

228708



SIDLEY AUSTIN LLP  
1501 K STREET, N.W.  
WASHINGTON, D.C. 20006  
(202) 736 8000  
(202) 736 8711 FAX

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SYDNEY  
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WASHINGTON, D.C.

thynes@sidley.com  
(202) 736 8198

FOUNDED 1888

January 31, 2011

VIA ELECTRONIC FILING

Rachel D. Campbell, Director  
Office of Proceedings  
Surface Transportation Board  
395 E Street, S.W.  
Washington, D.C. 20423

ENTERED  
Office of Proceedings

JAN 31 2011

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Public Record

Re: Review of Commodity, Boxcar, and TOFC/COFC Exemptions  
Docket No. EP 704

Dear Ms. Campbell:

Enclosed for filing in the above-captioned proceeding please find the Comments of Canadian Pacific Railway Company ("CP"). CP does not intend to present oral testimony at the hearing scheduled for February 24, 2011, and submits the enclosed comments in lieu of such an appearance.

Very truly yours,

  
Terence M. Hynes

TMH:aat  
Enclosure

**BEFORE THE  
SURFACE TRANSPORTATION BOARD**

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**Docket No. EP 704**

**REVIEW OF COMMODITY, BOXCAR, AND  
TOFC/COFC EXEMPTIONS**

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**COMMENTS OF CANADIAN PACIFIC RAILWAY COMPANY**

**Paul Guthrie  
Vice President - Legal Services  
Canadian Pacific Railway Company  
401 9th Avenue, S.W.  
Gulf Canada Square, Suite 500  
Calgary, Alberta T2P 4Z4 Canada**

**Patrick Riley  
Director – Legal Regulatory Affairs  
Canadian Pacific Railway Company  
401 9<sup>th</sup> Avenue, S.W., Suite 920  
Gulf Canada Square, Suite 500  
Calgary, Alberta T2P 4Z4 Canada**

**Terence M. Hynes  
Matthew J. Warren  
Noah A. Clements  
Sidley Austin LLP  
1501 K Street, N.W.  
Washington, D.C. 20005  
(202) 736-8000**

*Counsel for Canadian Pacific Railway Company*

**Dated: January 31, 2011**

**BEFORE THE  
SURFACE TRANSPORTATION BOARD**

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**Docket No. EP 704**

**REVIEW OF COMMODITY, BOXCAR, AND  
TOFC/COFC EXEMPTIONS**

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**COMMENTS OF CANADIAN PACIFIC RAILWAY COMPANY**

Pursuant to the decision served in the above-captioned proceeding on October 21, 2010, as corrected by a decision served on October 25, 2010 (the "*October 25 Decision*"), Canadian Pacific Railway Company and its U.S. rail carrier affiliates, Soo Line Railroad Company, Dakota, Minnesota and Eastern Railroad Corporation and Delaware and Hudson Railway Company, Inc. (collectively, "CP") submit these Comments regarding the Board's review of certain categorical exemptions from regulation pursuant to 49 U.S.C. § 10502. In the *October 25 Decision*, the Board requested comments from interested parties regarding three issues: (1) "the effectiveness of these exemptions in the marketplace"; (2) "whether the rationale behind any of these exemptions should be revisited" and (3) "whether the exemptions should be subject to periodic review." *October 25 Decision* at 3.

As CP's comments demonstrate, the ICC's decisions exempting certain categories of highly competitive freight traffic from stifling regulation have benefited railroads and shippers alike, by eliminating burdensome tariff and contract summary filing requirements, affording carriers and their customers flexibility to respond quickly to changes in the dynamic North American marketplace, and fostering investment and service innovation. A rollback of the Board's categorical exemptions would be patently inconsistent with Congress' express directive that rates and services be established, to the maximum extent possible, by market forces – not

regulation. Moreover, reversal of deregulatory actions that contributed greatly to the financial recovery of the railroad industry and created positive incentives for carriers to invest in needed infrastructure would stifle continued improvement at a time when the demand for efficient transportation services is expected to grow substantially. There is no legitimate basis for revoking or curtailing the TOFC/COFC, boxcar or commodity-based exemptions under the governing legal standards articulated in the ICC Termination Act of 1995, Pub. L. 104-88, 109 Stat. 803 (1996) ("ICCTA") and this Board's precedents. Accordingly, for the reasons discussed below, CP urges the Board to dismiss this proceeding.

## **I. THE GOVERNING LEGAL FRAMEWORK**

The *October 25 Decision* suggests that this proceeding was prompted by certain "informal inquiries" that the Board has received in recent years "questioning the relevance and/or necessity of some of the existing commodity exemptions, given the changes in the competitive landscape and the railroad industry that have occurred over the past few decades." *October 25 Decision* at 3 (emphasis added). Based upon such "inquiries," the Board has scheduled a hearing to "explore the continuing utility of and the issues surrounding the categorical exemptions under § 10502." *Id.* (emphasis added). With all respect, the legal standard for promulgating a categorical exemption, or revoking a previously-approved exemption, is not whether the exemption is "relevant," or "necessary," or whether it is deemed to have "continuing utility." Rather, the Board's power – indeed, its statutory duty – to aggressively pursue exemptions from regulation, and to consider requests to revoke or modify a previously approved exemption on a case-by-case basis, are governed by the standards set forth at 49 U.S.C. § 10502 and well-established precedents under that statute.

**A. Congress Has Mandated That The Board Exempt Carriers From Regulation To The Maximum Extent Consistent With The Rail Transportation Policy.**

The Board's authority to promulgate categorical exemptions is set forth at 49 U.S.C.

§ 10502, which states:

The Board, to the maximum extent consistent with this part, shall exempt a person, class of persons, or a transaction or service whenever the Board finds that the application in whole or in part of a provision of this part —

(1) is not necessary to carry out the transportation policy of section 10101 of this title; and

(2) either —

(A) the transaction or service is of limited scope; or

(B) the application in whole or in part of the provision is not needed to protect shippers from the abuse of market power.

