that these harms are very likely to occur, but I can see that there are available remedies to these harms that would not impede the overarching objectives of the Applicants.

I. DME IS THE ONLY REGIONAL RAILROAD CONNECTING WITH ALL SEVEN CLASS I RAILROADS; IT IS A "NEUTRAL" CARRIER

Given its size, territorial reach, and connections with all seven U.S. Class I railroads, DME is unique among regional railroads. DME's lines extend through

[1] I will refer to DM&E and IC&E, collectively, as "DME," just as was done in the subject railroad control application ("Application") filed with the Board in STB Finance Docket No. 35081. I intend in my statement to employ terminology in a manner consistent with the Application. Accordingly, I will use the term "DME" as explained above, and, to the extent that I use other terms such as "Transaction," "Applicants," etc., I use them in the same way that they are used in the Application.

important agricultural areas of the Upper Midwest and Northern Plains States, including the key Midwestern agricultural markets of Iowa, South Dakota, Illinois, Minnesota, and Missouri.[2] DME's lines also link the key U.S. rail gateways of Chicago, Kansas City, and the Twin Cities of Minneapolis and St. Paul, and connect to facilities located along the Mississippi River. DME's system interconnects with western Class I railroads UP and BNSF Railway Company ("BNSF") at several locations, including Chicago and numerous locations north and west of Chicago. In addition, due to the historic connection between DME's IC&E lines and CPR, DME has interline ties with CPR, particularly at Chicago and the Twin Cities (Minneapolis/St.Paul).

At DME's southern terminus, Kansas City, DME connects with KCSR, Norfolk Southern Railway Company ("NS"), UP, and BNSF. DME connects with Canadian National Railway ("CN") in the Chicago terminal area, and at points west of Chicago, such as Rockford, IL, and Dubuque, IA. Finally, DME's route to Chicago affords DME connections to all six U.S. Class I railroads operating there – BNSF, CN, CP, NS, UP, and CSX Transportation ("CSX") – and several terminal and short line railroads operating in the Chicago area. No other non-Class I railroad boasts such an extensive route network, wealth of interline connections, or access to key interline gateways. It is no surprise that the STB has deemed the Transaction "significant" under its rules. Due to its size and scope, DME handles local traffic (traffic that both originates and terminates on its own lines) and it participates in a large amount of traffic moved in cooperation with connecting carriers like BNSF, CP, CSX, NS, and KCSR. DME's participatory revenues for all traffic were in excess of [redacted] in 2006 (and may

[2] The multi-state region in which DME operates accounts for over 50% of all U S corn production.

even be greater due to CP and CN lack of reporting to the STB waybill sample for Canadian terminated traffic.) The combined DME did not derive from a single Class I railroad spinoff, and, as a consequence, DME is far more than a regional feeder of traffic to a single "patron" Class I railroad, as is often the case for smaller railroads. Rather, DME is widely recognized as an independent[3] and neutral regional rail "hub" system, which may alternate between competing and partnering with the same Class I railroad depending upon the circumstances.

I have examined DME traffic flows, and, in particular, its interline traffic flows with connecting Class I carriers. In connection with that undertaking, I have also examined the traffic flows of CPR, with a particular focus on CPR's interline traffic movements with its alliance partner UP. In so doing, I have noted that DME traffic patterns reinforce the proposition that DME is truly a "neutral" carrier whose market focus is attuned to finding the best and most economical options and markets for its customers. While DME faces significant competition from the other carriers that surround it (particularly, but not exclusively, BNSF, UP, and CPR), depending upon the commodity and the destination/origination markets, it is just as often a competitor with BNSF, UP, and CPR as it is a partner with these three carriers.

For example, my traffic analysis discloses that DME-originated grain moves to Pacific Coast export markets via BNSF interline service to the Port of Seattle. DME-

[3] One need not look any further than DME's ongoing efforts to extend its route westward to tap the coal fields of Wyoming's Powder River Basin for solid evidence of DME's independence from, and desire to compete with, the western Class I railroads that surround it. See Dakota, Minnesota & Eastern Railroad Corporation Construction Into The Powder River Basin, STB Finance Docket No. 33407.

BNSF export grain flows compete with CPR-originated U S. domestic grain, which is almost entirely interchanged with UP at the Kingsgate, BC/Eastport, ID, gateway[4] for handling to export terminals at Portland, OR and Seattle, WA. However, while DME is BNSF's partner – and UP's and CPR's competitor – for export grain flows to the Pacific Coast, the situation is different elsewhere. For example, DME and UP are partners in the movement of DME-originated grain moving to UP served points in Iowa, Kansas, and Missouri. In addition, DME interlines grain with CSX, which moves to NS-competitive markets in Georgia, but DME also moves grain in interline service with NS to CSX-competitive destinations in Georgia. The conclusion of my traffic analysis is that DME is not preternaturally inclined to favor interline relationships with any one carrier or group of carriers. Rather, DME's traffic flow relationships appear to be highly pragmatic and case-by-case, and, as a result, provide numerous competitive alternatives for its shippers.

Attached as Exhibit 1 is a traffic flow map showing all DME local and participatory traffic for 2006 with all connecting carriers color-coded to show their respective participatory revenues in the legend. Exhibit 1 illustrates that DME is not partial to any one carrier, but seeks out revenue opportunities and competitive alternatives for its customers with all major interline railroads with which it connects.

Now, CPR proposes to acquire the DME system and integrate DME traffic flows into CPR's system in a manner consistent with CPR's individual market objectives, revenue strategies, and the CPR/UP interline traffic alliance. This will have a significant

[4] The "Kingsgate Gateway" is a strategic interchange point for UP and CPR. Under the so-called CanAm West alliance agreement, CPR and UP route traffic between western Canada and the western and south-central U.S. and Mexico via this gateway. My traffic analysis suggests that CPR-to-UP traffic flows for grain originating on CPR's (Soo Line) routes also moves in accordance with this CPR/UP CanAm agreement.

impact on DME traffic flows, DME's current interline partnerships, and the competitive options of shipper and receivers who ship and/or receive traffic via DME.

[Exhibit 1: REDACTED]

II. THE COMPETITIVE IMPACTS OF THE PROPOSED CP-DME TRANSACTION SHOULD BE EVALUATED IN THE CONTEXT OF THE COMPREHENSIVE CPR/UP TRAFFIC ALLIANCE

Since at least 2001, CPR and UP have participated in a comprehensive traffic alliance under which each carrier views the other as a "preferred partner" with respect to the pricing and solicitation of interline traffic flowing in three geographic "corridors" between and among the U.S., Canada and Mexico.[5] According to CPR, "[j]oint CPR/UP

[5] It is my understanding that the CPR/UP traffic alliance – now generally known as the "CanAm" alliance – may have developed, at least in part, in response to the proposed, but

teams oversee the operations of the Can-Am corridors and make strategic decisions with respect to operations, marketing, technology, and investment."[6] A chief objective of this CPR/UP alliance is to facilitate the flow of traffic that may be considered "NAFTA traffic" (that is, traffic flowing between and among the U.S., Canada and Mexico), and to ensure that both carriers work together to compete against alternative NAFTA-oriented transportation services.

Under CanAm, CPR and UP have been exploiting the network synergies of their combined systems and have been benefiting from the commercial favoritism of a comprehensive traffic solicitation, pricing and operating alliance.[7] So close is the CPR/UP strategic relationship that, in 2001, John Koraleski, UP's Executive Vice President – Marketing and Sales, declared, "We are two railroads thinking of ourselves as one." "Turning a Corner," Railway Age, October 2001.[8] Given such strategic ties and the advantages that CPR gains from this arrangement, it is extremely likely that CPR and UP will revisit their alliance relationship to capture the traffic flow opportunities presented by CPR's proposed acquisition of control of DME. In short, the Transaction will have competitive impacts well beyond the bounds of CPR's own system; the impacts

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ultimately aborted, formal consolidation of the BNSF and CN systems, and the STB "moratorium" on mergers imposed in response to the proposed BNSF-CN combination. I also understand that CPR and UP may have contemplated that the alliance could form the foundation for a formal merger, had BNSF and CN proceeded with their consolidation plans. Based upon UP's position in the STB's major railroad consolidation rulemaking proceeding – Major Rail Consolidation Procedures, 5 S.T.B. 539 (2001) – it appears, however, that UP prefers not to pursue a merger with CPR or with any other carrier.

[6] Canadian Pacific Railway 2006 Corporate Profile and Fact Book ("CPR 2006 Fact Book") at 44 (available at http://www8.cpr.ca/cms/English/Investors/Fact+Book/default.htm).

[7] CPR 2006 Fact Book ("CPR 2006 Fact Book") at 44-45.

[8] Available at http://www.railwayage.com/oct01/cprail.html.

of the Transaction will be shaped by the collective competitive interests of CPR and UP, and the Board should evaluate the Transaction with the CPR/UP alliance in mind.

In fact, owing in no small measure to the CanAm alliance, UP dominates NAFTA traffic flows to and from virtually every U.S.-Mexico rail gateway, including Laredo, Eagle Pass, El Paso and Brownsville. It is estimated that UP, with the cooperation of its alliance partner, CPR, may control over 80% of the important international rail traffic flow between and among the U.S., Canada, and Mexico. One of the reasons that UP may enjoy over 80% of the traffic in the market is that it operates and markets the only single-line rail service between Chicago and the primary interchange location with Mexico – Laredo, TX. UP's CPR-augmented dominance of NAFTA traffic, particularly traffic to and from Mexico, is highlighted in Exhibit 2, below, which shows UP's overwhelming market share of U.S.-Mexico rail flows.

Exhibit 2 also reflects the importance of the Chicago gateway in the UP/CPR alliance service offerings, particularly with respect to traffic flows between, on the one hand, CPR-served points in eastern Canada and the northeastern U.S. and, on the other, UP-served points in the western and south-central U.S. and the Mexican gateways of Laredo and Eagle Pass. My examination of publicly-available CPR materials indicates that the CanAm alliance governs the movement of CPR/UP traffic through Chicago that originates or terminates in eastern Canada and on the U.S. lines of CPR's Delaware and Hudson Railway Company, Inc., subsidiary. Thus, the alliance covers the entire CPR network. It is therefore predictable that CPR will integrate its to-be-acquired DME properties into the CanAm alliance framework, commercially benefit from the leverage of the critical mass of the CPR/UP traffic alliance, favor and promote traffic flows in cooperation with UP, and discourage service offerings competıng with CPR/UP services.

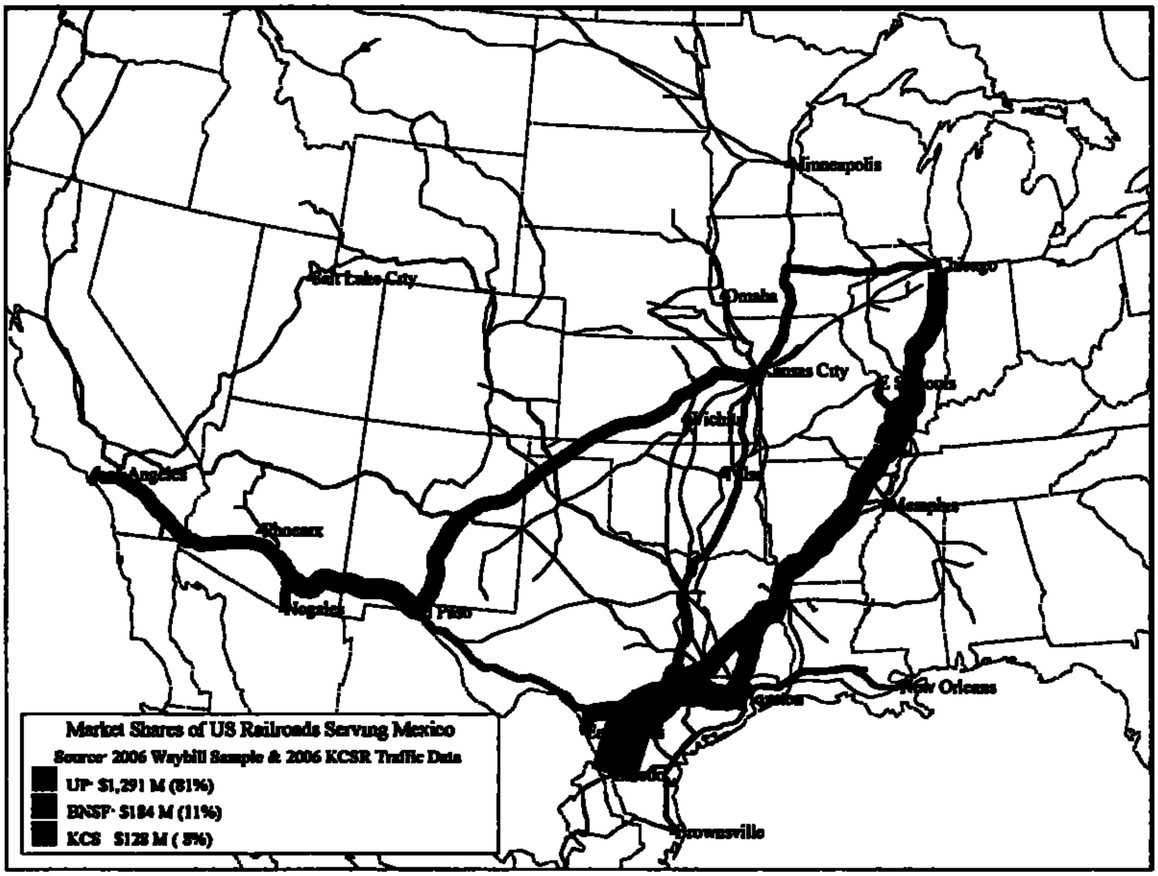

Exhibit 2: Market Shares of U.S. Railroads Serving Mexico

The CPR/UP alliance has been effective in growing the volume and revenue of the interlıne traffic of both particıpatıng raılroads. Interlıne traffic between CPR and UP has grown consıderably as NAFTA traffic flows have mounted. Exhıbit 3, below, demonstrates how CPR-UP interline traffic has grown since the advent of thc CPR/UP CanAm allıance. Thıs exhibıt draws a comparıson between allıance-orıented annual ınterline traffic volume growth for UP and for CPR from 2000 through 2006 and, separately, the annual traffic volume growth that each company has experıenced *excludıng* CPR-UP interlinc traffic. Exhibit 3 demonstrates that CPR/UP ınterline alliance traffic volume growth rate has significantly exceeded overall other traffic growth rate of each of these railroads.

