BEFORE THE

INTERSTATE COMMERCE COMMISSION

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In the Matter of: :

SANTA FE SOUTHERN PACIFIC CORPORATION : Finance Docket

-- CONTROL -- : 30400 et al.

SOUTHERN PACIFIC TRANSPORTATION :

COMPANY :

- x

Hearing Room A

12th & Constitution, N.W.

Washington, D.C.

Wednesday, January 16, 1985

The hearing in the above-entitled matter was convened, pursuant to notice, at 9:05 a.m.

BEFORE:

JAMES E. HOPKINS,

Administrative Law Judge

APPEARANCES:

As Heretofore Noted

C O N T E N T S

WITNESS	DIRECT	CROSS	REDIRECT	RECROSS
George F. Bardwell				
By Mr. Kenzie	7505			
By Mr. Wilson		7508		
I. William Ploth				
By Mr. Dreiling	7512			
By Mr. Wilson		7513		
By mr. Budeiri		7639		
By Mr. Dreiling			7648	
By Mr. Wilson				7652
Hilary Rawert				
By Mr. Raker	7656			
By Mr. Moates		7659		
By Mr. Raker			7707	
By Mr. Moates				7709
Donald L. Graf				
By Mr. Raker	7711			
By Mr. Moates		7712		

E X H I B I T S

Exhibit no.	IDENTIFIED	RECEIVED
DRGW-C-37	7507	
SFSP-C-99	7560	7653
SFSP-C-100	7572	7653
SFSP-C-101	7716	7747
SFSP-C-102	7720	7747
SFSP-C-103	7721	7747

PROCEEDINGS

JUDGE HOPKINS: Let's get on the record.

Are there a few preliminary matters?

MR. MOATES: Yes, Your Honor, if I may. Applicants have agreed with counsel for Union Pacific/Missouri Pacific that we will waive the appearance for cross examination of UP witness Kauders, K-a-u-d-e-r-s.

As Your Honor will recall, counsel for Arizona Electric, which has intervened in the UP/MP trackage rights dockets, indicated a desire to cross examine UP witnesses Kauders and Craig, and we, I think, informed Your Honor that we would reserve an objection to the appropriate time with respect to that request.

Since we are prepared to waive Mr. Kauders for purposes of live appearance, I think the time has come. We would like to make a presentation to Your Honor on the objection, and I think counsel for Arizona Electric are present, and they can respond, and hopefully we can clear this matter up.

JUDGE HOPKINS: Why don't we do this right away?

MR. MOATES: Your Honor, the basis for our objection is really straightforward, and it is twofold. First of all, Arizona Electric Power Cooperative filed

comments on November 21, 1984, in Finance Docket 30400, Sub Number 16 which is the Union Pacific trackage rights request.

In that submission, they state quite clearly on Page 3, under the caption Summary of Position, that they in their words "strongly support the UP/MP application" with a single modification, and the modification they seek is that the rights actually be expanded to include service to the Arizona Electric Power facility at Cochise, Arizona, which today is an exclusively served point on the Southern Pacific, and which Union Pacific/Missouri Pacific does not seek to serve in its application.

So, the first basis for the objection is very straightforward, and that is that this party is not an adverse party to the Union Pacific, and a so-called examination would not be cross examination. These are not adversarial parties.

To the extent that Arizona Electric indicates it may wish to obtain some information from witnesses Vaudera or Craig, we submit that there are other ways to do that than the vehicle of cross examination, which is reserved for the adversarial development of facts by parties of contrasting positions.

Secondarily, Your Honor, to the extent that

the request for cross examination is based upon a desire to explore the willingness of the Union Pacific to accept this modification to its proposal, which Arizona Electric proposes, or to even determine what counsel may think are relevant facts to support their request to the Commission, and the Commission ordered that, we would object to any such examination on the grounds that the Commission has made it eminently clear that conditions on a merger will not be predicated on a preexisting, alleged preexisting problem with competition.