49 U.S.C. § 10502(a) (emphasis added).

Section 10502 traces its origin to the Railroad Revitalization and Regulatory Reform Act, Pub. L. 94-210, 90 Stat 31 (1976) (the "4R Act"). As the Board observes (*October 25 Decision* at 2), the 4R Act represented "an effort to revitalize the struggling railroad industry," which had experienced decades of financial decline, including the bankruptcies of several of the nation's largest carriers. Congress found that the industry's financial difficulties were caused, to a substantial degree, by the heavy-handed regulatory policies administered by the former ICC.<sup>1</sup> In order to reverse that trend, Congress enacted a variety of provisions (including the exemption statute) that were designed to free railroads from unnecessary and counterproductive regulation.

Several years later, in the Staggers Act, Pub. L. 96-448, 94 Stat. 1895 (1980), Congress significantly broadened the exemption statute by imposing on the ICC an affirmative duty to grant exemptions whenever it found that regulation was not necessary to carry out the provisions

<sup>1</sup> See, e.g., H.R. Rep. No. 94-725, 94<sup>th</sup> Cong., 1<sup>st</sup> Sess. 80 (1975); S. Rep. No. 94-499, 94<sup>th</sup> Cong., 2d Sess. 2, U.S. Code Cong. & Admin. News 1976, at 14.

of the newly-enacted Rail Transportation Policy ("RTP").<sup>2</sup> The legislative history of the Staggers Act made clear Congress' expectation that the agency would wield its exemption authority aggressively to remove as many regulatory impediments as possible:

The Conferees expect that, consistent with the policies of this act, the Commission will pursue partial and complete exemptions from remaining regulation. The Conferees anticipate that through the exemption process the Commission will eventually reduce its exercise of authority to instances where regulation is necessary to protect against abuses of market power where other federal remedies are inadequate for this purpose. Particularly, the Conferees expect that as many as possible of the Commission's restrictions on changes in prices and services by rail carriers will be removed and that the Commission will adopt a policy of reviewing carrier actions after the fact to correct abuses of market power.

H.R. Conf. Rep. 96-1430, at 104-105 (1980) (emphasis added). Consistent with this clear policy directive, the ICC promulgated a variety of categorical exemptions, including the TOFC/COFC, boxcar and commodity-based exemptions at issue in this proceeding, and "class" exemptions that, among other things, reduced the regulatory burdens associated with railroad line sales and grants of trackage rights.

Congress expressed its approval of the ICC's expansive use of the exemption provisions: "[t]hese exemptions have proven highly beneficial to shippers and railroads."<sup>3</sup> Given the clear success of the deregulatory policies set forth in the Staggers Act, Congress articulated its intent, in the ICCTA, to "preserve the careful balance put in place by the 4R Act and the Staggers Act

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<sup>2</sup> The RTP states that "it is the policy of the United States Government," *inter alia*, "(1) to allow, to the maximum extent possible, competition and the demand for services to establish reasonable rates for transportation by rail; (2) to minimize the need for Federal regulatory control over the rail transportation system . . . ; (3) to promote a safe and efficient rail transportation system by allowing rail carriers to earn adequate revenues" and "(6) to maintain reasonable rates where there is an absence of effective competition." 49 U.S.C. § 10101 (emphasis added).

<sup>3</sup> See S. Rep. No. 104-176, 104<sup>th</sup> Cong. 1<sup>st</sup> Sess. 8 (1995).

that led to a dramatic revitalization of the rail industry while protecting significant shipper and national interests.”<sup>4</sup> The Board itself echoed Congress’ assessment, observing that:

The Staggers Act granted railroads freedom from an overly restrictive and burdensome regulatory regime, enabling them to compete more effectively with each other and with other transportation modes, most notably motor carriers and barge lines. . . . The competitive process unleashed by the Staggers Act has been one of the most significant public policy successes of this century.”

*Union Pacific Corp., et al. – Control and Merger – Southern Pacific Corp., et al.*, 1 S.T.B. 233, 384 (1996) (emphasis added).

The policies adopted by Congress in the 4R Act and the Staggers Act “fundamentally changed the economic regulation of the railroad industry.” *October 25 Decision* at 2. In particular, the exemption provisions embody a presumption that rail carrier rates and services should not be regulated unless government intervention is shown to be necessary to prevent the abuse of market power. Absent such circumstances, “[the Board] has no choice but to grant an exemption.” *Coal Exporters Ass’n v. United States*, 745 F.2d 76, 82 (D.C. Cir 1984).

**B. The Standards For Revoking An Exemption, In Whole Or In Part, Are Well-Established.**

The circumstances under which the Board may roll back an exemption, in whole or in part, are set forth in Section 10502(d), which provides: “The Board may revoke an exemption, to the extent it specifies, when it finds that application in whole or in part of a provision of this part to the person, class, or transportation is necessary to carry out the transportation policy of section 10101 of this title.” 49 U.S.C. § 10502(d). This provision is consistent with Congress’ directive in Section 10502(a) that the Board “shall” grant exemptions “to the maximum extent consistent with” the RTP, and reflects Congress’ intent that “carrier rates and practices [should]

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<sup>4</sup> See S. Rep. No. 104-176, at 6.

be disciplined by market forces rather than government regulation.” *Mr. Sprout Inc. v. United States*, 8 F.3d 118, 122 (2d Cir. 1993).

The standards governing the Board’s consideration of a petition to revoke an exemption are well-established. The Board and its predecessor have consistently held that “a party [seeking revocation of an exemption] has a burden of showing that our prior findings supporting the initial exemption were clearly wrong, or that changed circumstances require us to revisit them.” *Rail Exemption Auth. – Misc. Agri. Commodities – Pet. of G. & T. Terminal Pack’g Co. to Revoke Conrail Exemption (“G&T”)*, 8 I.C.C.2d 674, 677 (1992).