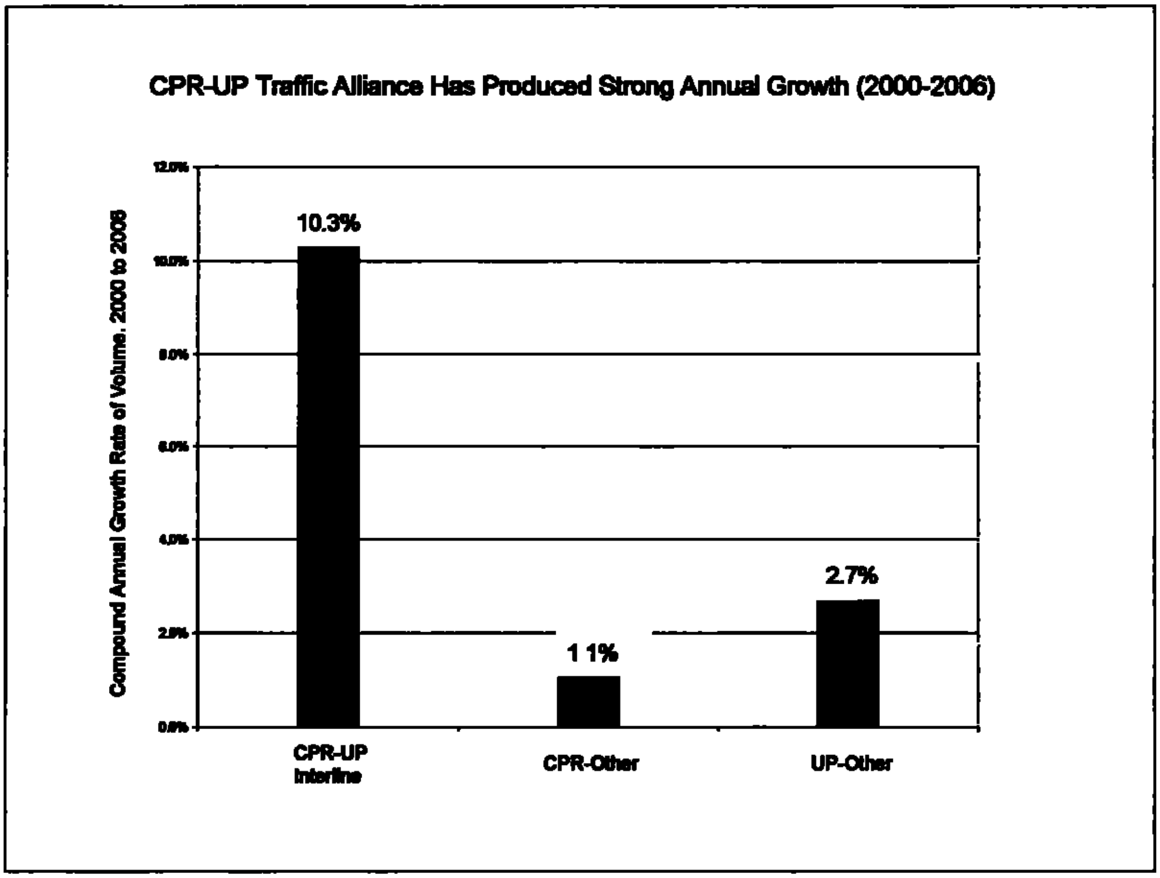

Exhibit 3: CPR-UP Traffic Alliance Has Produced Strong Annual Growth (2000 to 2006)

Exhibit 3 clearly illustrates the traffic growth impact of the CPR/UP traffic alliance, and it suggests the importance of the alliance to CPR's and UP's respective strategic planning and marketing initiatives since it allows both CPR and UP to leverage alliance interline traffic with non-alliance traffic. It also reinforces the proposition articulated by UP's Mr. Koraleski that UP and CPR are indeed two railroads that think of themselves as one. Because CPR and UP do think of themselves as one, it is important that the proposed Transaction be evaluated with that proposition in mind. My statement discusses the harms to competition that will flow from the proposed Transaction, taking into account the CPR/UP traffic alliance and its likely influence on future traffic flows from DME lines and on historic relationships between DME and its interline partners. In evaluating such impacts in this context, I have been able to identify key competitive markets as well as the locations of shippers and receivers who will be adversely affected by the Transaction, unless appropriate remedial conditions are imposed. Such adverse impacts of the proposed Transaction are discussed below.

III. CPR WILL ADJUST DME TRAFFIC FLOWS TO MAXIMIZE CPR'S REVENUES AND CONTRIBUTIONS TO THE DETRIMENT OF GRAIN BUYERS AND RECEIVERS IN CERTAIN U.S. GRAIN MARKETS

Because I have been retained specifically to investigate and to testify in this proceeding regarding possible adverse impacts of the Transaction on KCSR and its customers, I have, among other things, focused upon traditional DME-KCSR traffic flows that would be threatened. In addition, I have assessed, and will comment upon here, why CPR will likely manipulate historic DME traffic flows to promote CPR single-line hauls and longer-haul CPR/UP alliance routes. In short, I have determined that, following the Transaction, CPR is likely to take steps to divert DME-originated grain traffic away from KCSR-served grain purchasers and receivers located in the south-central U.S. in favor of hauls that would garner more revenue for CPR, either by itself or in partnership with UP.

Exhibit 4, below, shows the current price levels and volumes for various grain export and domestic markets. The exhibit illustrates the average lengths of haul for carload grain movements and per-car revenues. Not surprisingly, per car revenues generally increase relative to length of haul. Again, this exhibit shows why CPR would have an economic incentive to divert traffic to longer haul export markets and that the rail transportation price levels are within the range to make it feasible to divert grain from domestic receivers served by KCSR to export markets.

[Exhibit 4: REDACTED]

As background, KCSR-served feed mills located in the south-central U.S. which receives on average over 12,000 carloads of DME-origin grain annually. These KCSR-served grain consumers receive DME-origin carloads pursuant to a pricing and service (haulage) agreement[9] between DME and KCSR. KCSR has informed me that it has made significant long-term investments in line capacity, motive power and freight car

[9] I will refer to the DME-KCSR grain haulage agreement as the "Grain Agreement."

fleets[10] to enable it to transport DME-originated grain to receivers in the south-central United States.

Under its current terms, the Grain Agreement will expire within the next ten years. Recognizing the mutual advantages of the Grain Agreement, KCSR had initiated negotiations with DME for an extension of the Grain Agreement as well as the addition of service guarantees and penalties for violating these guarantees. These changes would have not only preserved existing shipper benefits but also would have allowed for a contract time frame that better reflects the long-lived assets that KCSR has committed and are necessary (motive power, freight cars, line capacity) to ensure the reliable and efficient flow of grain to KCSR's grain consumers.

[Exhibit 5: REDACTED]

10 [redacted]

Exhibit 5, above, depicts – (1) the location of KCSR-served grain consumers that purchase DME-originated grain transported under the Grain Agreement, and (2) the annual number of DME-originated grain carloads transported to each such grain buyer. In turn, I have identified and assessed potential alternative markets where CPR could divert formerly neutral DME-originated grain currently destined to KCSR-served receivers to other destination markets.

A. In order to secure lucrative hauls for DME-originated grain, CPR will favor longer interline grain routings with its alliance partner, UP, rather than interline routings with KCSR

As noted above, CPR's service and marketing activities do not take place in a strategic vacuum. Far from being a neutral player in interline traffic flows, CPR seeks out longer haul opportunities that further the objectives of the CPR/UP alliance. For example, with respect to grain originating on CPR's lines in the U.S., such traffic is predominantly routed in interline service with UP, via the "Kingsgate Gateway," to Pacific Coast export facilities at Portland, OR, and Seattle, WA. This traffic data indicates that, in the event that CPR is unable for any reason to secure DME-origin grain flows to CPR-served Pacific Coast export terminals such as Vancouver, BC (which possibility I will discuss below), CPR will opt to pursue the next-best thing – moving grain for Pacific Coast export in interline service with UP via Kingsgate.[11] Such a CPR-

[11] As stated in the Applicants' market analysis, "CPR's corn business is almost entirely export traffic ... 95% of all CPR U.S. originated corn is exported (via Pacific Northwest terminals) and only 5 percent moves to domestic end users. By contrast 60 percent of DME's corn is delivered to domestic destinations. Likewise, 90 percent of CPR's U.S. soybean traffic is exported, whereas 75 percent of DME's soybean shipments are domestic movements." CPR-2 /DME-2 Market Analysis-Exhibit 12, page 8. This statement demonstrates CPR's preference to route grain for Pacific Coast export in order to maximize revenue and contribution, as opposed to routing it to domestic markets.

UP alliance interline routing would still provide for a substantially longer haul for CPR than DME currently supplies for DME-originated grain moving to KCSR at Kansas City.

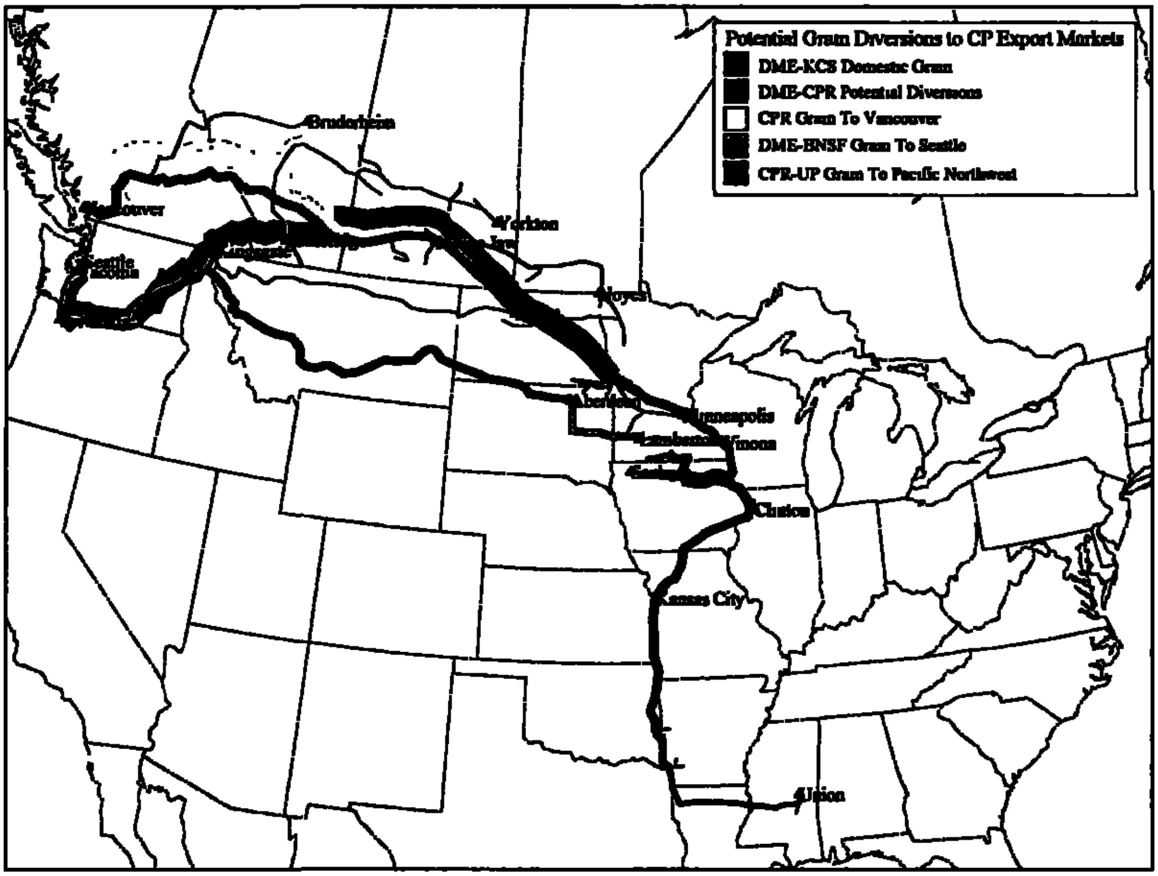

Exhibit 6: Potential Grain Diversions to CP Export Markets

Because of CPR's strategic preferences, it is highly likely that DME-originated grain now headed to domestic consumers, including grain consumers located on KCSR, would be the target of CPR/UP alliance-oriented diversion to U.S. Pacific Coast export facilities. As shown in Exhibit 6, some DME-origin grain already moves to the Pacific Coast for export, but does so in DME-BNSF interline service.[12] Absent an agreement between CPR and BNSF that will ensure BNSF's continued role in such interline grain

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[12] As I have demonstrated in Exhibit 4, above, and in my analysis generally, long-haul export grain traffic moves such as those that BNSF and DME are participating in jointly are quite attractive.

service post-Transaction (a development that may have been negotiated so as to assure BNSF's non-opposition to the Application), such DME-BNSF grain traffic would be an obvious target for CPR-UP diversion following consummation of the Transaction. If BNSF has been able to secure its future role in interline transportation of DME-origin grain to Pacific Coast export, then shorter haul, interline grain traffic will be a special target for diversion in the nearer term. In such a case, however, CPR would have to pursue possible grain export volumes not committed to BNSF, and DME-origin grain to KCSR destinations would appear to be the "low-hanging fruit."

Just as it could do to maximize possible longer single-line hauls (discussed below), CPR could take steps to promote longer haul CPR/UP export grain flows that would undercut DME-KCSR grain traffic movements. Specifically, even if it is unable for whatever reason to terminate the Grain Agreement in the nearer term, CPR could cause its haulage services under that agreement to deteriorate to such a degree that the service would become too inefficient and costly to KCSR and too unreliable and/or too expensive for KCSR's customers.[13] I understand that the Grain Agreement lacks strict performance standards or tough penalties in the event that DME's (potentially, in the future, an integral part of CPR's) service were allowed to deteriorate measurably. Accordingly, there would be a strong incentive for CPR to purposely allow KCSR haulage service to deteriorate (to the detriment of KCSR-served grain consumers), and

[13] As mentioned above, I understand that KCSR [redacted] If that were to occur, KCSR would have either to absorb such increased costs or it would have to adjust its service prices to the customers currently benefiting from DME's and KCSR's respective commitments to the Grain Agreement.

considerable upside if, in so doing, CPR can re-direct such grain to potentially more lucrative longer haul export markets through its alliance with UP, or on its own. Thus, even if the Grain Agreement were to survive the Transaction, there is little to deter CPR from rendering that agreement useless, unless stronger performance provisions were to be added that would ensure that CPR did not engage in purposeful, systematic haulage service deterioration.

Regardless of whether motivated by its pursuit of longer single-line grain hauls or by its efforts to promote longer movements under its alliance with UP – or even to change the routing of the existing DME-BNSF agreement flows, so that CPR gains a longer haul – I have shown that CPR has, on balance, very strong incentives to target domestic interline grain flows, such as those handled with KCSR under the Grain Agreement, for diversion. Such a consequence of the Transaction will be a significant disadvantage for the KCSR-served grain consumers in who rely heavily upon DME-KCSR grain flows and derive such substantial benefits from highly efficient access to reasonably-priced grain from DME sources. The effective loss of economical access to DME-sourced grain would be thoroughly disruptive and potentially catastrophic due to the lack of readily available alternative sources through KCSR interline service with other carriers.

The Transaction-related harms that would otherwise befall KCSR-served grain consumers could and will be avoided if CPR would make the necessary commitments to ensure the continued availability of DME-KCSR grain routings, or, should CPR refuse to do so, if the STB would condition its approval of the Transaction upon protecting such flows. A reasonable remedy would be a long-term extension of the Grain Agreement along with more rigorous performance standards to ensure that CPR would not evade its obligations under the agreement through purposeful service deterioration. Such a remedy would reflect the term of the investments that KCSR has made (and will continue to make) for the benefit of grain receivers located on its lines, and would ensure that KCSR's shippers, who rely so extensively on DME-sourced grain, do not face the loss of such a critical and advantageous grain source.