And in this regard the filing of Arizona Electric on its face makes it clear that that is what they are dealing with here. They concede that the coal movement that they are concerned about, which is one that originates on the Santa Fe at, I believe, Deming, New Mexico, terminates on the Southern Pacific at Cochise, Arizona, moves from a Santa Fe local point to a Southern Pacific local point, and nothing is going to change about that as a result of this merger.

They refer in here several times in somewhat colorful language to what they feel is the difficult situation of the captive shipper client today. We respectfully submit that this is a classic utility rate problem, and that is what we are really looking at here.

It is the kind of problem that the Commission has found is uniquely not suited to be resolved in merger cases, and I draw Your Honor's attention just as an example to the Commission's discussion of conditions criteria in the Union Pacific/Missouri Pacific merger decision. I refer you particularly to 366 ICC at 562 through 564.

I would like to just read a few sentences out of that section. First of all, the Commission noted in that proceeding that the Kansas City Southern in that proceeding was proposing certain conditions that were not related directly to the impact of the merger, and the Commission said as follows about the position of the Departments of Justice and Transportation with respect to that:

"DOT asserts that conditions should be imposed only where needed to ameliorate or eliminate reductions in competition resulting directly from the proposed consolidation.

"DOJ contends that conditions to a rail consolidation should be imposed only when we find that the merger without conditions may be anticompetitive, and that the conditions sought are reasonably designed to remedy directly the anticompetitive effects threatened by the merger.

"DOJ takes the position that before conditions can be imposed upon a merger, it must be shown that the merger may reduce competition in particular markets and that the proposed conditions will lessen or neutralize the anticompetitive thrust of the merger."

The Commission goes on and says that "The position on conditions argued by the DOT and DOJ is consistent with our current policy regarding conditions."

Later, in the next paragraph, they summarize the position and say, "As we stated in BN/Frisco, the conditions on a merger are not to be used to ameliorate long-standing problems which were not created by the merger and are not to be imposed if they are in no way related either directly or indirectly to the involved merger, and are not to be used to require a merged carrier to protect carriers against circumstances not caused by the merged carrier."

So, I think, Your Honor, it is very clear that on the dual bases that counsel seeks to cross examine when they are not in an adversarial position with Union Pacific, and because the purport of any such cross examination would be to deal with this conditional condition that they proposed which we would submit the Commission on its face would find an inappropriate

condition, and which in fact is one which Union Pacific doesn't seek in this case, we would be wasting everybody's time.

So, we strenuously object to the request of Arizona Electric to cross examine any UP witness.

MR. DOWD: Your Honor, Calvin Dowd for Arizona Electric.

Before responding to Mr. Moates' objection, I would ask for what I hope is at this point just a housekeeping matter. Arizona Electric's petition for leave to intervene has yet to be ruled upon by Your Honor. It was filed on the 21st of November. No objections or responses in opposition were received.

Mr. Moates' comments indicate he characterizes APCO effectively as a party intervenor, and other parties have considered us as such.

JUDGE HOPKINS: I will grant the motion to intervene.

MR. DOWD: Thank you, Your Honor.

With respect to Mr. Moates' objections, I would like to take his second point first. The merits of Arizona Electric's substantive request for relief are simply not at issue at this point, nor for that matter is the Commission's policy on trackage rights or the potential for changes in that policy in the future.

At this point the only matter presented is APCO's right to cross examine witnesses in an open hearing, so we don't really see the relevance of any argument with respect to the merits of APCO's comments or its position or the merits of the position of any other party with respect to trackage rights.

With regard to the first objection, that we are not adverse parties, I have several points. First, Arizona Electric has effectively filed comments which, while as a secondary or fallback position, indicate a preference for the Union Pacific's application as filed as an alternative to having it denied altogether.

It is clear that our primary position is one of opposition to a limitation that the UP has placed on its trackage rights application. We have a separate prayer for relief which is different from that of the Union Pacific. We have requested an extension or an expansion of the rights which the UP has sought, and in that respect we do have divergent interests from the Union Pacific on this issue.