A petition to revoke must demonstrate conduct that frustrates the NRTP, and it must show that Commission regulation can and will be effective in carrying out the NRTP. Generally, we will not revoke an exemption unless the regulatory provisions which would thereby be reinstated are capable of ameliorating the harm that a petitioner alleges . . . . Moreover, violations must be serious enough to indicate abuse of market power which can and ought to be corrected by regulation.

*G&T* at 676-77 (emphasis added). Moreover, “petitions to revoke must be based on reasonable, specific concerns demonstrating that reconsideration of the exemption is warranted.” *Minnesota Commercial Ry., Inc. – Trackage Rights Exemption – Burlington Northern R. Co.*, 8 I.C.C.2d 31, 35 (1991) (“*Minnesota Commercial Ry.*”) (emphasis added). See also Finance Docket No. 34503, *Timber Rock Railroad, Inc. – Lease Exemption – The Burlington Northern and Santa Fe Ry. Co.*, (served October 7, 2004) at 2; Finance Docket No. 33326 *et al.*, *I&M Rail Link LLC – Acquisition and Operation Exemption – Certain Lines of Soo Line Railroad Company d/b/a Canadian Pacific Railway*, 2 S.T.B. 167 (1997), *aff’d sub nom. City of Ottumwa v. STB*, 153 F.3d 879 (8th Cir. 1998) (“*I&M Rail Link*”).

Consistent with the language of Section 10502(d), the Board’s analysis in revocation proceedings focuses on those sections of the RTP that are related to the underlying statutory

provision(s) from which the exemption was granted. *Minnesota Commercial Ry.* Thus, in determining whether revocation of any of the categorical exemptions at issue in this proceeding is warranted, the “essential issue” is whether railroads exercise market power over the subject commodity(ies) to such an extent that regulation of rates and service terms for those traffic segments is necessary to protect the public. See *WTL Rail Corp. – Petition for Declaratory Order and Interim Relief*, STB Docket No. NOR 42092, slip op. at 3 (served Feb. 17, 2006) (citing *Rail Exemption Misc. Agricultural Commodities*, 8 I.C.C.2d 674, 682 (1992)). As CP demonstrates in Part II below, the ICC’s findings concerning the highly competitive nature of the traffic that is subject to the categorical exemptions remain true today, and there is no legal or factual basis that would support a conclusion that regulation of exempt commodities is now necessary to further the goals of the RTP.

The *October 25 Decision* raises the further question whether, even if revocation of one or more categorical exemptions is not warranted at this time, those exemptions nevertheless ought to be subject to “periodic review.” *October 25 Decision* at 3. The answer to that question is “no.” Absent a persuasive showing that a particular exemption is no longer consistent with the RTP, there is simply no reason to “revisit” the wisdom of the ICC’s categorical exemptions on a periodic basis. Such general review proceedings would be the epitome of unnecessary regulation that Congress’ policy directives have consistently sought to eliminate. The procedure contemplated by Section 10502(d) – pursuant to which a party, upon demonstrating “reasonable, specific concerns” that warrant revocation, may petition the Board to institute a proceeding to consider revoking a specific exemption (or elements thereof) – is appropriately designed to

safeguard the public interest without imposing substantial and unnecessary regulatory burdens on carriers and shippers.<sup>5</sup>

**C. The Governing Legal Standards Have Not Changed Since The Categorical Exemptions Were Promulgated.**

The *October 25 Decision* (at 3) suggests that the passage of time may provide reasons to reconsider the categorical exemptions. Specifically, the Board observes that “as long as 30 years have passed since the adoption of many of these exemptions,” and poses the question whether “changes in the competitive landscape and the railroad industry that have occurred over the past few decades” may warrant “explor[ing] the continuing utility” of the TOFC/COFC, Boxcar and commodity exemptions. *Id.* Neither developments affecting the rail industry in the post-Staggers era nor any change in the law justifies a deviation from the clear Congressional policy directives upon which the categorical exemptions are based.

As CP demonstrates in Part II below, there are no changed factual circumstances that would vitiate the prior findings of the Board and its predecessor, the ICC, that regulation of exempted traffic is not necessary to further the goals of the RTP. The categorical exemptions at issue in this proceeding have delivered the beneficial results anticipated by the ICC in its exemption decisions. And those benefits have been achieved without any adverse impact on the effectiveness of competition for the subject traffic – in fact, competition for exempt rail traffic is even more vigorous today than it was 20 years ago.

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<sup>5</sup> Indeed, it is not clear that the Board has authority to initiate a proceeding to “review” or revoke a categorical exemption *sua sponte*. While the provision of Section 10502 that governs proceedings to establish an exemption states that “[t]he Board may, where appropriate, begin a proceeding under this section on its own initiative,” 49 U.S.C. § 10502(b) (emphasis added), the provision governing revocation proceedings contains no such language, stating instead that “[t]he Board shall, within 90 days after receipt of a request for revocation under this subsection, determine whether to begin an appropriate proceeding.” 49 U.S.C. § 10502(d)(emphasis added).

There is no question that railroads are financially better off today than they were when the categorical exemptions were put in place. However, a healthier railroad industry should not be a cause for concern – much less a reason to reverse the deregulatory policies that helped the industry to survive, renew its infrastructure and deliver increasingly efficient service to shippers. To the contrary, the Staggers Act's provisions – including a broadened exemption statute that affirmatively directed the ICC to utilize it “to the maximum extent” consistent with the RTP – were expressly intended to promote the financial health of America's railroads. The RTP likewise instructs the Board to pursue policies that “minimize the need for Federal regulatory control over the rail transportation system” and “allow[ ] rail carriers to earn adequate revenues.” 49 U.S.C. § 10101.