B. If possible, CPR will look to increase its revenues and contribution on DME-origin grain traffic by preferentially pricing traffic flows to longer-haul markets in CPR single line service and away from interline routings with KCSR

[Exhibit 7: REDACTED]

Exhibit 7 shows again that CPR would be economically motivated to push DME-origin grain to more distant markets in order to increase CPR's revenue opportunities. As the chart demonstrates, CPR and other railroads also depicted in the chart garner comparatively higher overall revenues for the transportation of grain to export via Pacific Coast ports such as Vancouver, Portland and Seattle. This exhibit also indicates that, ideally, the greatest post Transaction contribution potential for CPR would be to divert DME-origin grain to CPR-served Pacific Coast ports for export to Pacific Rim countries. In 2005, for example, CPR transported approximately [redacted] carloads of grain to export facilities in Vancouver, earning freight revenues of over [redacted] annually.

In light of these economic circumstances, CPR, like any other profit-maximizing firm, is quite likely to examine how it can adjust prices and service to guide DME grain originations to the most lucrative hauls for CPR, which, as my investigation has shown, would be, ideally, moving this grain in CPR single-line service to the Pacific Coast for export to Pacific Rim consumers. Such a preference would arise despite evidence to show that hauls to domestic grain consumers such as those located on KCSR's lines may be no less efficient, but comparatively less remunerative, than longer hauls to the Pacific Coast.[14] To so divert DME grain flows, I also would expect CPR to adjust rates for DME traffic simultaneously to encourage export hauls and to discourage shorter hauls to domestic grain consumers. Just as it would do to promote CPR-UP interline moves of grain to U.S. Pacific Coast export facilities, I would expect CPR concurrently to evaluate its traffic agreements with other railroads to see which such agreements could impede

[14] As further evidence of CPR's likely financial incentives to divert grain traffic, in 2005, as I have mentioned before, DME and KCSR together handled approximately 12,000 carloads of grain on average to receivers in the south-central U.S. markets pursuant to the terms of the Grain Agreement The total combined revenue for this traffic was approximately [redacted] from total per car rates of about [redacted] DME received approximately [redacted] per carload and KCS approximately [redacted] To move this same grain traffic in post-Transaction single-line service to Vancouver, CPR could earn revenue of [redacted] per carload and contribution of [redacted] per carload (Exhibit 7).

CPR's Pacific Coast export traffic opportunities.[15] Those agreements that could be terminated in the short term likely would be, and, for those that cannot be terminated, CPR would probably explore other ways to discourage their continued use by reduced service levels.

Exhibit 6, which I discussed in the preceding section of my statement, shows, among other things, the single-line service route over which DME-originated grain could be diverted away from KCSR domestic consumers and to CP-served Pacific Coast export facilities. That map shows that a post Transaction all-CPR route for DME-originated grain to Vancouver is roughly comparable to existing DME-BNSF export grain routings, which underscores again, in my view, the feasibility of grain diversions away from domestic consumers.

C. Additional grain diversions to other CPR/UP alliance destinations are likely, further disadvantaging KCSR-served receivers

As noted throughout above, due to the comprehensive CPR/UP traffic alliance, CPR and UP assure each other a preferred position when jointly developing interline traffic. Again, as noted throughout above, CPR and UP will attempt to maximize CPR-UP interline traffic opportunities over other CPR and UP interline traffic options. Evidence of this includes the interline movement of CP/Soo-origin grain moving from sources in the U.S. in long haul service with UP to the ports of Portland and Seattle, and, of course, more generally, the CanAm traffic flows. Such preferences would most likely

[15] I have determined that DME originates grain which it interchanges with BNSF for export through the Port of Seattle. (My research indicates that total per car revenues for such movements are about [redacted] As with DME-KCSR traffic handled under the Grain Agreement, this traffic, as previously noted, is potentially divertible grain traffic, which CPR might seek either to transport in single-line service to Vancouver or to divert to a route favoring CPR and its CanAm alliance partner UP.

extend to DME traffic, should CPR acquire control of DME. Thus, beyond the Pacific Coast export market opportunities I have discussed above, CPR and UP may, in accordance with the general objectives of their traffic alliance, look to secure CPR(DME)-UP traffic flows to UP-served points south of Kansas City at the expense of traffic currently moving in interline service with other carriers such as KCSR. Under this scenario also, the CPR/UP alliance, as applied to DME traffic, would influence new CPR(DME)-UP interline traffic flows to points south of Kansas City, which would likely be favored over existing interline movements with KCSR.

Although I do not believe that CPR(DME)-UP interline grain traffic flows to UP-served destinations south of Kansas City (such as points in Arkansas, Louisiana, Texas, and/or export facilities along the Gulf Coast) would be as appealing as long haul grain traffic opportunities to the Pacific Coast export markets, it is nevertheless likely that CPR would prefer to undertake such southerly grain traffic flows with UP rather than non-alliance interline carriers. Thus, I anticipate that, after the Transaction, to the extent CPR and UP recognize market demand for grain to move to UP-served receivers in Arkansas, for example, CPR and UP will look to meet such demand by diverting traffic away from other interline grain flows in the same general direction, including interline grain traffic flows from DME points to KCSR-served customers located in the general vicinity of UP's customers. After the Transaction, KCSR-served receivers who acquire grain from DME-origins will have difficulty obtaining volumes from DME sources, because CPR would look to preferentially price DME grain traffic to enable it to move via CPR's alliance partner, UP, either to domestic destinations west or south of Kansas City or to

UP-served Gulf Coast export facilities (and thence to markets in Europe and South America).

Finally, just as it would be inclined to do to promote longer haul CPR/UP alliance flows and single-line CPR hauls for grain, CPR would look to ways to discourage the movement of traffic via the Grain Agreement, should CPR perceive that it would benefit more from moving grain to southern feedlots in cooperation with UP. In the sections above, I have noted that, wherever CPR finds that the Grain Agreement would conflict with CPR's profit opportunities for moving grain to non-KCSR-served destinations, CPR would look for ways to undermine the effectiveness of the Grain Agreement service by permitting service levels to decline

In any case, whether CPR looks to divert DME grain to Pacific Coast export markets in cooperation with its alliance partner UP, pursues such opportunities in CPR single-line service through the port of Vancouver, or partners with UP in moving such grain to UP-served domestic consumers to the south of Kansas City (or to export facilities along the Gulf Coast), KCSR served shippers and receivers are very likely to be given short shrift. In the absence of an extension of the Grain Agreement (and modification of that agreement to assure adequate CPR service post Transaction), KCSR-served grain receivers that benefit from the Grain Agreement would face significant disruption in their customary source markets. Such KCSR-served shippers are likely face commercial pressure in attempting to find alternate sources of grain, for which it is quite possible they will have to pay higher prices. I understand that KCSR will offer additional testimony in connection with its Comments to demonstrate how KCSR-served grain shippers and receivers would be hurt by post Transaction diversions of DME-origin grain that, as I have indicated above, could occur under any one or more of the three scenarios set forth in Section III of my statement.

IV. CPR SHOULD NOT BE PERMITTED TO ADVERSELY AFFECT COMPETITION IN NAFTA TRAFFIC FLOWS THROUGH CHICAGO BY UNDERCUTTING KCSR

I have thus far discussed the Transaction-related harms that would result from changes to grain traffic flows and the importance of an extended (and strengthened) Grain Agreement as a remedial measure, but the Grain Agreement is not the only pro-competitive KCSR-DME agreement threatened by the Transaction. DME and KCSR also have a contract under which DME has agreed to provide certain haulage services for KCSR between Kansas City and Chicago (the "Chicago Agreement"). Although I understand that traffic is not currently moving pursuant to the Chicago Agreement, this instrument nevertheless serves as a competitive counterbalance for UP single-line service traffic flows in the Mexico-to-Chicago NAFTA corridor. Given UP's marked dominance in such NAFTA traffic flows (see Exhibit 2, above), it is important that shippers have available to them service alternatives that can constrain UP's apparent market power in this corridor.

The existence of the Chicago Agreement keeps available to shippers a KCSR Laredo-Chicago service alternative that otherwise would not exist. Moreover, the Chicago Agreement is also a reflection of DME's willingness to serve as a partner to KCSR in facilitating Mexico-Chicago traffic flows, and, but for the proposed Transaction, could quite possibly have served as the precursor to a broader-based KCSR-DME arrangement that would have intensified competition in this corridor. The Transaction will change all of that, most likely precluding any further agreements designed as an alternative to UP single-line service (the only single-line route in the important Chicago-Laredo NAFTA corridor), and probably also resulting in the complete elimination of the Chicago Agreement itself. It is impossible to see this consequence of the Transaction as anything but anti-competitive.

Here, too, the tight relationship between CPR and UP is the main factor behind why, without an appropriate concession from CPR or a condition from the Board, CPR will be motivated to terminate any agreement that preserves KCSR haulage rights access to Chicago, and to decline to negotiate any expanded rights for KCSR. In the preceding sections of my verified statement, I have discussed the CPR/UP traffic alliance, and have noted that one of the key NAFTA gateways for traffic moving pursuant to this alliance is Chicago. Given CPR's vested interest in promoting alliance-oriented NAFTA traffic flows, CPR would have no interest in arrangements that would aid a perceived competitor in this lane – KCSR. If KCSR should lose haulage access to Chicago, KCSR's ability to compete with CPR/UP in traffic flows through this gateway and Laredo is diminished and the already dominant CPR/UP alliance alternative is strengthened.

As with the Grain Agreement, there is an easy remedy to this anticompetitive consequence of the Transaction. CPR should be required to permanently to keep in place the Chicago Agreement, and CPR should also be required to negotiate modifications to that agreement to allow for the movement of all traffic under reasonable terms. Such a remedy would not only address CPR's increased ability to add to UP's dominance in Mexico-Chicago traffic flows through their alliance, but it will also ensure that shippers would continue to have available to them service alternatives that replicate those that UP is otherwise uniquely able to provide.

George C. Woodward, Managing Director

George C. Woodward is the Managing Director of Clouds Hill Capital, Inc. He founded Clouds Hill Capital with over fifteen years of strategic advisory experience. He focuses on strategic planning services; pricing and yield analysis, mergers and acquisitions and complex business negotiations that enhance corporate value. He has led assignments related to transportation and logistics, financial services, life sciences, equipment leasing and information technology.

Mr. Woodward was chief commercial officer at ALK Technologies, Inc., a transportation and logistics related information technology firm in Princeton, NJ, that provides merger and acquisition analytical services; decision support systems; computer mapping and in-vehicle navigation software. Mr. Woodward provided strategic advisory services for the successful privatization of the Mexican National Railways (FNM) by Kansas City Southern Industries and Transportación Ferroviaria Mexicana; the joint acquisition of Conrail by CSX and Norfolk Southern; Burlington Northern-Santa Fe merger; Canadian National-Illinois Central-Wisconsin Central mergers; and the Southern Pacific Union Pacific merger.

Mr. Woodward was Executive Vice President-Distribution Services for Southern Pacific Transportation Company, a California based intermodal transportation company focused on international trade between Asia and North America. In 1989 he was a member of the investment group that proposed a management-employee buyout of Southern Pacific. Prior to that he was Vice President-Marketing with Consolidated Rail Corporation in Philadelphia where he managed the overall business development and pricing efforts that contributed to Conrail's financial turnaround. He was a member of the senior management team that led the initial public offering of Conrail in 1987.

Mr. Woodward holds an MBA in Finance from The Wharton School of the University of Pennsylvania and a Bachelor of Science in Physics from the Georgia Institute of Technology. He is a graduate of the Advanced Management Program at Harvard Business School. He was formerly a Director and served on the audit and governance committees of IVANS, Inc., an insurance industry related information technology firm. He was also a Director of TTX Company, a transportation industry equipment-leasing firm. He is a Director of the Philadelphia Belt Line Railroad and President of the Board of Directors of the Intermodal Transportation Institute, an executive education program and public policy forum at the University of Denver.

VERIFICATION

I, George C. Woodward, declare under penalty of perjury that the foregoing statement is true and correct Further, I certify that I am qualified to file this Verified Statement. Executed this 4th day of March, 2008.

George C. Woodward

**BEFORE THE
SURFACE TRANSPORTATION BOARD**

FINANCE DOCKET. NO. 35081

CANADIAN PACIFIC RAILWAY COMPANY, ET AL.

– CONTROL –

DAKOTA, MINNESOTA & EASTERN RAILROAD CORP., ET AL.

**COMMENTS OF THE KANSAS CITY SOUTHERN RAILWAY COMPANY AND
REQUEST FOR CONDITIONS**

EXHIBIT D

VERIFIED STATEMENT OF THAD JONES

BEFORE THE
SURFACE TRANSPORTATION BOARD

FINANCE DOCKET NO. 35081

CANADIAN PACIFIC RAILWAY COMPANY, ET AL.
– CONTROL –
DAKOTA, MINNESOTA & EASTERN RAILROAD CORP., ET AL.

VERIFIED STATEMENT OF THAD JONES

My name is Thad Jones. I am President and Founder of AEFNA, LLC. After a 28 year career in the agriculture industry, where I gained management experience in grain merchandising, soybean processing, transportation, pork processing, corn wet milling, and vegetable oil usage and processing, I formed AEFNA LLC in 2005 to provide support to senior management in the agriculture, energy, and food sectors in North America. Immediately prior to forming AEFNA, I was Senior Vice President of Bunge North America, which is one of the nation's largest agribusiness firms, the world's largest oilseed processor and seller of bottled oil, and has corn dry milling, soybean and canola processing, and grain elevator interests in North America. I have a B.A. in economics from DePauw University. My full background and experience is attached as an appendix to this verified statement.

The purpose of my verified statement is to provide testimony regarding the likely adverse impacts of the proposed CP-DME Transaction[1] upon the grain elevators (shippers) located in the states of Iowa and Minnesota who ship grain, primarily corn, via DME/KCSR interline rail service

[1] I will refer to DM&E and IC&E, collectively, as "DME," just as was done in the subject railroad control application ("Application") filed with the Board in STB Finance Docket No. 35081. In addition, I intend in my statement to employ terminology in a manner consistent with the Application filed in this proceeding.

to various feed mills (receivers) in the south-central United States for use as feedstock in the poultry industry. I have also been asked to address the impact of the Transaction on the feed mills who are located on KCSR's lines in the states of Kansas, Oklahoma, Arkansas, and Mississippi and who are the buyers of the corn and pay the freight rate. As I explain I below, my analysis of the Transaction indicates that the shippers and receivers of DME/KCSR delivered corn are likely to see adverse competitive effects in the form of reduced market access for the shippers and higher prices for the receivers as a result of the Transaction.

I. THE GRAIN MARKETS ARE COMPLICATED AND TRANSPORTATION COSTS PLAY AN IMPORTANT ROLE

The North American grain trade is a vibrant active market consisting of an integral mix of futures and options, cash (physical) commodities, logistics, freight, and economies of scale that drive efficiency. For the past century, the supply lines have been focused on domestic and international food production through food processors and animal feed channels. Several macro economic factors influence the trading of cash grain in North America. Annual crop production and weather are key drivers of relative supply and demand economics as each crop year develops. Government policy is fundamental to land use management and crop planting decisions. International currency can also impact export and import demand and further drive ocean freight values.