The fact of the matter is that our cross examination will -- is designed to clarify the testimony of the Union Pacific witnesses as it relates to our prayer for relief or as it relates to factors relevant to our prayer for relief.

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The purpose of cross examination is not simply to impeach testimony of witnesses, but is also entirely appropriate for clarification of testimony, for examination or exploration within the scope of the direct testimony, of the basis for that testimony, and it is in that spirit and with that intent that our request was filed.

We would also note, Your Honor, that the ICC's regulations regarding the rights of intervenors in no way restrict intervenor's rights to participate. Intervenors are in fact granted full rights as parties in all proceedings in which their petitions are granted.

And the past rulings in this docket, including Your Honor's recent ruling with regard to the Tex-Mex diversion study controversy, indicate a preference in this docket for full development of the record, and for free and open, if you will, exchange with respect to evidence, and that is fully consistent with our request here.

I would also point out that there are parties who are participating in cross examination, specifically the Department of Transportation and Department of Justice and the California Department of Transportation, who are not in adverse postures with either Union

Pacific or Santa Fe, at least not yet, and are going to be cross examining witnesses for parties whose positions they may ultimately support.

We are slightly different. We have indicated a conditional support for one party at the outset, but like these government parties we, or I should say like Arizona Electric, these government parties are not adverse to any participant at this point.

And finally, I would just say to Your Honor that our cross examination, as we have indicated, we request 20 minutes, which we probably will not need, for each witness. We propose to be very brief. We will stay within the scope of each witness's direct examination.

Mr. Moates is very capable, and I am certain he will raise any appropriate objections to the scope of the cross examination, and to any indications that we are going beyond the witness's direct testimony. And even at that point those objections really go more toward the weight that should be attached to the answers that these witnesses would give rather than the propriety of our cross examination.

JUDGE HOPKINS: Thank you, Mr. Dowd.

Mr. Roach?

MR. ROACH: Your Honor, I just want to say

that Union Pacific takes no position on the procedural issue of whether cross examination should be permitted. I would confirm what both counsel stated, which is that our application does not encompass the right to serve a generating plant of the intervenor.

JUDGE HOPKINS: Well, I am going to allow them to cross examine these witnesses. I see a divergency, and even if the Commission has taken a position in its final report in these proceedings, it is very possible the Commission could take a different tactic in another decision, so I am allowing it.

Now, the next stage will be the point about how you are going to handle the cross examination of Mr. Kauders. I understand you want to do it by telephone.

MR. MOATES: That is right. We would then just propose to add counsel for Arizona Electric to the conference call. Now, I assume, Your Honor, that your ruling here certainly doesn't preclude us from making appropriate objections during the course of examination if we find particular questions to be offensive.

JUDGE HOPKINS: Not at all. I am allowing it because there is somewhat of a divergency of the interests of the parties here, and I do want everything out on the record. You struck a point there, Mr. Dowd, that I like, stating for the record.

Anything further? Any other preliminary matters?

MR. ROACH: Well, I would just state, Your Honor, I assume we can work out an informal means of handling this. We are quite willing to cooperate to avoid Mr. Kauders having to make an appearance at the hearings, and I am not clear on --

JUDGE HOPKINS: I had understood that you were going to try and work it out on a telephonic conference.

MR. DOWD: Yes, whatever system they work out is fine with us.

JUDGE HOPKINS: Why don't you work it out? The parties can work that out together.

MR. ROACH: All right, so Mr. Kauders will not be here, and we will work out another procedure.

JUDGE HOPKINS: That is right.

MR. ROACH: One other point, Your Honor. I handed up to you a letter stating that the statement of Mr. Irion is being withdrawn, and the letter explains that the reason for that is that there are discussions toward an agreement on the issue, and it is a relatively minor issue, so we have decided not to take further hearing time on that point.

JUDGE HOPKINS: Is it correct that Dr.

Bardwell is going to be the witness now for the Denver and Rio Grande? Is that our first witness?