More importantly, there has not been any change in the statute or Congress' policy directives that would justify elimination of (or substantial modifications to) the categorical exemptions. In enacting ICCTA, Congress reaffirmed its intent to “make[] it an explicit part of the agency's statutory duty to utilize exemptions to the maximum extent permissible under the law.” H.R. Rep. No. 311, 104th Cong. 1st Sess. 96 (1995). The notion that the mere passage of time warrants a wholesale reconsideration of categorical exemptions that have benefited both carriers and shippers for decades is fundamentally at odds with the Board's governing statute.

Both the legislative history of Section 10502 and judicial precedents interpreting that statute demonstrate that Congress did not intend to give the Board a roving mandate to “re-regulate” by rolling back previously approved exemptions on its own initiative. Rather, the statutory scheme adopted by Congress envisions that revocation should be considered, on a case-by-case basis, based upon a clear showing that reassertion of regulation is necessary to correct an actual abuse of market power. H.R. Conf. Rep. No. 1430, 96th Cong., 2d Sess. 105 (1980), U.S.

Code Cong. & Admin. News 1980, pp. 3978, 4137. See also *Ill. Commerce Comm'n v. I.C.C.*, 819 F.2d 311, 316 (D.C. Cir. 1987) (approving the Commission's "determin[ation] that the chances of market power abuses arising from the [trackage rights] exemption were remote and that it was not necessary to withhold the general exemption in order to protect shippers from this remote possibility; the rare cases of market power abuse could be remedied in subsequent proceedings"); *Brae Corp. v. United States*, 740 F.2d 1023, 1043 (D.C. Cir. 1984) ("Congress itself envisioned after the fact review to correct isolated market abuses that may follow the lifting of protective regulations"). The revocation mechanism that Congress provided is set forth in Section 10502(d), which contemplates targeted requests for revocation based upon demonstrated abuses of market power in specific instances, not vague "informal inquiries" questioning the "relevance" or "continuing utility" of the categorical exemptions.

## **II. THERE IS NO CREDIBLE EVIDENCE TO SUPPORT REVOCATION OF THE BOARD'S CATEGORICAL EXEMPTIONS.**

The *October 25 Decision* requests comments regarding whether "the rationale behind any of these [categorical] exemptions should be revisited." *October 25 Decision* at 3. Specifically, the Decision poses the question whether "changes in the competitive landscape and the railroad industry that have occurred over the past few decades" warrant reconsideration of one or more categorical exemptions. *Id.* As this part of CP's Comments demonstrates, there is no credible evidence to support a conclusion that changes in the rail industry since the categorical exemptions were adopted now require the Board to re-impose rate and/or service regulation on the subject traffic in order to carry out the goals of the RTP. To the contrary, the evidence clearly indicates that the exemptions have promoted the policies embodied in the RTP, and continue to do so today.

A recent study of competition in the railroad industry commissioned by the Board, and conducted by Christensen Associates, found that the deregulatory policies of the Staggers Act have greatly benefited both carriers and shippers:

The deregulation of the railroad industry ushered in increased market flexibility, competitive and differential rates for rail service, and a climate open to innovation. In the years following the passage of The Staggers Act, the railroad industry experienced dramatic reductions in costs and increased productivity, which yielded higher returns for carriers and lower inflation-adjusted rates for shippers. Thus both railroads and their customers benefited from regulatory reform.<sup>6</sup>

The Christensen Report examined rate trends across many types of traffic, including both regulated commodities and others that have been exempted. Based upon that analysis, Christensen Associates concluded that the “increase in railroad rates experienced in recent years is the result of declining productivity growth and increased costs rather than the increased exercise of market power.” Christensen Report at ES-5 (emphasis added). A supplement to the Christensen Report published in January 2010 reaffirmed that key finding.<sup>7</sup> The Christensen Report fatally undermines any suggestion that developments in the rail industry in the post-Staggers era have given rise to a need for the Board to reassert regulatory jurisdiction over traffic that was deregulated pursuant to Section 10502.

The Preliminary National Rail Plan issued by the Federal Railroad Administration in 2009 likewise concluded that the deregulatory policies of the Staggers Act have resulted in a more healthy and highly competitive rail industry:

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<sup>6</sup> Laurits R. Christensen Assocs., *A Study of Competition in the U.S. Freight Railroad Industry And Analysis of Proposals That Might Enhance Competition: Revised Final Report*, ES-1 (Nov. 2009) (“Christensen Report”) (emphasis added).

<sup>7</sup> Laurits R. Christensen Assocs., *An Update to the Study of Competition in the U.S. Freight Railroad Industry: Final Report*, at 4-11 (Jan. 2010) (“Christensen Update”).

**“By many measures, the U.S. freight rail system is the safest, most efficient and cost effective in the world . . . . Before 1980, when railroads were partially deregulated, they focused on survival. In recent years, they have been thriving and privately funded freight railroads have focused on enhancing the reliability of their service and their intermodal capacity . . . . A review of the previous 29 years since the railroads were partially deregulated by the Staggers Act of 1980 reveals improvements in the railroads’ physical plant (infrastructure) as well as their performance metrics. Safety and fuel efficiency have remarkably improved. Rail rates are lower today than in 1980, when compared in constant dollars.”<sup>8</sup>**

FRA cautioned that “[f]reight rail infrastructure maintenance and capacity enhancements, however, can only occur with Federal legislation and policies that allow rail carriers to earn revenues that are sufficient to encourage their continued investment in the system.” *Id.* at 9.

Further telling evidence that the categorical exemptions have not generated any material anticompetitive consequences is the fact that, in more than 25 years of experience, only a handful of requests have been filed pursuant to Section 10502(d) seeking revocation of a categorical commodity exemption. Those few revocation petitions involved peripheral issues such as the use of privately-owned trailers by railroads in providing intermodal services<sup>9</sup> or the alleged failure of an individual carrier to provide adequate service.<sup>10</sup> Until now (in an obvious response to the October 25 Decision), no party has ever requested that the Board to revoke a categorical

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<sup>8</sup> Federal Railroad Administration, *Preliminary National Rail Plan: The Groundwork for Developing Policies to Improve The United States Rail System* (October 15, 2009) at 4, 9 (emphasis added).