Price Discovery

Price is a pivotal aspect of grain trading. On the one hand, it is an outcome of planting decisions, government policy, and weather. On the other hand, price drives planting and marketing decisions. The final delivered price of the grain paid by the elevator to the farmer or by the end user (in this case – the feed mills in the south-central United States) to the elevator is largely reflected by two main components: the per-bushel price of grain at the origin, which is typically pegged to the price traded at the Chicago Board of Trade, and the freight expense from origin to destination Together, these two key functions set prices across North America on a minute by minute, hourly, and daily schedule. Grain quality can also impact price, but is typically a small price indicator compared to freight and the Chicago Board of Trade underlying futures value. A buyer of grain will continually seek the lowest delivered price, and as noted, the transportation cost of getting the grain from the origin point to the destination point plays a critical role in that decision making process.

Getting Grain to Market/Price Setting and Basis

Grain is produced on farms of all sizes with various types of equipment. Each crop is harvested upon maturity. Upon harvesting, the grain is transported from the field and is stored in farmer owned bins, for eventual sale to the elevator, or is delivered from the field to elevator owned grain bins. The local price paid by the elevator to the producer (farmer) for grain is largely determined by the CBOT futures price, less applicable freight, to deliver the commodity to a CBOT warehouse. Thus, in the beginning stages of CBOT evolution and grain production, if the price at the CBOT was \$1 00 per bushel and the freight from Chicago to Des Moines, Iowa was \$.10 per bushel, the price for grain delivered to Des Moines would be S 90 per bushel (\$1.00 less S.10 freight per bushel), less handling costs, quality discounts, and a profit margin for the grain elevator.

Importantly, the CBOT and the freight cost together essentially defined the price of the grain at a given "local point." Accordingly, one can imagine all the various grain elevators and related freight expense from different geographics versus the CBOT delivery point(s) which were in the Chicago area. The difference between the CBOT futures price and the local price was determined to be the "basis." Today, the "basis" is a globally recognized methodology to relate pricing across an interwoven network of supply and demand points. The main component of the basis is freight expense.

Basis as Supply and Demand Indicator

The basis, while largely representing freight cost, also represents freight availability and local supply and demand indicators of relative value. Therefore, in the middle of fall harvest when supply lines are full and transportation is typically stressed, the basis typically trends lower In times of tight supply due to freight availability, diminished supply lines, logistical supply imbalances, or perhaps later in the crop season, the basis trends higher. The basis is used in trading grain and can be used in conjunction with truck, rail, barge, and ocean freight components. In some cases, the basis is used as a pricing mechanism for a direct shipment of physical grain. In other cases, a pricing point is formed by use of the basis. In some cases, physical goods may be shipped against the pricing point. In other cases, physical goods may be bought and sold against the pricing point; essentially using the pricing point as a physical hedge against expected purchase or sale of grain.

Grain Spreads

This need for flexibility in grain supply chains is constantly driven by interconnecting markets that have independent economic factors that drive decision making and profitability. For example, the drivers of ocean freight profitability likely are not the same as local truck profitability. Likewise the profit drivers for a large livestock integrator and meat processor, who require vast quantities of corn and feedstuffs, are not the same as a railroad. But nonetheless, every day and every year the markets interface and react with one another to harmonize the endless supply chain around the globe.

To a large extent the methodology to allow the grain markets to interface is the concept of "grain spreads" that are largely driven by freight values. For example a grain elevator in central Ohio may sell corn by truck to Toledo for eventual export, locally to a poultry or swine integrator, locally to an ethanol plant, or by rail to the southeast to additional large livestock integrators. In each situation a freight matrix exists with the "basis" that allows the elevator to determine the best sale price. The difference between all the different destinations is the "spread." Freight costs and local demand impact the basis. Therefore if a southeast buyer would like more corn from Ohio, they can raise the price they are willing to pay thereby impacting the "spread" against other potential destinations for that same corn. Likewise, if the local trucking concern would like more freight from a certain elevator, due to his truck profitability and routing matrix, the trucking company can lower local freight costs from the elevator, thereby raising the elevator's sales price, also impacting the local "spread" against the southeast.

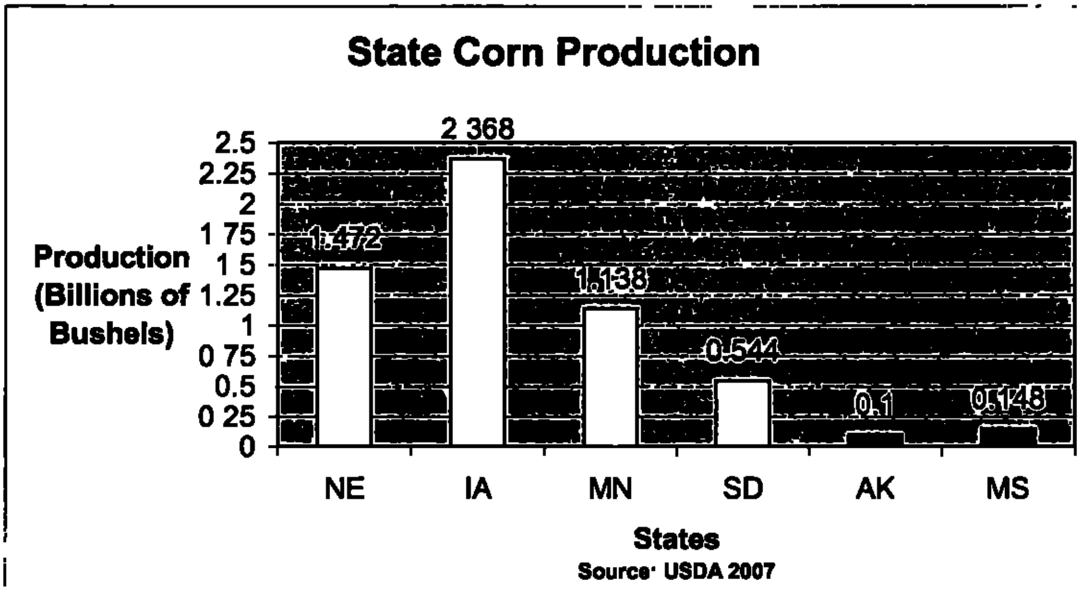
Railroads, acting independently, or with adjoining railroads, can also significantly alter the "spreads" between grain markets. The resulting impacts on local prices to farmers, and delivered prices to customers can be significant, and sometimes change the profitability of each. This is particularly the case when shippers and receivers are economically tied to just one railroad. Furthermore rail freight rates can directly impact grain flow patterns.

To understand this, one need only look at how the rail industry has changed its grain business over the past two decades. During this time, railroads have become oriented toward mainline corridor optimization. This has resulted in the sale of many underutilized branch lines to "short line railroads" and line abandonment in non economic areas. The railroads have also moved toward larger railroad car units of agricultural products. The era of "three car units" and "fifteen car blocks" has given way to "25's, 50's, 75's and 100 car units" that may include incentives and penalties for quick loading and unloading. Shippers or receivers can become disadvantaged with the sale or closure of branch lines or with changes in the railroad ownership structure. The trend toward larger unit sizes has required elevators and buyers to expend capital to accommodate the delivery and pricing mechanism or incur immediate economic disadvantages for those unable to expand.

Most railroads have an ongoing relationship with shippers and receivers and naturally want to service them. However like all companies in the grain supply matrix, the goal of each company in each segment of the supply chain is to make money and often times in the grain trade, the single point shipper and receiver has been at a disadvantage to the railroad's goal of profit enhancement. In many cases rail related pricing and routing decisions have impacted grain spreads and the "directional flow" of grain.

II. THE TRANSACTION WILL CHANGE THE ECONOMIC FACTORS OF DME ORIGINATED GRAIN TO THE DETRIMENT OF KCSR SERVED FEED MILLS IN THE SOUTH-CENTRAL UNITED STATES

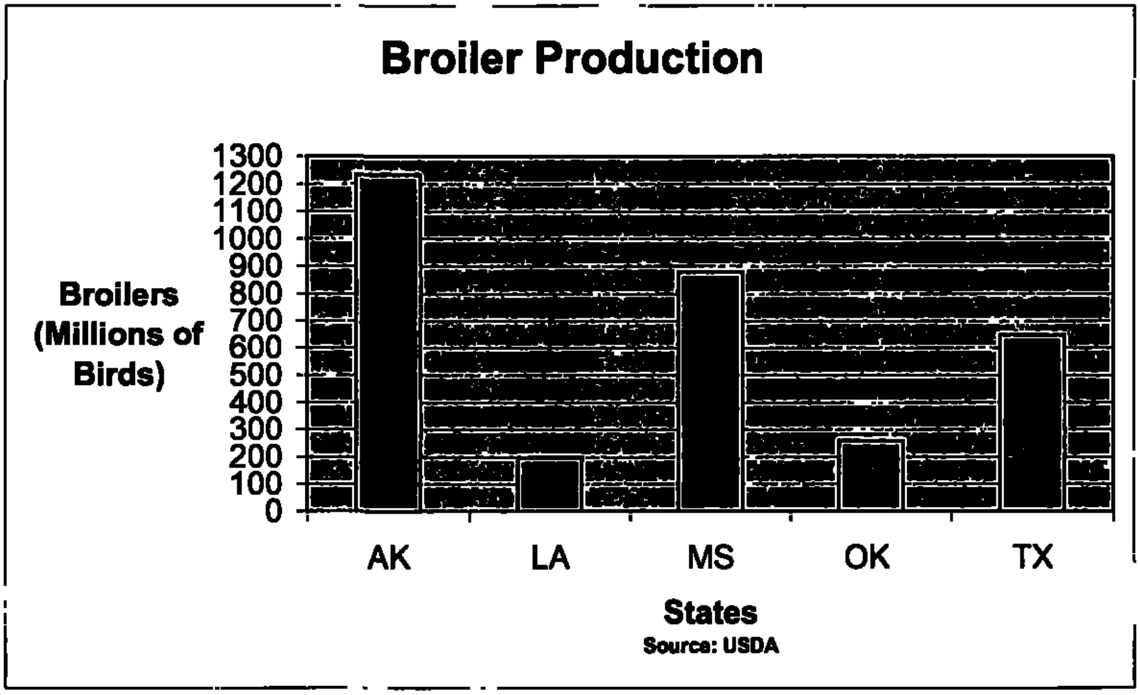
One of the primary commodity movements on all of railroads involved in the Transaction is grain and related feedstuffs Corn is the primary agriculture product involved. As shown in the chart below, corn production from the three key DM&E and IC&E served states represents approximately 30 % of the total corn production in the U.S. In 2007 these three states, South Dakota, Minnesota, and Iowa, produced 4 Billion bushels of corn out of the total 13 Billion produced in all of the United States Neighboring Nebraska, not directly served by the DM&E or IC&E, but an important source of grain for KCSR movements to Mexico, produced 1.4 billion bushels, over 10 % of the total U.S. crop Collectively, the four states can produce approximately 40 % of the entire U.S. corn production in a given year.



Also of note on the above chart is corn production in the two states of Arkansas and Mississippi, which are two of the primary destination markets for DME/KCSR routed corn. These two states are net importers of corn. Iowa and Minnesota provide a substantial amount of corn to feed mills in Kansas, Oklahoma, Arkansas, and Mississippi (as well as other south-central states) for use as feed for the large poultry industry that is a mainstay of the south central U.S. agricultural economy and a large provider of cost efficient poultry products in the U.S. retail food and foodservice industries.

Broiler Production

The south central portions of the U.S. have been large poultry (referred to in the trade as "Broilers") producing states for a long time. As a result, certain grain flow patterns have developed and these patterns have largely been uninterrupted, predominately allowing corn from the large production states in the northern U.S. to move efficiently to the south for livestock feed. As depicted in the chart below, Arkansas and Mississippi are two of the very largest states in broiler production. These two states are served by the KCSR and have benefited by the common grain tariff pricing structure that exists between the DME and KCSR which allows for the KCSR equipment to efficiently gather corn from the key corn producing states on the DME and deliver it to Arkansas and Mississippi on KCSR lines.

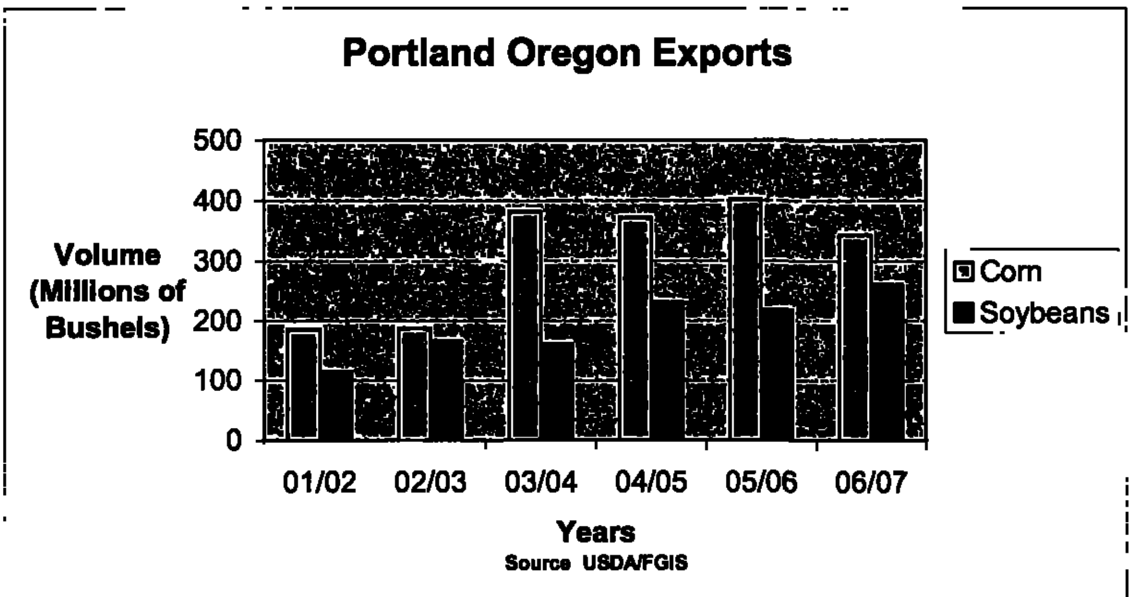


Indeed, based upon what other witnesses have told me, it is my understanding that virtually all of the DME originated grain that is interlined with KCSR is delivered to KCSR served feed mills that serve the poultry markets in these south-central states and that the feed mills in Kansas, Oklahoma, and Arkansas depend upon this DME originated grain as the primary source of rail delivered feedstock. This indicates to me that the lowest delivered price of corn to these feed mills is via the DME/KCSR rail option, and that if such feed mills had to obtain their primary source of non local corn from other origins, they would end up paying more.

Competing Markets

Although these feed mills have been able to secure grain via the DME/KCSR routings from DME origins in Iowa and Minnesota to their south-central locations, these feed mills are competing with other destinations (i.e. buyers/receivers at other destinations) for Upper Midwest originated corn. In fact, one of the largest export ports in the world is immediately south of the region and is the U.S. Gulf Coast. These large export facilities are huge buyers of corn and other grain and typically over 50 % of the U.S. exported grain annually is shipped through these ports.

Likewise to the Pacific Northwest is a series of export facilities spanning from Portland Oregon to Seattle Washington, and northward to Vancouver, British Columbia, Canada. Collectively referenced as the Pacific Northwest, or "PNW," these terminals source grain from the upper U.S. Midwest and the western Canadian provinces for eventual export through the PNW terminals.[2] The chart below shows the relative volume annually for the past few years for the U.S. terminals in the PNW (excluding Vancouver)



[2] Corn off of IC&E's lines known as the "Corn Lines" has not been a traditional source of PNW export corn, although corn originating from Minneapolis/St. Paul and Omaha/Council Bluffs, as well as numerous other origins in Minnesota, Nebraska, North Dakota, and South Dakota, has been. Nonetheless, as I discuss below, IC&E corn from the Corn Lines will likely become a potential source of PNW corn as a result of this Transaction and changing market conditions in the grain industry.