MR. WILSON: Yes, Your Honor, for the convenience of Dr. Bardwell, who is scheduled also as a witness for the Rio Grande, we have made an accommodation here to cross examine him on the statement for the Rio Grande first thing.

JUDGE HOPKINS: Off the record.

(Whereupon, a discussion was held off the record.)

JUDGE HOPKINS: Back on the record.

MR. MAC KENZIE: Your Honor, Kevin MacKenzie, appearing for the Denver and Rio Grande.

Whereupon,

GEORGE E. BARDWELL,

was recalled as a witness and, having been previously duly sworn, and was examined and testified further as follows:

DIRECT EXAMINATION

BY MR. MAC KENZIE:

Q Dr. Bardwell, have you prepared a verified statement on behalf of the Denver and Rio Grande in this proceeding?

A I have.

Q And does that statement appear in DRGW-20 as

Appendix C to the Rio Grande's opposition traffic study?

A It does.

Q Are there any changes you wish to make to your verified statement, or to the portions of the Rio Grande's opposition traffic study to which it relates?

A Yes. I should like to make four. On Page 5, where it states "a million random digits" should read "one million random digits."

On Page 7, the bottom figure on the rightmost column, the expansion factor should read 25.3989, not 35.3989.

On Page 8, "a million random digits" should read "one million random digits," the "a" changed to "one."

In Appendix A, the formula for the square of standard error of the mean is not intelligible.

Q Dr. Bardwell, have you prepared a paper that reflects the correct formula?

A I have.

Q Do you have that before you now?

A I do.

Q Does it contain any other corrections to formulas in Appendix A?

A Yes. And then the formula for N has the

bottom index of the submission incorrect. It should read H. Both of those corrections are on another sheet of paper which I have prepared.

MR. MAC KENZIE: Your Honor, I would ask that the sheet of paper to which Dr. Bardwell has referred be marked as DRGW-C next in line, which I believe is 37.

JUDGE HOPKINS: That will be marked for identification.

(The document referred to was marked for identification as Exhibit Number DRGW-C-37.)

BY MR. MAC KENZIE: (Resuming)

Q Now, Dr. Bardwell, with those changes, do you adopt the verified statement that appears as Appendix C to the Rio Grande's opposition traffic study as your statement in this proceeding?

A Yes, I do.

Q Is your statement true and correct to the best of your knowledge, information, and belief?

A To the best of my knowledge.

MR. MAC KENZIE: Your Honor, I tender the witness for cross examination.

JUDGE HOPKINS: Thank you.

Mr. Wilson.

CROSS EXAMINATION

BY MR. WILSON:

Q Good morning, Dr. Bardwell. Dennis Wilson, representing the applicant.

The changes this morning have answered a few of my questions.

I would like to ask you first what was the sampling unit for the Rio Grande rail traffic diversion study?

A The individual car movement as indicated in the statement with regard to the time periods involved.

Q Were cars in multiple car shipments in the Rio Grande traffic study sample assigned actual revenue, or were they assigned average per car revenue for cars in the multiple car shipment?

A In each case the mean revenue or average revenue per car was used.

Q Were you involved, sir, in the decision that Rio Grande's final evaluator, Mr. Brainard, used only two choices, the zero percent and the 100 percent, when he was evaluating the sample?

MR. MAC KENZIE: Just a minute, counsel. I believe in this particular study the evaluator is Mr. Thiessen.

THE WITNESS: It has simply been a

long-standing statistical decision that that should be the case.

BY MR. WILSON: (Resuming)

Q And were your reasons for restricting the choices to zero and 100 here the same as you gave in connection with your cross examination yesterday?

A That is correct.

Q Now, sir, on Page 3 of your verified statement, you state that the results of the traffic diversion study are set forth in the exhibit, the Rio Grande acquisition traffic study that you made changes to, and I have a few questions about those results.

If you could turn to Page 19 of the Rio Grande traffic diversion study, sir, this is the beginning of a 13-page table entitled Summary of DRGW Carload and Revenue Losses by Sample Year, by Class of Traffic, by Origin, by Destination.