<sup>9</sup> See *American Rail Heritage v. CSX Transp.*, ICC Docket No. 40774, 1995 WL 358842 at \*2 (served June 16, 1995) (“*American Rail Heritage*”); *WTL Rail Corp. – Petition for Declaratory Order and Interim Relief*, STB Docket No. NOR 42092, slip op. at 3 (served Feb. 17, 2006) (“*WTL*”).

<sup>10</sup> E.g., *Roseburg Forest Prods. Co. – Alternative Rail Service – Cent. Oregon & Pac. R.R., Inc.*, STB Fin. Docket No. 35175, Ex Parte No. 346 (Sub-No. 25-C), slip op. at 1-2 (served March 4, 2009) (noting petitioners sought partial revocation of class exemption for lumber and wood products).

exemption in its entirety.<sup>11</sup> Moreover, the Board has never found that wholesale revocation of a categorical commodity exemption was necessary to carry out the RTP.

To the contrary, the Board's few revocation decisions confirm the wisdom of its categorical exemptions. For example, in *American Rail Heritage*, the ICC found that "[t]he [TOFC/COFC] exemption has been in effect since 1981, and the national transportation system, insofar as it involves intermodal transportation, has not only survived but flourished." *American Rail Heritage* at \*4. Likewise, in rejecting a petition for partial revocation of the TOFC/COFC exemption in *WTL*, the Board found that:

Shippers can truck their freight to any railroad intermodal ramp, or move it entirely over the highways, enabling them to choose the most effective and commercially responsive service and price offerings . . . . These options effectively constrain the railroads' market power with respect to TOFC service and equipment. *WTL* has not shown that intermodal service today is inadequate. On the contrary, the record amply documents that intermodal service is characterized by rapid growth and commercial innovations to meet customer demands.

*WTL* at 2, 4 (reiterating prior ICC findings).

In short, the quantitative evidence shows that the level of competition that North American railroads face today is no less vigorous than it was at the time the ICC promulgated the categorical exemptions at issue in this proceeding. As a railroad headquartered in a trade-dependent country (Canada) that conducts substantial rail operations both cross-border and within the United States, CP's experience is that the intensity of competition for rail business is greater today than it was twenty years ago. As the following discussion of the principal exempt commodities handled by CP in cross-border and U.S. domestic service demonstrates, the rationales underlying the ICC's exemption of TOFC/COFC traffic and other commodity groups

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<sup>11</sup> See *Comments of Washington State Potato Comm'n*, (Jan. 24, 2011); *Comments of Consumers United for Rail Equity*, (Jan. 26, 2011).

remain valid today, and strongly support the continued exemption of those traffic sectors from burdensome and unnecessary rate and service regulation.

**A. Intermodal Traffic**

The ICC exempted the rail portion of TOFC and COFC service from regulation in *Improvement of TOFC/COFC Regulation*, 364 I.C.C. 731 (1981), *aff'd in relevant part sub nom. American Trucking Ass'ns v. ICC*, 656 F.2d 1115 (5th Cir. 1981).<sup>12</sup> In granting the exemption, the ICC found that “this traffic is highly competitive with motor carrier service . . . . Neither mode has the inherent ability to dominate the market for the type of freight which is shipped in trucks or containers.” *Notice of Proposed Rulemaking*, 45 Fed. Reg. 79123, 79123 (Nov. 28, 1980), *adopted in* 364 I.C.C. at 732. Based upon those findings, the agency concluded that “the potential for railroad abuses of market power in TOFC/COFC service is virtually non-existent.” *Id.* (emphasis added). The Commission found that an exemption would promote the goals of the RTP by “plac[ing] primary reliance on market forces, not government regulations, to establish reasonable rates and maintain necessary services.” *Id.* at 79124. The ICC also predicted that the exemption would benefit both carriers and shippers by eliminating “complex and inflexible rate structures and service plans” and freeing them to respond quickly to marketplace initiatives by non-regulated competitors. *Id.* at 79123.

The TOFC/COFC exemption has been one of the great success stories of the post-Staggers era. Freedom from excessive regulation enabled rail carriers to increase the volume of

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<sup>12</sup> The ICC subsequently extended the exemption to include the provision of motor carrier service as part of an intermodal movement in *Improvement of TOFC/COFC Regulations (Railroad-Affiliated Motor Carriers and Other Motor Carriers)*, 3 I.C.C.2d 869 (1987). Two years later, the ICC exempted from economic regulation virtually all remaining services related to intermodal shipments. *Improvement of TOFC/COFC Regulations (Pickup and Delivery)*, 6 I.C.C.2d 208 (1989), *aff'd sub nom. Central States Motor Freight Bureau, Inc. v. ICC*, 924 F.2d 1099 (D.C. Cir. 1991).

intermodal shipments from approximately 3 million containers and trailers in 1980 to more than 12 million units in 2006.<sup>13</sup> As these data graphically demonstrate, intermodal traffic is now the fastest growing business sector for North America's railroads. The ability to respond rapidly to changing market conditions fostered innovative new service offerings by railroads, ocean carriers and third parties. The exemption of intermodal traffic also generated significant environmental benefits, as railroads have succeeded in diverting massive numbers of trucks from the highways.