Whether or not grain goes to the PNW, Mexico, U.S. Gulf Coast, or U.S. domestic receivers, depends in part upon the freight rates. As a general rule of thumb, the industry uses Omaha, Nebraska and Council Bluffs, Iowa as an imaginary reference point for where the corn will typically move. If the origin is west and north of, or at, Omaha/Council Bluffs, the corn will generally move to the PNW or Mexico. If the origin point is east of that point, this corn will move to the Great Lakes, to U.S. domestic markets in the south-central and south-east states, or to the east coast. Corn from Minneapolis/St. Paul tends to go to any of the various destinations, although lately such corn has also been moving the PNW export markets.

In my expert opinion, and is discussed more below, for various reasons this imaginary reference point is likely to shift to the east and south (if it is not already doing so) so that origin points that would not be traditional candidates for the PNW or Mexican markets will now be so. Such a shift will make it easier for the Applicants, in a post-Transaction environment, to control pricing and service over former DME origins so as encourage non-traditional grain flows.

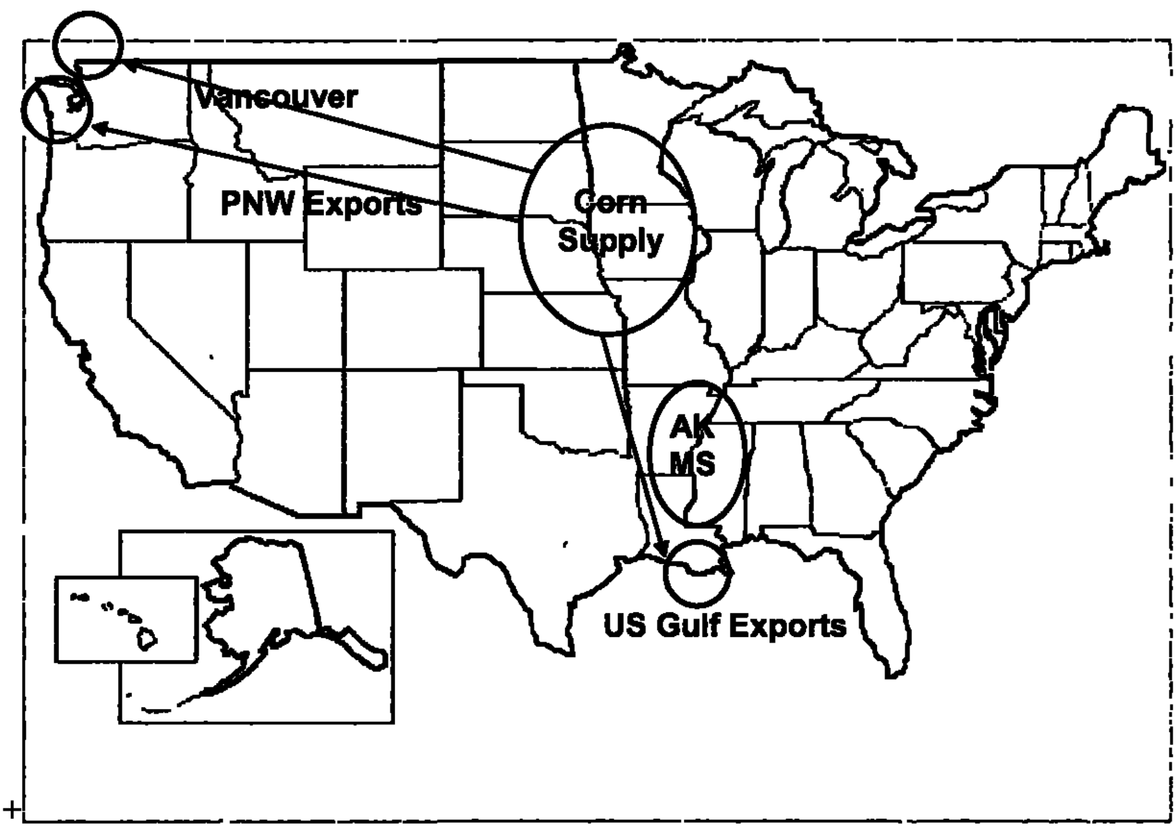
U.S. Grain and Freight Spreads

In determining how decisions are made in the overall market, it is important to understand that sellers (grain elevators) are always looking for access to more markets because doing so will increase demand for corn from that origin. Buyers are always looking for the lowest delivered cost of grain. As noted, transportation costs, and especially rail rates, plays an enormously important role in this process. Receivers (buyers) of corn must determine the best delivered price — whether delivered by rail, truck, barge, or a combination of modes. Buyers do this by looking at the per-bushel cost at the various origin points and then adding the transportation costs from that origin to the point of destination and then selecting the overall lowest delivered cost On the flip side, an originating elevator is determining the price that it can pay the producer (farmer) and the price it is willing to sell to a buyer by looking at various market factors, including transportation costs and buyer demand. Obviously, the grain elevator with the most buyers at the lowest transportation rate will have more demand for its corn and can obtain a higher selling price Rail pricing and service can often determine where a product is sold and for how much.

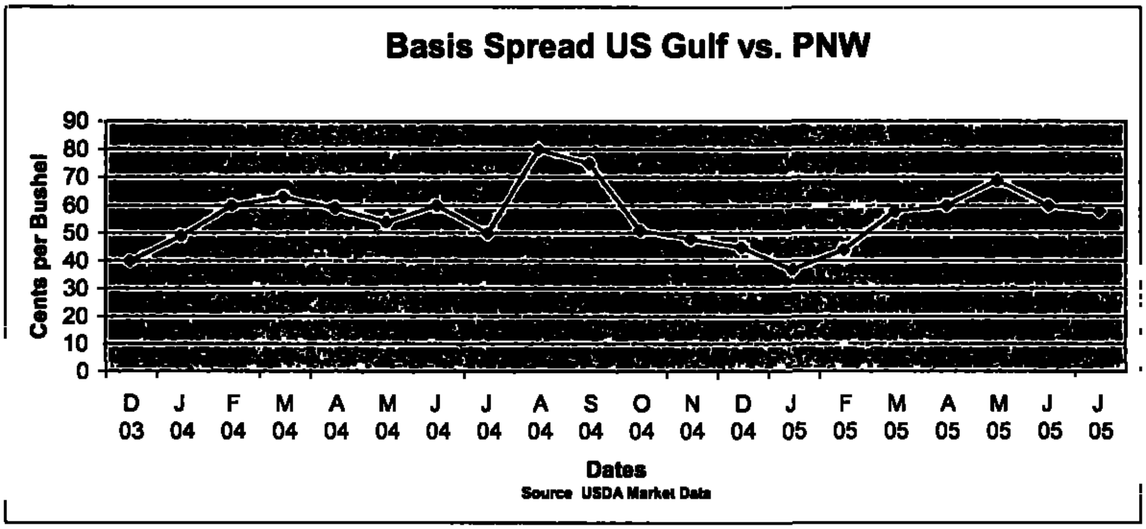
The Export Spread

In nearly every grain transaction a spread exists. As relevant here, it appears the big spreads from the upper Midwest U.S. are to the U S Gulf Coast and to the PNW While more localized spreads exist, they may be more truck oriented or truck and rail. In this case, a subset of the export spreads relates to the south central U.S and the Mexico rail export market.

PNW /GULF CORN SPREAD



The export spread between the U S. Gulf and the PNW can be tracked by using USDA data or industry data While less accurate perhaps on a daily basis, the USDA data can identify the general market and over time demonstrates price differentials. The chart below indicates a "typical spread" of fifty to sixty cents per bushel between the U.S. Gulf and the PNW. This is partially driven by corn availability, delivered freight expense, and ocean freight. The west coast typically has less ocean freight expense, and shorter distances to reach China and Asia, while the U.S. Gulf also serves those markets, it serves Europe and Africa continents more predictably than the PNW.



The south central U.S. domestic corn market typically trades at a five to ten cent discount to the U.S. Gulf Coast, according to industry sources. The difference between the U.S. Gulf Coast and PNW can be from several factors including multiple, and different priced supply points, different market conditions on various days, the "demand" aspect of the basis, handling margins, profit opportunities, and transportation costs. Nonetheless, the spread between the per-bushel price to the PNW and the per-bushel price to the Gulf Coast or the south-central states is significant, which gives CP significant rate flexibility so as to influence the ultimate destination.

Using published unit train data from the USDA "Weekly Transportation Report " the freight from Minneapolis to the PNW for unit trains is approximately $3,350 per car compared to approximately [redacted] per car from the ICE lines to the poultry customers. Thus the net spread is:

PNW premium to the Gulf is approximately (based on the above chart) 55, less 10 to poultry operations is 45, less 27 freight (Mnpls to PNW vs Iowa to AR/MS Poultry), which would allow an additional 18 cents in freight or basis to originate additional corn from the ICE/DME system for the PNW Export rather than to the poultry markets.

The fact that transportation rates play a role in impacting the spread and grain flows is outlined in the following summary from the February 28, 2008 "Weekly Transportation Report published by the USDA

Higher Spread Boosts Shipments from the Pacific Northwest
For the week ending February 21, inspections in the Pacific Northwest (PNW) increased 17 percent to .766 mmt but decreased in Mississippi (1.19 mmt) and Texas Gulf (.149 mmt) regions. The increase in PNW shipments is fueled in part by greater Asian demand for corn and wheat, and an unusually wide spread of $45 between Gulf and PNW ocean rates. As of February 22, the cost of shipping grain to Japan out of the Gulf was $107 per mt, 2 percent higher than the previous week, and the rate from PNW was $62 per mt, 2 percent lower.

The USDA report also reflects the year to date trend, and 2007 data further documents large percentage gains in PNW exports for corn and beans versus the U.S. Gulf. Note that 2008 PNW year to date corn exports are up 33 % versus 2007, while the U.S Gulf is up only 11%.

Table 16

Grain Inspections for Export by U.S. Port Region (1,000 metric tons)

Port regions	Week ending 02/21/08	2008 YTD[1]	2007 YTD[1]	2008 YTD as % of 2007 YTD
Pacific Northwest				
Wheat	**304**	**2,173**	**2,169**	**100**
Corn	**225**	**1,451**	**1,092**	**133**
Soybeans	**236**	**1,843**	**1,435**	**128**
Total	**766**	**5,467**	**4,696**	**116**
Mississippi Gulf				
Wheat	**76**	**630**	**755**	**83**
Corn	**739**	**5,940**	**5,351**	**111**
Soybeans	**378**	**3,544**	**4,112**	**86**
Total	**1,194**	**10,114**	**10,218**	**99**

CP Will Seek To Shift Origins

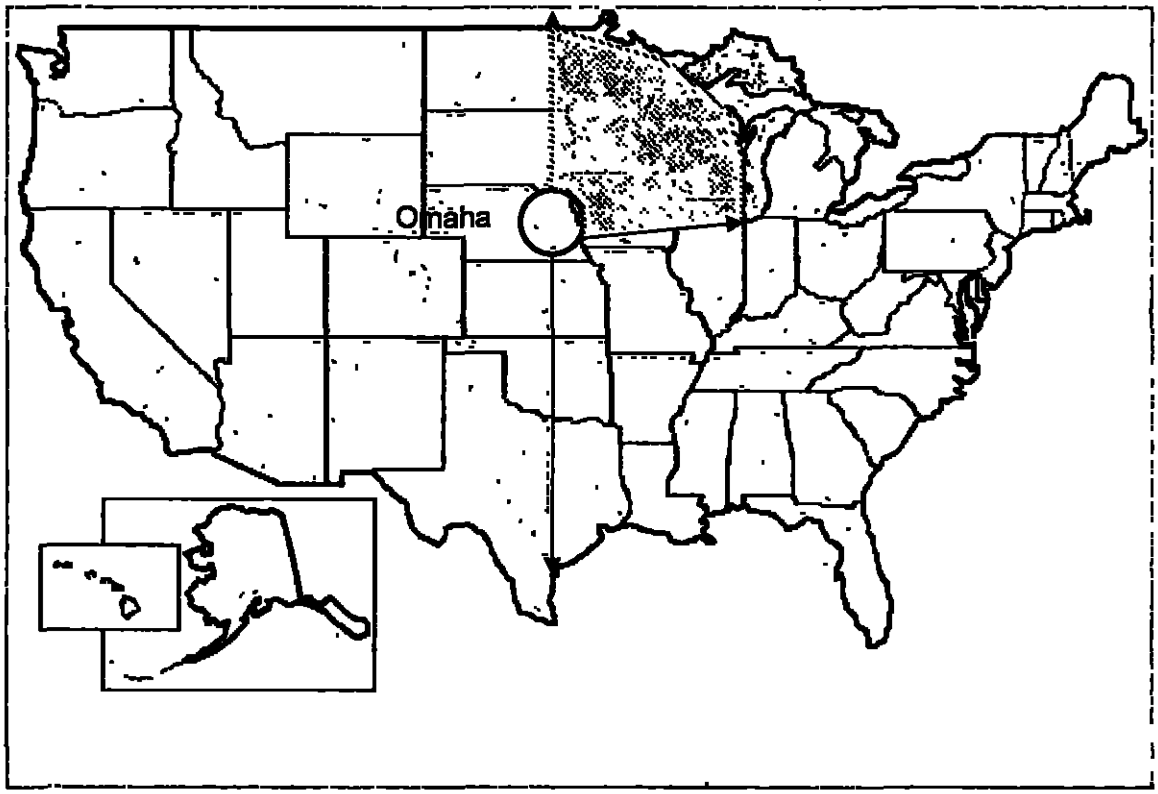
In this case, CP will, in a post-Transaction environment, control DME's grain originations. Based upon my discussions with Mr. Woodward and Mr. Bilovesky, and my knowledge of grain traffic flows, I share the opinion that CP is likely to seek ways in which to encourage grain flows to the PNW (or other destinations) so that the combined DME/CP system achieves the long-haul. If successful in its efforts, the Transaction could potentially reduce the available markets for corn originating on the Corn Lines by making routings to markets other than the PNW uneconomical. If so, the grain shippers (elevators) on the Corn Lines could see a reduction in the number of end users as CP will encourage rail movements to the PNW. From the feed mills' perspective, if this occurs, they will be forced to look to other sources of grain, but at higher prices than they pay today. The potential long-haul routings available to CP are as follows:

1. To The Pacific Northwest

My understanding of the existing traffic flows shows that there are existing CP(Soo)/Union Pacific ("UP") routings from the Minneapolis/St. Paul area to the PNW and existing DME/BNSF routings to the PNW. Given the shifting geographic markets, I would expect CP to encourage corn exports to the PNW from origins further south of Minneapolis and from the east of the DME/BNSF existing routings. As the PNW export terminals search for corn volume for export, the chart below confirms that corn availability is limited in the western and northern states; the traditional origin points for PNW corn. In fact, the largest supply of corn is in Iowa, Minnesota, South Dakota, and Nebraska, providing enticing long haul opportunities for CP/UP or CP/BN routings.

Thus, the imaginary East/West "Omaha" line is likely to shift as depicted in the following chart.