Dr. Bardwell, focusing on the first line, which shows traffic between Colorado and California, my question is, what confidence could one have that 168 cars from Colorado to California would have been diverted in 1982?

A Let me indicate at the outset that I did not participate in the tabulation on Pages 15 through 31, and I have in fact no knowledge of the accuracy or

inaccuracy of those figures. I did not participate in them, nor did I calculate a confidence level for any one of the figures except for the totals.

Q Okay. Well, would you agree, sir, that when you are displaying subtotal results of a traffic study such as Rio Grande's traffic study on state-to-state flow bases, that in fact you can attach relatively little confidence to any individual state-to-state flow representation?

A In general, that is true. For the individual figures that are shown on these tables, I cannot vouch for lack of confidence or a great confidence, because I have not looked at the individual variances for these subtotals.

Q Okay. You are familiar, I assume, with the ICC way bill sample and how it is developed, are you not?

A Yes, generally.

Q In your opinion, could you have any confidence in rail market share numbers based on ICC way bill sample data where the flow depicted was a flow from a single BEA to another single BEA?

A It would depend upon whether or not the size of the subgroup was sufficient to give you a substantial -- substantially small sampling error, so I

can't say offhand whether or not I would agree or disagree.

Q Based on your knowledge of the sample, would you say that generally the size of the subgroup would be so small that your standard error would be large?

A Generally, that is true.

Q And if you decided to break the data down further, say, on the basis of a two-digit STCC code breakdown, would that lead to even higher standard errors and even less confidence in the number?

A Generally, that is true.

Q Okay. Thank you, sir. Those are all the questions I have.

JUDGE HOPKINS: Thank you. Anything further, Mr. McKenzie?

MR. MAC KENZIE: Nothing further.

JUDGE HOPKINS: You are excused, sir.

THE WITNESS: Thank you.

(Witness excused.)

MR. MAC KENZIE: Your Honor, I would suggest that we defer moving the admission of D[illegible] Hardwell's verified statement.

JUDGE HOPKINS: As long as you remember it.

MR. MAC KENZIE: We will try to, sir.

JUDGE HOPKINS: Who is next? Mr. Ploth?

MR. WILSON: Mr. Ploth is scheduled as the next witness, Your Honor.

JUDGE HOPKINS: Where are they?

Off the record.

(Pause.)

JUDGE HOPKINS: Back on the record.

MR. DREILING: For the next witness, KCS calls Mr. I.W. Ploth.

Whereupon,

I. WILLIAM PLOTH

was called as a witness, and having been first duly sworn, took the stand, and was examined and testified as follows:

DIRECT EXAMINATION

BY MR. DREILING:

Q Mr. Ploth, would you state your full name for the record?

A My name is I. William Ploth.

Q And by whom are you employed?

A Kansas City Southern Railway Company.

Q And what is your function with Kansas City Southern?

A Vice president, market development.

Q Did you have occasion to prepare and submit on behalf of Kansas City Southern in this proceeding three

verified statements in pleadings designated KCS-12, KCS-14, and KCS-15?

A That's correct.

Q And did you have occasion to submit corrections to those statements in pleadings designated KCS-15 and KCS-18?

A Yes.

Q Those three statements as corrected in the errata to the pleadings, do they constitute your testimony you are offering here today?

A They do.

Q Do you have any further additions or corrections to that testimony?

A None.

Q Are the facts set forth in that testimony true to the best of your knowledge and belief?

A Yes, they are.

MR. DREILING: I tender the witness.

JUDGE HOPKINS: Thank you.

Mr. Wilson.

CROSS EXAMINATION

BY MR. WILSON:

Q Good morning, Mr. Ploth. My name is Dennis Wilson, representing the applicant.

Sir, I would like to question you first about

your verified statement. In KCS-14, on Page 2 of that statement, in the second paragraph, you make the general point that railroads will attempt to obtain their long hauls even where that results in more circuitous, less efficient routings.