Any suggestion that "changes in the competitive landscape" over this time period warrant a rollback of the TOFC/COFC exemption is simply wrong. The rail consolidations of the 1980s and 1990s increased the competitive alternatives for intermodal shippers by creating new single-line services and routing options. For example, the acquisition of the former Conrail system by Norfolk Southern and CSXT created strong two-carrier rail competition at the Port of New York/New Jersey, which had previously been served exclusively by Conrail. In approving that transaction, the Board found that it "will significantly expand rail intermodal service offerings in the Eastern United States, and enhance the already substantial level of rail/truck competition for this important transportation service." *CSX Corp. & Norfolk Southern Corp. – Control and Operating Agreements/Leases – Conrail, Inc.*, 3 S.T.B. 196, 327 (1998) (emphasis added).

Likewise, in the *Burlington Northern-Santa Fe Merger* decision, the Board held that:

"the expanded coverage of regions and ports should increase the options of intermodal shippers that require transportation from and to numerous sources and destinations. Those shippers will have a single-line network connecting them to almost all major western ports and important inland hubs such as Birmingham, Memphis, Dallas, Houston, St. Paul, and Chicago. This has the potential to enhance US competitiveness in export commerce and to create additional single-line opportunities among Canada, the United

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<sup>13</sup> See *Railroad Facts*, Association of American Railroads (2010) at 26. Intermodal volumes declined from the 2006 level during the 2008-2009 recessionary period, but have more recently staged a recovery.

**States and Mexico. Burlington Northern, Inc.,—Control and Merger – Santa Fe Pacific Corp., 10 I.C.C. 2d 661, 737 (1995).**

More recently, CN's acquisition of Wisconsin Central and the Elgin, Joliet and Eastern Railway, in conjunction with the opening of an efficient, modern container terminal at Prince Rupert, BC, created a strong new competitive alternative for containers moving between Asia and the U.S. Midwest. To the south, Kansas City Southern's ("KCS's") acquisition of TFM positioned it to participate in the development of new intermodal terminal facilities at the Mexican port of Lazaro Cardenas. Container volume moving via Lazaro Cardenas has grown rapidly, from 43,445 TEUs in 2004 to 591,467 TEUs in 2009,<sup>14</sup> and plans are in place to increase capacity at the port to 2.2 million TEUs annually.<sup>15</sup> The emergence of new port facilities at Prince Rupert and Lazaro Cardenas provide even more potential routing options for intermodal cargo moving to and from the interior United States.

CP and other rail carriers compete to participate in the movement of international container traffic as but one link in a global supply chain that, in turn, competes with other supply chains involving other product sources, ocean shipping companies, ports, surface carriers and third parties. The routing of international container traffic is largely controlled by the ocean shipping lines, but other parties in the supply chain can also influence the ports and routes selected to move the traffic.

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<sup>14</sup> Lazaro Cardenas Port, *Movimiento Portuario de Carga –Historico*, available at [http://puertolazarocardenas.com.mx/Docs%20pdf/Puerto/Mov\\_Historico.pdf](http://puertolazarocardenas.com.mx/Docs%20pdf/Puerto/Mov_Historico.pdf) (last visited Jan 28, 2011); *Press Release: The Port Breaks in 2010 Cargo Handle*, (Feb. 17, 2000), available at <http://www.lazarocardenasport.com.mx/english/index.php/news/24-cargo-handle-january> (last visited Jan 28, 2011).

<sup>15</sup> See Lazaro Cardenas Port, *Business Projects*, available at <http://www.lazarocardenasport.com.mx/english/index.php/business-opportunities/business-projects> (last visited Jan 28, 2011).

CP faces intense competition for international container freight from a variety of sources, including other railroads, motor carrier service, competing intermodal terminals at the ports it serves, and water-rail routes via alternate ports. In the West, CP provides intermodal service via the Port of Vancouver to and from the U.S. Midwest. Competitive options available for such movements include CN rail service via both Vancouver and Prince Rupert, BC, as well as alternative water and rail carrier services operating between the Midwest and the ports of Seattle/Tacoma and Los Angeles/Long Beach. In the East, CP intermodal service between the Port of Montreal and the U.S. Midwest competes with efficient service offerings from CN (via Halifax and Montreal) and both Norfolk Southern and CSXT (via New York/New Jersey, Philadelphia, Baltimore and other East Coast ports). Water routings via East Coast ports also compete with CP's Vancouver service offering for shipments to and from Asia. The percentage of container traffic between Northeast Asia and the U.S. East Coast that moves via the Panama Canal to East Coast ports has tripled over the past decade. The Panama Canal expansion project, which is slated for completion in 2014, will further enhance the competitiveness of container routings via East Coast ports.<sup>16</sup> The multitude of port and inland rail routing options now available to international container shippers is depicted in Exhibit A.<sup>17</sup> As a result of these competitive dynamics, intermodal traffic shifts between ports and supply chains on an almost daily basis for wide variety of reasons (including reasons totally unrelated to the pricing and quality of rail service).

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<sup>16</sup> See Jean-Paul Rodrigue, Van Horne Institute, *Factors Impacting N. American Freight Distribution in View of the Panama Canal Expansion* 31 (2010) ("East and Gulf coast ports see the expansion of the Panama Canal as an opportunity to increase cargo volumes and gather a greater share of the transpacific trade") (emphasis in original).

<sup>17</sup> *Id.* at 27 fig. 11: *Standard Transit Times from Shanghai and North American Routing Options (in Days)* (attached as Exhibit A).

CP also faces substantial competition from motor carriers for both international and “domestic” intermodal traffic. International containers that formerly moved via CP service between the Port of New York/New Jersey and points in Canada (including Montreal and Toronto) now move over all-rail and rail/truck routes originated by a competing railroad at the same port. The relatively short distance between the New York metropolitan area and both Montreal and Toronto also makes direct truck service between those points an attractive competitive option.