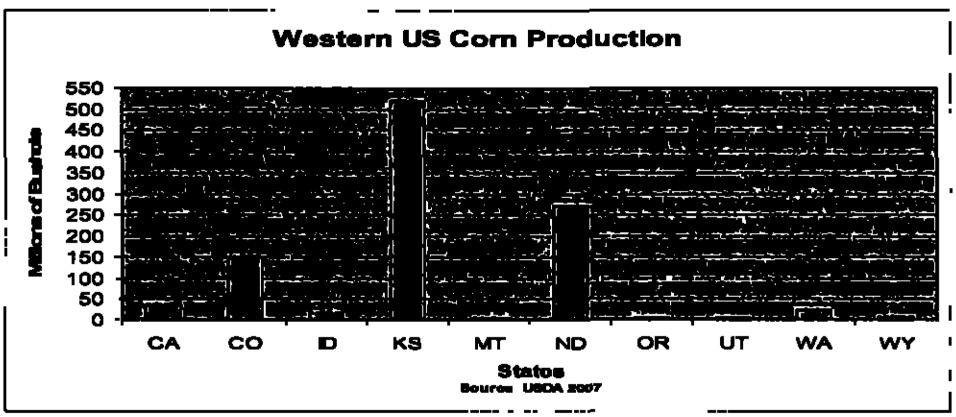
Possible New PNW Origins



In addition to PNW/Gulf spreads that may encourage more corn to the PNW on the supply side, there is simply not enough excess corn being produced in the existing markets sourcing the PNW export markets to meet the demand. The supply will be further exacerbated as major ethanol centers come on line.[3] Export buyers will have to seek alternative sources of corn, particularly considering that corn exports in 2007 were at record levels.

[3] Ethanol production has grown rapidly across the U.S. The primary feedstock for ethanol production using current technology is corn. A primary co-product of ethanol is Distillers Dried Grains, a feed ingredient. This statement focuses on the impact of grain flows as a result of CP/DME/ICE having common ownership and corporate strategy. Most of the corn that will flow to the new ethanol plants will be delivered by truck and therefore is intentionally not included in my statement. While the local supply of corn will be impacted by new ethanol production, this document addresses the rail movements of corn from the upper Midwest U.S. to current and alternative CP served destinations.

Most of the IC&E Corn Line car loadings of corn that are currently interchanged with KCSR for delivery to the south-central poultry markets originate at four locations in Minnesota. The result of CP actively seeking the long haul to the PNW and the shifting of the traditional origin sources will certainly bring these three Minnesota locations into the source market for PNW corn. The chart below shows the low production states in the extreme northwest U.S. One larger production state is Kansas, but it does not appear the CP has direct line access to Kansas origins.



2. To Canada

As a result of the Transaction, CP will also have the ability to route DM&E and IC&E corn to Canada. The western Canadian provinces are rich in various crops produced. However corn is not one of them. Should corn demand develop for domestic Canadian feedstock, or if corn exports were to be developed from Vancouver, the obvious new supply point would be the DM&E and IC&E lines providing single long haul opportunities for the CP.

3. To UP Served Destinations

While I have no personal knowledge of any alliance agreements between CP and Union Pacific ("UP") that would cause CP to favor UP routings, if that were to occur, KCSR served feed mills in the south-central U.S. would see their access to DME(IC&E) originated corn eliminated. CP could continue to encourage existing corn routings to the Kansas City gateway, perhaps even under a promise to "keep the Kansas City gateway open on commercially reasonable terms," but rather than interchange that corn with KCSR at Kansas City, CP would interchange it to UP. The resulting impact would be to raise the delivered cost of corn for these KCSR served feed mills by essentially eliminating the existing supply lines to KCSR at Kansas City.

Twenty-seven of the twenty-eight KCSR served feed mills are located solely on the KCSR line. A logical attempt to provide a CP/UP routing via the Kansas City gateway may advantage UP served feed mills and maintain multiple outlets for Corn Line shippers, but would actually raise the delivered price of corn to most KCSR served feed mills If CP diverted this corn to UP destinations, the KCSR receivers would have to turn to other KCSR served origins or to joint-line service between another railroad and KCSR to fill their demand. I understand from Mr. Bilovesky that for those receivers who rely upon DME originated corn as their primary source of grain that this would result in a higher delivered price of corn. It might also be possible for feed mills served by KCSR to use the corn delivered to nearby UP served feed mills. However, the cost of unloading, reloading, and trucking the feed from a UP served location to a KCSR served feed mill would certainly be more expensive than the existing IC&E/KCSR price.

III. SUMMARY AND CONCLUSIONS

Diversion of the existing DME/KCSR sourced supply to the PNW markets, to Canada, to Mexico, or to UP served feed mills will lessen the available corn supply for KCSR served feed mills, causing these feed mills to seek alternative sources and usually at higher prices. Such alternative sources are likely available, such as Omaha/Council Bluffs, Illinois, or Indiana, but for a substantial number of these feed mills, such corn is going to be more expensive on a delivered cost basis. Indeed, because most of the KCSR sourced corn from Omaha/Council Bluffs is already going to Mexico, for a large number of feed mills this corn is already more expensive, on average, than DME/KCSR sourced corn. Furthermore, adding demand to the Omaha/Council Bluffs market will only seek to raise the price of corn for Mexican buyers, the feed mills, and the poultry producers

Illinois and Indiana corn may be available, but KCSR does not serve those origins. Such corn would have to be interlined with another carrier. For many of the KCSR served feed mills, such joint-line service is more expensive today on a delivered cost basis and would likely remain so in the future. Likewise, it may even be possible for some of the KCSR served feed mills to obtain the corn from UP served feed mills via a transload operation or via some other transportation means (i.e. a combination of barge, rail, and/or truck), but again, at a higher delivered cost than what KCSR served feed mills enjoy today.

In summary, the impact on grain trade resulting from the Transaction is complicated, but the impact should not be underestimated as the involved railroads access portions of 30 % of the U.S. corn supply. While there are likely to be some benefits, there are also likely to be competitive harms, especially to those feed mills located on the KCSR in the south-central U.S. who receive their feedstock from corn that is sourced via the DME/KCSR grain agreement. Those feed mills in Oklahoma, Arkansas, and Kansas will lose access to their primary source of corn; forcing them to fill that demand by buying from other sources at higher prices. One way to mitigate this harm would be to ensure that KCSR has permanent ratemaking authority for the origination of corn from

IC&E origins and to ensure that CP takes no action to degrade the transit times over the existing routes.

S. THAD JONES

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Fort Wayne, IN 46804 **tjones@aefnallc.com**

Professional Experience.

President (2005-Present)
AEFNA LLC
Providing senior management support to the agriculture energy and food sectors in North America.

Senior Vice President (2003-2004)
Bunge North America
North America Vegetable Oil Refining and Packaging, Bakery Products
Soy oil, Canola oil, Palm, Peanut and Olive Oil, Animal Fats

President & Chief Operating Officer (2001-2002)
Cerestar USA
U S Corn Wet Miller – Subsidiary of Cerestar S A – Paris, France
Fructose, Glucose, Unmodified, Modified and Spray Dried Starch

Group Vice President (2000-2001)
Cerestar USA

Chief Administrative Officer (1995-2000)
Central Soya Company, Inc./Eridania Béghin-Say America
U S Soybean Processor and Specialty Soy Product Manufacturer
Soybeans, Soybean Meal and Oil, Soy Lecithins, Soy Protein Concentrate

Vice President-Business Development (1993-1994)
Central Soya Company, Inc.

President (1989-1992)
Innovative Pork Concepts
U S Holding Company for Swine Genetics and Pork Processing

President and General Manager (1991-1992)
Indiana Packers Co (an affiliate of Central Soya Company, Inc.)
U S Pork Processing – JV with Mitsubishi

Vice President and General Manager (1984-1989)
Central Soya Company, Inc., Fort Wayne, IN
U S Domestic and Export Grain Business
Corn, Soybeans, Wheat, Oats

Director of Grain Operations (1983-1984)
Ingram Barge Company, Nashville, TN
U S Inland Waterways – Dry Cargo

Grain Division (1976-1983)
Central Soya Company, Inc.

Professional Experience·

Corn Refiners Association Board of Directors
Indiana Manufacturing Association Board of Directors
National Grain & Feed Association Board of Directors and Executive Committee
Indiana Packers Board of Directors

Education·

DePauw University, B.A. in Economics
INSEAD Executive Program

VERIFICATION

I, Thad Jones, declare under penalty of perjury that the foregoing statement is true and correct. Further, I certify that I am qualified to file this Verified Statement.

Executed this 3rd day of March, 2008.

Thad Jones

**BEFORE THE
SURFACE TRANSPORTATION BOARD**

FINANCE DOCKET. NO. 35081

CANADIAN PACIFIC RAILWAY COMPANY, ET AL.

– CONTROL –

DAKOTA, MINNESOTA & EASTERN RAILROAD CORP., ET AL.

**COMMENTS OF THE KANSAS CITY SOUTHERN RAILWAY COMPANY AND
REQUEST FOR CONDITIONS**

EXHIBIT E

EVIDENTIARY EXHIBITS

**ALL EVIDENTIARY EXHIBITS ARE DESIGNATED
HIGHLY CONFIDENTIAL AND ARE
REDACTED FROM THE PUBLIC VERSION**

Color

of the critical mass of the CPR/UP traffic alliance, favor and promote traffic flows in cooperation with UP, and discourage service offerings competing with CPR/UP services.

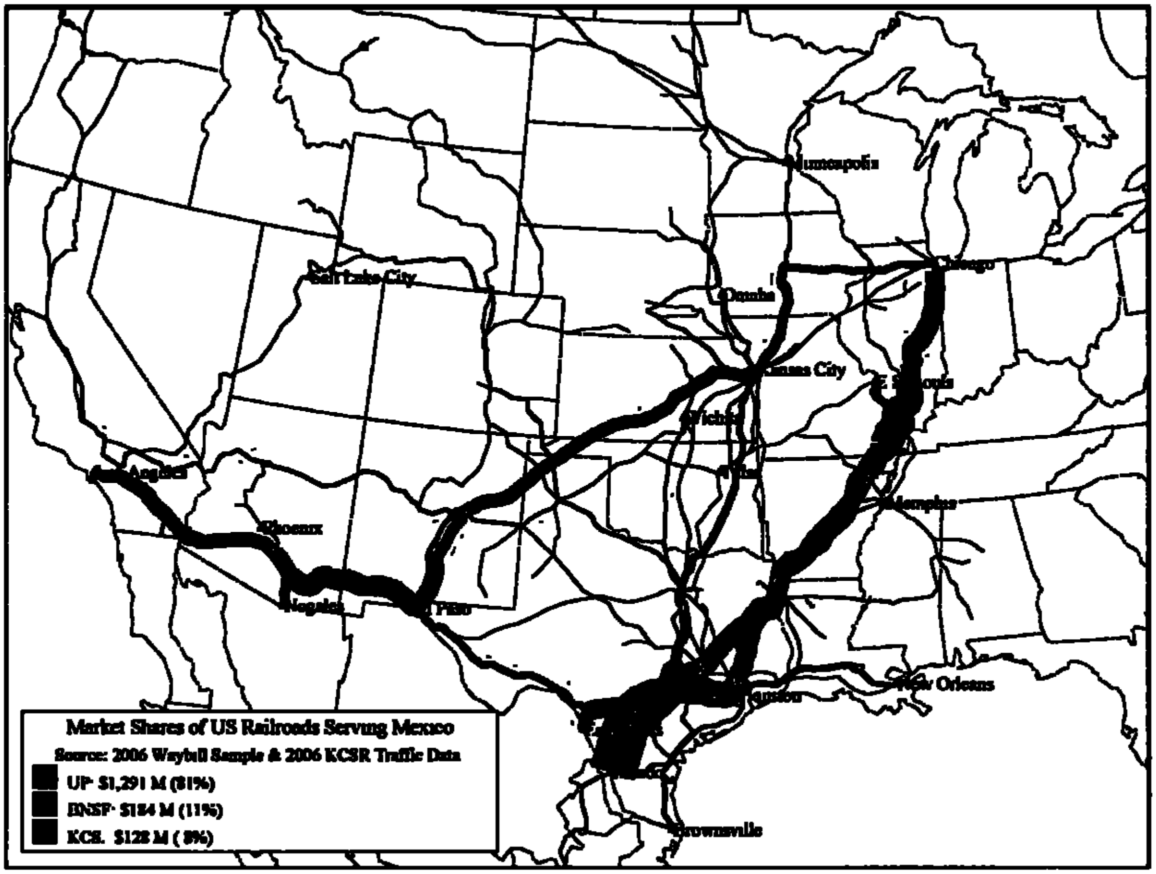

Exhibit 2: Market Shares of U.S. Railroads Serving Mexico

The CPR/UP alliance has been effective in growing the volume and revenue of the interline traffic of both participating railroads. Interline traffic between CPR and UP has grown considerably as NAFTA traffic flows have mounted. Exhibit 3, below, demonstrates how CPR-UP interline traffic has grown since the advent of the CPR/UP CanAm alliance. This exhibit draws a comparison between alliance-oriented annual interline traffic volume growth for UP and for CPR from 2000 through 2006 and, separately, the annual traffic volume growth that each company has experienced *excluding* CPR-UP interline traffic. Exhibit 3 demonstrates that CPR/UP interline alliance traffic volume growth rate has significantly exceeded overall other traffic growth rate of each of these railroads.

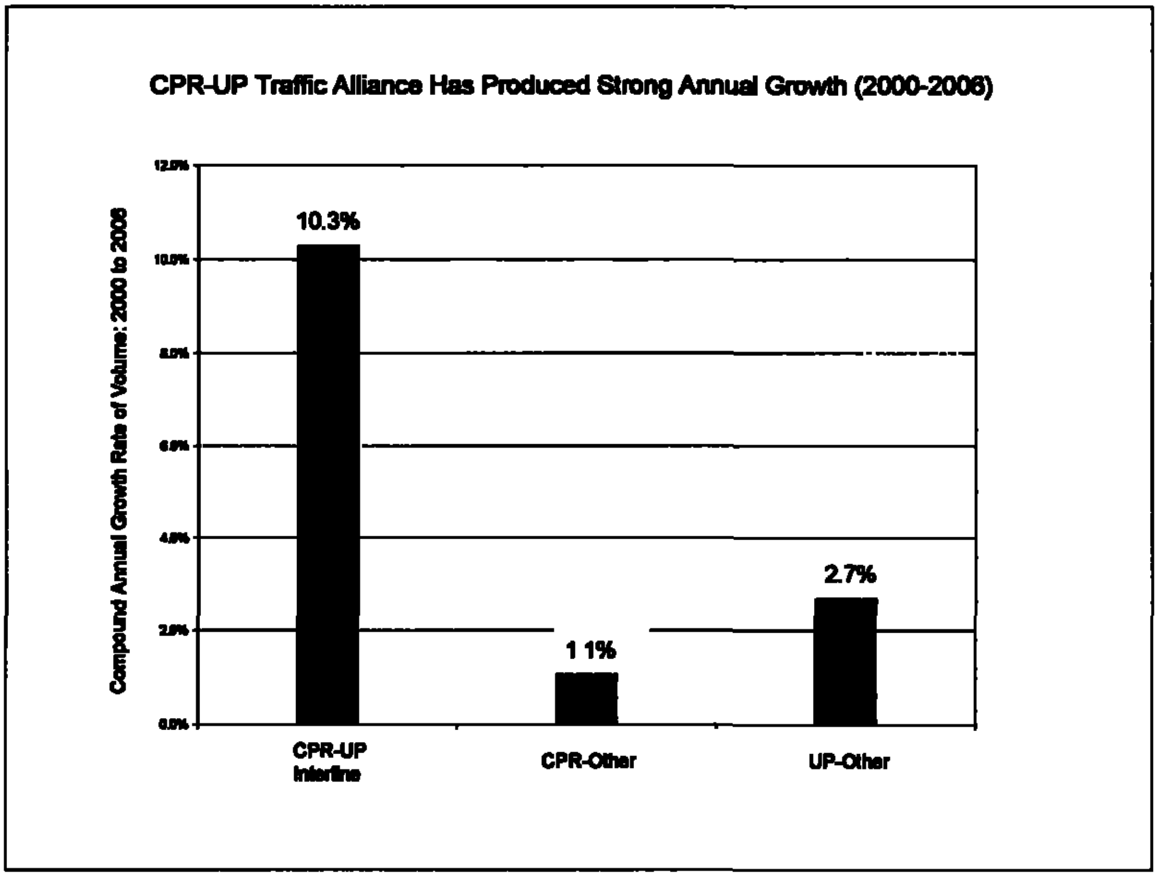

Exhibit 3: CPR-UP Traffic Alliance Has Produced Strong Annual Growth (2000 to 2006)

Exhibit 3 clearly illustrates the traffic growth impact of the CPR/UP traffic alliance, and it suggests the importance of the alliance to CPR's and UP's respective strategic planning and marketing initiatives since it allows both CPR and UP to leverage alliance interline traffic with non-alliance traffic. It also reinforces the proposition articulated by UP's Mr. Koraleski that UP and CPR are indeed two railroads that think of themselves as one. Because CPR and UP do think of themselves as one, it is important that the proposed Transaction be evaluated with that proposition in mind. My statement discusses the harms to competition that will flow from the proposed Transaction, taking into account the CPR/UP traffic alliance and its likely influence on future traffic flows

UP alliance interline routing would still provide for a substantially longer haul for CPR than DME currently supplies for DME-originated grain moving to KCSR at Kansas City.

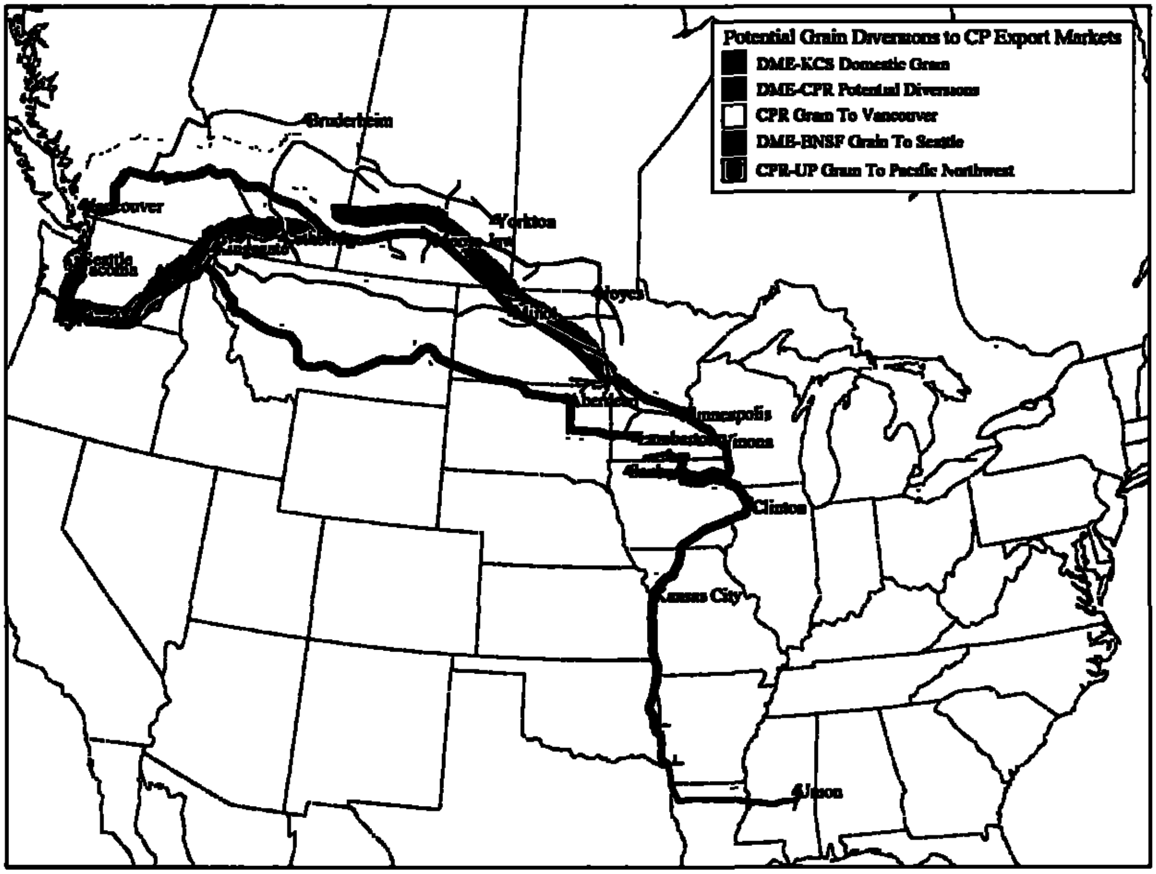

Exhibit 6: Potential Grain Diversions to CP Export Markets

Because of CPR's strategic preferences, it is highly likely that DME-originated grain now headed to domestic consumers, including grain consumers located on KCSR, would be the target of CPR/UP alliance-oriented diversion to U S. Pacific Coast export facilities. As shown in Exhibit 6, some DME-origin grain already moves to the Pacific Coast for export, but does so in DME-BNSF interline service.[12] Absent an agreement between CPR and BNSF that will ensure BNSF's continued role in such interline grain

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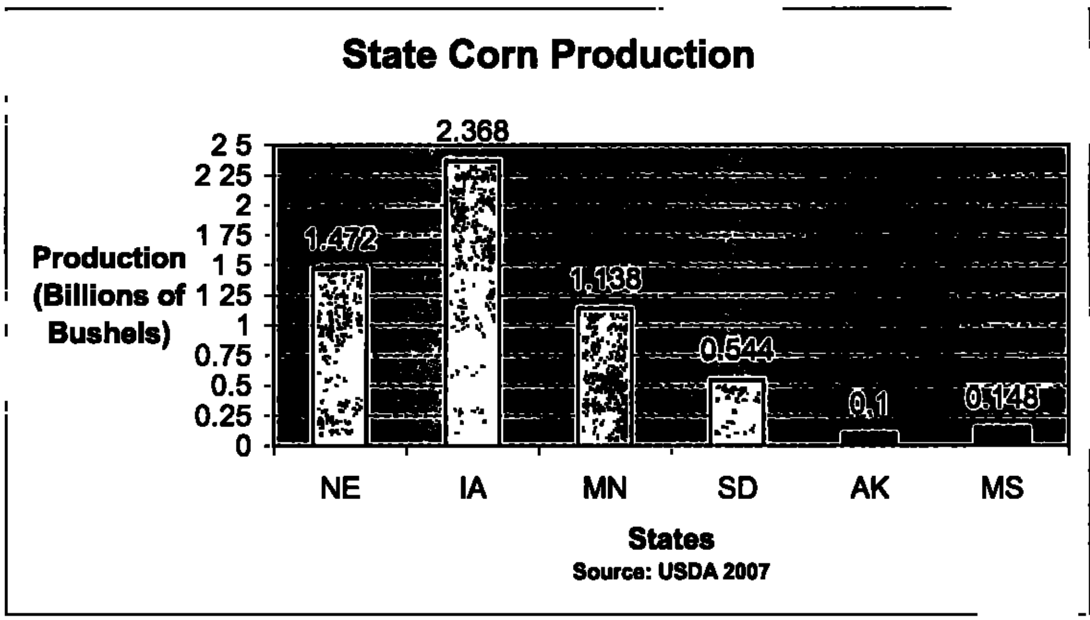
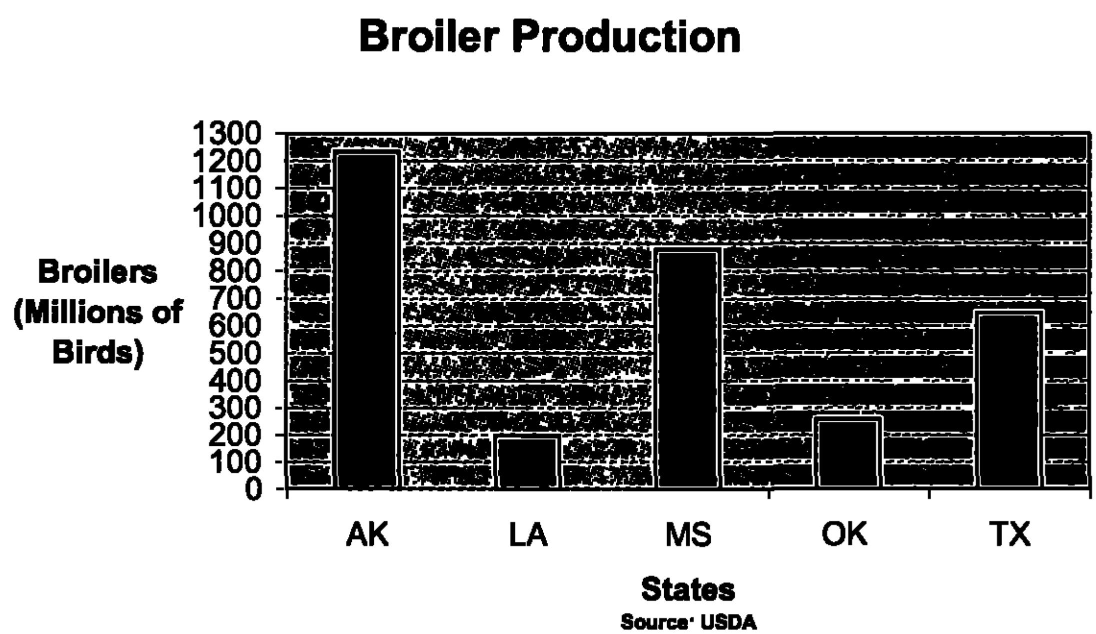
[12] As I have demonstrated in Exhibit 4, above, and in my analysis generally, long-haul export grain traffic moves such as those that BNSF and DME are participating in jointly are quite attractive.



Also of note on the above chart is corn production in the two states of Arkansas and Mississippi, which are two of the primary destination markets for DME/KCSR routed corn These two states are net importers of corn Iowa and Minnesota provide a substantial amount of corn to feed mills in Kansas, Oklahoma, Arkansas, and Mississippi (as well as other south-central states) for use as feed for the large poultry industry that is a mainstay of the south central U.S. agricultural economy and a large provider of cost efficient poultry products in the U.S. retail food and foodservice industries

Broiler Production

The south central portions of the U.S. have been large poultry (referred to in the trade as "Broilers") producing states for a long time. As a result, certain grain flow patterns have developed and these patterns have largely been uninterrupted, predominately allowing corn from the large production states in the northern U.S. to move efficiently to the south for livestock feed As depicted in the chart below, Arkansas and Mississippi are two of the very largest states in broiler production. These two states are served by the KCSR and have benefited by the common grain tariff pricing structure that exists between the DME and KCSR which allows for the KCSR equipment to efficiently gather corn from the key corn producing states on the DME and deliver it to Arkansas and Mississippi on KCSR lines.

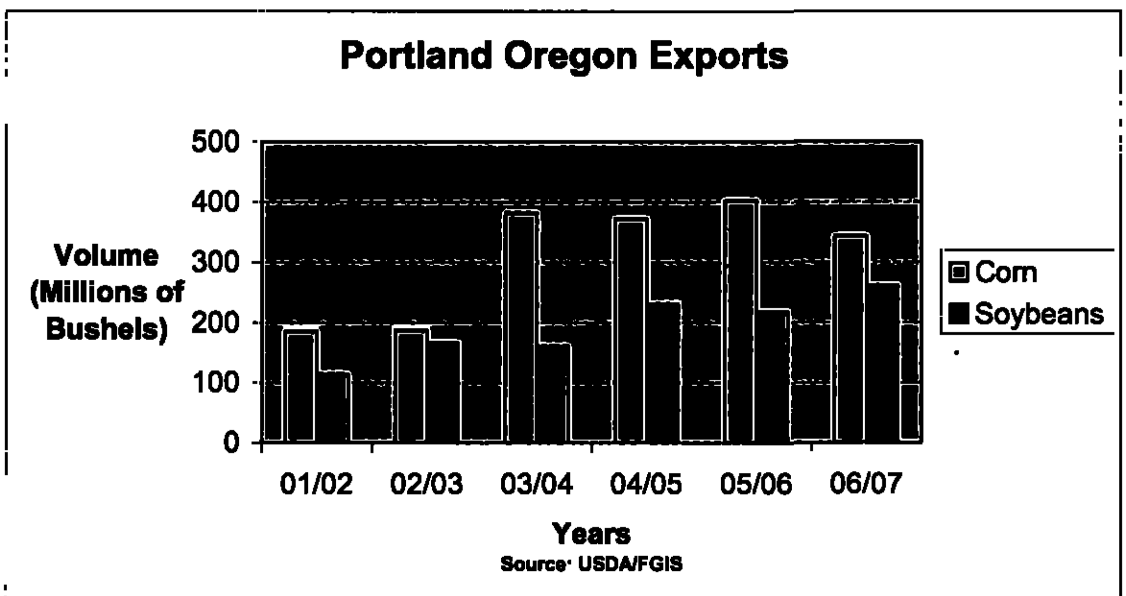


Indeed, based upon what other witnesses have told me, it is my understanding that virtually all of the DME originated grain that is interlined with KCSR is delivered to KCSR served feed mills that serve the poultry markets in these south-central states and that the feed mills in Kansas, Oklahoma, and Arkansas depend upon this DME originated grain as the primary source of rail delivered feedstock. This indicates to me that the lowest delivered price of corn to these feed mills is via the DME/KCSR rail option, and that if such feed mills had to obtain their primary source of non local corn from other origins, they would end up paying more.

Competing Markets

Although these feed mills have been able to secure grain via the DME/KCSR routings from DME origins in Iowa and Minnesota to their south-central locations, these feed mills are competing with other destinations (i.e buyers/receivers at other destinations) for Upper Midwest originated corn. In fact, one of the largest export ports in the world is immediately south of the region and is the U.S. Gulf Coast. These large export facilities are huge buyers of corn and other grain and typically over 50 % of the U.S. exported grain annually is shipped through these ports.