Competition for domestic transborder TOFC/COFC traffic is likewise intensely competitive. Because every domestic intermodal shipment begins and ends with a truck movement (from the point of origin to an intermodal ramp, and from another intermodal terminal to the ultimate destination), CP must compete for such traffic with other railroads (and intermodal facilities located along their lines). For all but the longest movements, direct truck service offers yet another viable competitive option for domestic intermodal shipments. Third parties also play a significant role in determining the carriers, routes and supply chains selected to handle domestic intermodal traffic. In particular, third party logistics companies oversee virtually all CP cross-border domestic intermodal shipments. The vigor of competition that CP (and other railroads) face for domestic intermodal traffic is reflected in the constant turnover of customers and revenues in that intermodal business sector. Shifting price/service/equipment-supply bids by CP and its competitors result in annual revenue “churn” (the absolute value of the sum of revenue gains and losses) in an amount equal to 10-15% of CP’s total domestic intermodal revenues.

There is also increasing competition among railroads and their supply chain partners for investments in infrastructure. Railroads compete vigorously to site new intermodal facilities on

their lines. That competition imposes downward pressure on the negotiated rail rates for traffic that will use such facilities. Regulatory changes that impair the ability of railroads to earn the returns necessary to support these initiatives could jeopardize future supply chain investment.

In short, the fundamental premise underlying the TOFC/COFC exemption – i.e., that the transportation of intermodal traffic is highly competitive – is even more true today than it was when the TOFC/COFC exemption was promulgated.

#### **B. Forest Products**

Forest products, including lumber, pulp and paper, account for a substantial portion of CP's cross-border exempt commodity traffic. The transportation by rail of forest products traffic was exempted from regulation by the ICC in *Rail Gen. Exemption Auth. – Lumber or Wood Products*, Ex Parte No. 346 (Sub-No. 25), 7 I.C.C.2d 673, 676 (1991) ("*Forest Products Exemption*"). Virtually every party (carrier and shipper alike) that filed comments in the proceeding supported the forest products exemption. *Id.* at 674. In granting the exemption, the ICC noted that "lumber shippers emphatically, and almost without exception, state that there is substantial intermodal and intramodal competition for their traffic and that present regulation inhibits the railroads from competing with other modes." *Id.* at 677. The agency further found that "rate levels on these products are substantially below the threshold levels for Commission maximum rate reasonableness intervention. Rates at those levels are conclusively presumed to be effectively competitive under the Act." *Id.* at 676 (emphasis added).

Neither any "change[ ] in the competitive landscape" nor any development in the rail industry since the forest products exemption became effective provides a basis for calling into question the continuing wisdom of exempting this traffic from unnecessary and burdensome rate and service regulation. To the contrary, the transportation of forest products throughout North America continues to be subject to strong competitive forces. The vast majority of CP forest

products traffic that originates or terminates in the United States originates at a point that has access to more than one rail carrier, either directly or via a reload center located on a second railroad's lines. Mills served by CP have the ability to move their products by truck to a reload center served by CN or another railroad. Conversely, CP utilizes reload centers to attract business from mills that are not situated on its lines. The United States is a key end market for Canadian forest products producers, and reload centers play a critical role in the logistics strategies of those firms. CP regularly experiences both traffic gains and losses in response to its pricing and service actions and the corresponding commercial strategies of its Canadian and U.S. railroad competitors. Moreover, the role of motor carriers in the movement of cross-border forest products is not limited to that of delivering products to a reload center. Trucks also compete directly with CP for line haul shipments of forest products to a variety of U.S. destinations.

CP's forest products traffic is also subject to substantial product and geographic competition. CP lumber, newsprint, paper and pulp customers compete among themselves, and with other Canadian producers and producers located in the U.S. Pacific Northwest and Southeast. Forest products originating in offshore countries also compete with North American products for U.S. sales. The potential destinations for CP-served forest products are also geographically diverse, creating numerous routing and end market possibilities for our customers. The geographic diversity of these shipments, and the large number of North American and foreign suppliers, create very strong commodity-based and location-based competition in forest products markets.

Another source of competitive pressure on rates and service offerings for forest products is the increasing displacement of newspapers and other printed materials by electronic media.

The long term decline in demand for forest products in the “digital age” places downward pressure on rail freight rates, as CP (and other carriers) seek to assist their customers in remaining competitive in their product markets. This technology-driven competitive phenomenon did not exist at the time the ICC exempted forest products traffic from regulation. One of the principal reasons for granting the exemption was the ICC’s finding that “[n]umerous shippers indicate that they need to be able to respond immediately and flexibly to compete in their own markets.” *Forest Products Exemption*, 7 I.C.C. 2d at 675. Re-regulating forest products traffic would reduce the flexibility available to North American forest products shippers in making their transportation arrangements at a time when they are increasingly vulnerable to offshore competition and technological obsolescence.

Perhaps the most compelling proof that CP (and other rail carriers) do not possess – much less exercise – market power with respect to forest products traffic is the fact that the vast majority of forest products shipments continue to move at rates below the jurisdictional threshold for STB rate reasonableness regulation. Approximately 85% of all CP forest products shipments move at rates reflecting an R/VC ratio of 180% or less. As the ICC found in *Forest Products Exemption*, such rates are “conclusively presumed to be effectively competitive.” 7 I.C.C. 2d at 676. Thus, revocation of the forest products exemption would serve no meaningful shipper protection purpose, as the vast majority of carrier rates for that traffic are, in any event, below the jurisdictional threshold.

For these reasons, there is no basis in law or fact for the Board to “revisit” the forest products exemption.