Likewise to the Pacific Northwest is a series of export facilities spanning from Portland Oregon to Seattle Washington, and northward to Vancouver, British Columbia, Canada. Collectively referenced as the Pacific Northwest, or "PNW," these terminals source grain from the upper U.S. Midwest and the western Canadian provinces for eventual export through the PNW terminals.[2] The chart below shows the relative volume annually for the past few years for the U.S. terminals in the PNW (excluding Vancouver)



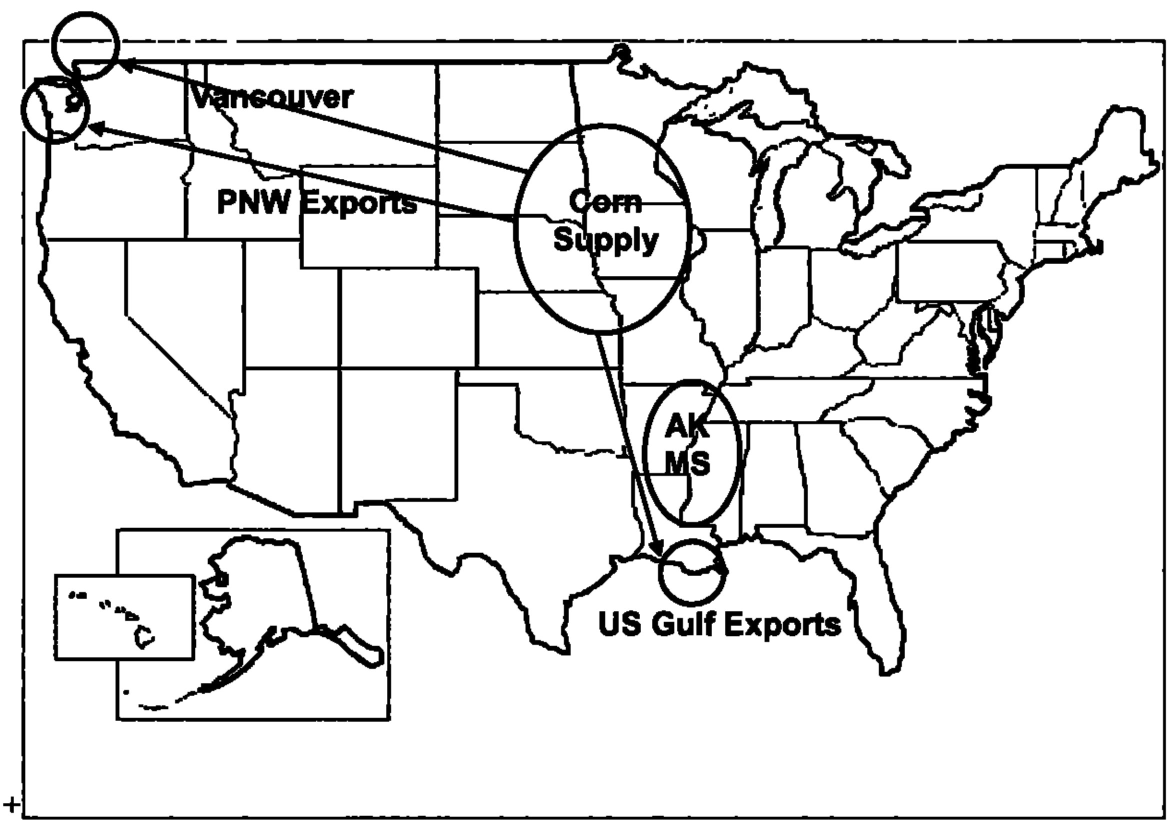
[2] Corn off of IC&E's lines known as the "Corn Lines" has not been a traditional source of PNW export corn, although corn originating from Minneapolis/St. Paul and Omaha/Council Bluffs, as well as numerous other origins in Minnesota, Nebraska, North Dakota, and South Dakota, has been. Nonetheless, as I discuss below, IC&E corn from the Corn Lines will likely become a potential source of PNW corn as a result of this Transaction and changing market conditions in the grain industry.

willing to sell to a buyer by looking at various market factors, including transportation costs and buyer demand. Obviously, the grain elevator with the most buyers at the lowest transportation rate will have more demand for its corn and can obtain a higher selling price. Rail pricing and service can often determine where a product is sold and for how much.

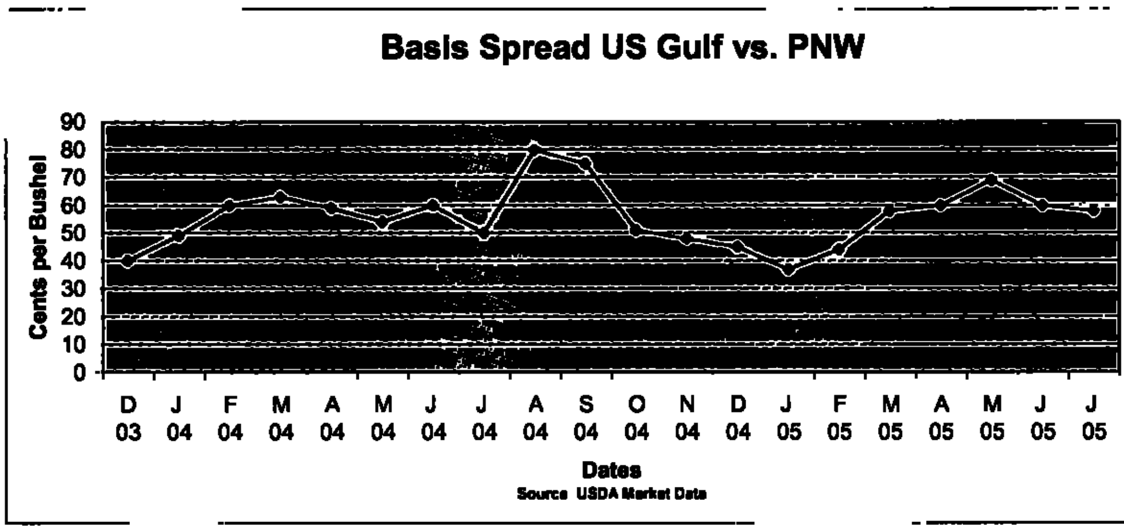
The Export Spread

In nearly every grain transaction a spread exists. As relevant here, it appears the big spreads from the upper Midwest U.S. are to the U.S Gulf Coast and to the PNW. While more localized spreads exist, they may be more truck oriented or truck and rail. In this case, a subset of the export spreads relates to the south central U S and the Mexico rail export market.

PNW /GULF CORN SPREAD



The export spread between the U.S. Gulf and the PNW can be tracked by using USDA data or industry data. While less accurate perhaps on a daily basis, the USDA data can identify the general market and over time demonstrates price differentials. The chart below indicates a "typical spread" of fifty to sixty cents per bushel between the U.S. Gulf and the PNW. This is partially driven by corn availability, delivered freight expense, and ocean freight. The west coast typically has less ocean freight expense, and shorter distances to reach China and Asia, while the U.S. Gulf also serves those markets, it serves Europe and Africa continents more predictably than the PNW.



The south central U S domestic corn market typically trades at a five to ten cent discount to the U.S. Gulf Coast, according to industry sources. The difference between the U.S. Gulf Coast and PNW can be from several factors including multiple, and different priced supply points, different market conditions on various days, the "demand" aspect of the basis, handling margins, profit opportunities, and transportation costs. Nonetheless, the spread between the per-bushel price to the PNW and the per-bushel price to the Gulf Coast or the south-central states is significant, which gives CP significant rate flexibility so as to influence the ultimate destination.

Using published unit train data from the USDA "Weekly Transportation Report" the freight from Minneapolis to the PNW for unit trains is approximately $3,350 per car compared to approximately [redacted] per car from the ICE lines to the poultry customers. Thus the net spread is:

PNW premium to the Gulf is approximately (based on the above chart) 55, less 10 to poultry operations is 45, less 27 freight (Mnpls to PNW vs Iowa to AR/MS Poultry), which would allow an additional 18 cents in freight or basis to originate additional corn from the ICE/DME system for the PNW Export rather than to the poultry markets.

The fact that transportation rates play a role in impacting the spread and grain flows is outlined in the following summary from the February 28, 2008 "Weekly Transportation Report published by the USDA.

> **Higher Spread Boosts Shipments from the Pacific Northwest**
> For the week ending February 21, inspections in the Pacific Northwest (PNW) increased 17 percent to .766 mmt but decreased in Mississippi (1.19 mmt) and Texas Gulf (.149 mmt) regions. The increase in PNW shipments is fueled in part by greater Asian demand for corn and wheat, and an unusually wide spread of $45 between Gulf and PNW ocean rates. As of February 22, the cost of shipping grain to Japan out of the Gulf was $107 per mt, 2 percent higher than the previous week, and the rate from PNW was $62 per mt, 2 percent lower.

The USDA report also reflects the year to date trend, and 2007 data further documents large percentage gains in PNW exports for corn and beans versus the U S Gulf. Note that 2008 PNW year to date corn exports are up 33 % versus 2007, while the U.S Gulf is up only 11%.

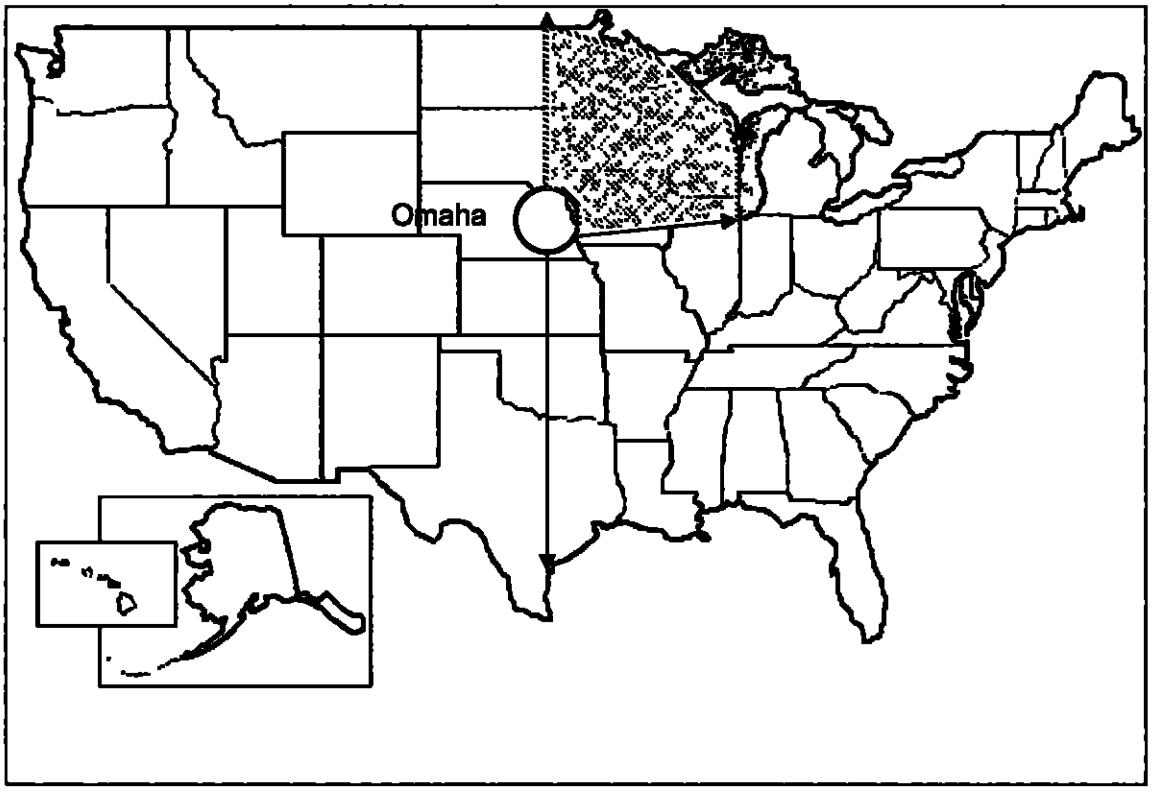
Table 16

Grain Inspections for Export by U.S. Port Region (1,000 metric tons)

Port regions	Week ending 02/21/08	2008 YTD[1]	2007 YTD[1]	2008 YTD as % of 2007 YTD
Pacific Northwest				
Wheat	**304**	**2,173**	**2,169**	**100**
Corn	**225**	**1,451**	**1,092**	**133**
Soybeans	**236**	**1,843**	**1,435**	**128**
Total	**766**	**5,467**	**4,696**	**116**
Mississippi Gulf				
Wheat	**76**	**630**	**755**	**83**
Corn	**739**	**5,940**	**5,351**	**111**
Soybeans	**378**	**3,544**	**4,112**	**86**
Total	**1,194**	**10,114**	**10,218**	**99**

CP Will Seek To Shift Origins

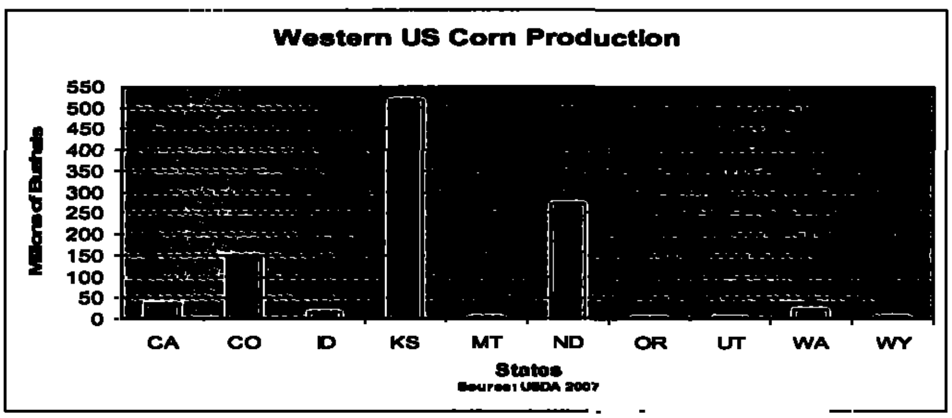
Possible New PNW Origins



In addition to PNW/Gulf spreads that may encourage more corn to the PNW on the supply side, there is simply not enough excess corn being produced in the existing markets sourcing the PNW export markets to meet the demand. The supply will be further exacerbated as major ethanol centers come on line.[3] Export buyers will have to seek alternative sources of corn, particularly considering that corn exports in 2007 were at record levels.

[3] Ethanol production has grown rapidly across the U.S. The primary feedstock for ethanol production using current technology is corn. A primary co-product of ethanol is Distillers Dried Grains, a feed ingredient. This statement focuses on the impact of grain flows as a result of CP/DME/ICE having common ownership and corporate strategy. Most of the corn that will flow to the new ethanol plants will be delivered by truck and therefore is intentionally not included in my statement. While the local supply of corn will be impacted by new ethanol production, this document addresses the rail movements of corn from the upper Midwest U.S. to current and alternative CP served destinations.

Most of the IC&E Corn Line car loadings of corn that are currently interchanged with KCSR for delivery to the south-central poultry markets originate at four locations in Minnesota. The result of CP actively seeking the long haul to the PNW and the shifting of the traditional origin sources will certainly bring these three Minnesota locations into the source market for PNW corn. The chart below shows the low production states in the extreme northwest U.S. One larger production state is Kansas, but it does not appear the CP has direct line access to Kansas origins.



2. To Canada

As a result of the Transaction, CP will also have the ability to route DM&E and IC&E corn to Canada. The western Canadian provinces are rich in various crops produced. However corn is not one of them. Should corn demand develop for domestic Canadian feedstock, or if corn exports were to be developed from Vancouver, the obvious new supply point would be the DM&E and IC&E lines providing single long haul opportunities for the CP.

3. To UP Served Destinations