### **C. Transportation Equipment**

Motor vehicles and parts shipments also account for a substantial portion of CP’s exempt traffic. The transportation of motor vehicles (STCC 37) by rail was exempted from regulation by

the ICC in *Rail Gen. Exemption Auth. – Transportation Equipment*, Ex Parte No. 346 (Sub-No. 27), 9 I.C.C. 2d 263 (1993) (“*Transportation Equipment Exemption*”). The exemption of shipments of motor vehicles and parts was strongly endorsed by the Motor Vehicle Manufacturers Association. *Id.* at 264. Indeed, the only party to oppose the exemption was Patrick W. Simmons (on behalf of the UTU Illinois Legislative Board), who expressed concern that an exemption would generate “reckless competition between rail carriers” that might lead to requests by the railroads for concessions from their organized employees. *Id.*

In granting the exemption, the ICC concluded that “[w]e are convinced that regulation is not necessary to carry out the RTP.” *Id.* at 265. This conclusion was supported by a finding that “there is, overall, effective competition for the rail transportation of motor vehicles and vehicle parts and accessories.” *Id.* In addition to modal competition, the Commission found that rates for motor vehicle traffic were constrained by “[g]eographic competition and the bargaining power and business options possessed by the automobile industry.” *Rail Gen. Exemption Auth. – Transportation Equipment*, Ex Parte No. 346 (Sub-No. 27), 1992 WL 1567 at \*2 (decision served July 9, 1992). The ICC also found that granting the exemption would promote the goals of the RTP by “reliev[ing] administrative and paperwork burdens associated with tariff filing and contract summary filing,” and by “allow[ing] quick and unhindered rate and service adjustments when changed market conditions mandate them.” *Id.* at \*3.

The ICC’s findings regarding the vigor of competition for motor vehicle traffic are equally valid today. The transportation of automotive traffic is subject to a high degree of inter- and intramodal competition. Trucks continue to enjoy a dominant position with respect to the transportation of vehicle parts, due in large measure to the greater service flexibility of motor carriage. CN is CP’s principal rail competitor for U.S.-bound vehicle shipments originating in

Canada, while northbound transborder and domestic U.S. shipments are subject to competitive pressure from additional rail routing options and direct truck service. Railroads have extended their competitive reach by gaining access to vehicle manufacturing facilities located on the lines of other rail carriers via truck-served reload centers. The distribution of automotive origins and destinations, and the wide range of lengths of haul associated with automotive traffic movements, make trucks a significant competitive threat to railroads for many shipments. Indeed, very recently, a U.S.-based auto manufacturer shifted its Canada-bound traffic from CP to a trucking company.

Geographic competition and shipper leverage play a major role in constraining rail rates for motor vehicle traffic, as they did at the time the transportation equipment exemption was promulgated. As the ICC observed, motor vehicle manufacturers are large, sophisticated companies that exercise significant negotiating leverage in a variety of ways. Automotive shippers distribute their business among multiple railroads in order to prevent any one carrier from acquiring market power over their traffic. They take advantage of the geographic dispersion of automobile manufacturing facilities by "bundling" their business during rail contract negotiations. This practice enables vehicle manufacturers to use the competitive leverage that exists at plants served by multiple railroads to obtain favorable rates for shipments to and from other facilities that enjoy fewer direct competitive options.

Approximately 94% of all CP motor vehicle and parts shipments move at rates reflecting an R/VC ratio of 180% or less. The fact that most rail shipments of motor vehicles and parts move at rates below the jurisdictional threshold for STB rate reasonableness jurisdiction constitutes powerful evidence that those rates are "effectively competitive." *Forest Products Exemption*, 7 I.C.C. 2d at 676. As in the case of forest products, revocation of the transportation

equipment exemption would serve no meaningful purpose, as the vast majority of carrier rates for that traffic are, in any event, below the jurisdictional threshold. Moreover, no motor vehicle shipper has ever filed a petition seeking revocation of any aspect of the transportation equipment exemption.

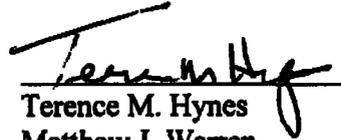
For these reasons, revocation of the transportation equipment exemption, in whole or in part, would be patently inconsistent with both the policies set forth in the RTP and Congress' directive in Section 10502.

### CONCLUSION

As the foregoing Comments show, the categorical exemptions promulgated by the ICC pursuant to the Staggers Act have greatly benefited both railroads and their customers. The transportation of TOFC/COFC traffic and other exempt commodities remains intensely competitive – indeed, such shipments are subject to even greater competitive forces today than they were decades ago. There is no legitimate reason for the Board to “revisit” the rationale underlying the categorical exemptions, or to subject them to periodic review going forward. Rather, as Congress has directed, the Board should continue to exempt rail transportation from regulation to the maximum extent possible, and rely upon petitions for revocation filed by shippers or other interested parties on a case-by-case basis as the method for addressing any isolated concerns regarding the exemptions that may arise from time to time.

For these reasons, CP respectfully requests that the Board dismiss this proceeding.

Respectfully submitted,



Terence M. Hynes  
Matthew J. Warren  
Noah A. Clements  
Sidley Austin LLP  
1501 K Street, N.W.  
Washington, D.C. 20005  
(202) 736-8000

Paul Guthrie  
Vice President – Legal Services  
Canadian Pacific Railway Company  
401 9<sup>th</sup> Avenue, S.W.  
Gulf Canada Square, Suite 500  
Calgary, Alberta T2P 4Z4 Canada

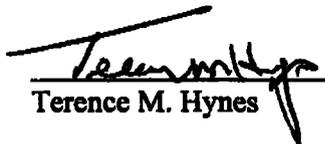
Patrick Riley  
Director – Legal Regulatory Affairs  
Canadian Pacific Railway Company  
401 9<sup>th</sup> Avenue, S.W., Suite 920  
Gulf Canada Square, Suite 500  
Calgary, Alberta T2P 4Z4 Canada

*Counsel for Canadian Pacific Railway Company*

Dated: January 31, 2011

**CERTIFICATE OF SERVICE**

I hereby certify that I have caused the foregoing Comments of Canadian Pacific Railway Company to be served by first class mail, postage prepaid, this 31st day of January 2011, on all parties of record.

  
Terence M. Hynes

# Exhibit A

## Figure 11: Standard Transit Times from Shanghai and North American Routing Options (in Days)