Could you give me a few examples, sir, of movements where KCS has obtained its long hauls via circuitous, inefficient routes?

A I think the primary example is traffic that we originate in the Beaumont, Texas, area, Port Arthur, Texas, area, that goes to the southeast, that we haul up through Shreveport. It is a very circuitous route as opposed to SP's and Missouri Pacific's route directly from Beaumont through New Orleans.

Other than that, we don't have the degree of circuity to obtain long haul routings, being a regional carrier, mostly having our traffic connected to other carriers when we originate it or terminate it.

Q What about the Mobil Oil shipments that you originate at Chaison, Texas? You occasionally obtain long haul routes on that, moving the traffic up from the Texas coast area to Kansas City and interchange it with Santa Fe for a movement back southwest to Los Angeles? Isn't that correct?

A There have been times when a movement has

occurred like that. I don't know the frequency of them.

Q Well, in competing for traffic over these less efficient routes, the KCS long haul routes, does KCS have a service disadvantage compared to more efficient rail routes?

A Most usually we do, but again, it depends on the set of circumstances for each individual market that is being served.

Q Does KCS and its connecting line have a cost disadvantage in this type of situation compared to the more efficient rail route?

A Generally speaking, if there is a more efficient single line route, and we have a joint line, a little more circuitous route, there would be less of a cost advantage to us.

Q Now, where KCS has higher costs on a route than does a competing railroad, does that place KCS at a ratemaking disadvantage compared to the competing railroad?

A Again, I would have to say it depends on the market involved, the rate structures that are moving the traffic, what the other rail carrier offers, whether or not the propensity is to observe rates close to the cost level, et cetera.

It is hard to make a general statement that covers everything.

Q Okay. Well, with that qualification, though, would you agree that in general where KCS has higher cost over its rail routes than its competitors do, that KCS is at a ratemaking disadvantage compared to its competing railroads?

A I would have to say generally yes.

Q Now, when KCS has a choice of competing for federal over a long haul, inefficient route and offer a short haul, more efficient route, does KCS generally offer both rates and service via both junctions where the shipper has a choice of two different options by which to route its traffic?

A Normally, our marketing practice is to offer as many routes and junction points as possible for the benefit of the shipper.

Q Okay. And you do this to improve your chances of getting the traffic from the shipper, do you not?

A Yes.

Q And do some shippers split their traffic and sometimes use routes with KCS via a KCS short-haul junction and sometimes use routes with KCS via a KCS long-haul junction?

A Again, I'd say generally that's probably true. Again, it gets to the point of whether or not the specific market allows that type of a split, whether or not contracts are in effect or things of that nature.

Q Now, where KCS has both a long haul, inefficient route and a short haul efficient route, does KCS look at its revenue-cost ratios for traffic on both routes in deciding which route it's going to solicit the hardest to try to sell it to the shipping marketplace?

A Generally, again, yes, that's true.

Q And are there occasions where profit margins on the long haul, inefficient route are lower than the profit margins on the shorter haul, short junction route?

A It's hard to answer, because that's a question that we've been debating for a long time, of whether or not the cash flow produced by the long haul route overcomes the short-range probability as depicted by the formula costing that we go through.

Q Well, what is your view of the matter?

A Again, when I look at specific types of traffic, I have to look at the long-range viability of the movement, the long-range traffic mix the KCS is presently enjoying. If we're going for cash flow, we go for the long route. If we're going for profitability on a short-run basis, we go for the shorter route.

Q Now, in competing for traffic over less efficient routes, does KCS try to match the rate and service offerings that are being offered over the more efficient rail routes?

A Yes.

Q Are there occasions where KCS and its connecting line have trouble matching these rate and service offerings?

A Yes.

Q And where KCS cannot come reasonably close to matching the rate and service offerings of the more efficient route, does it generally get much of the business?

A I hesitate to answer that because I'm not sure what you mean by "much."

Q Does KCS get a small share of the business?

A Could you give me a percentage range that you're looking for, please?

Q Well, where KCS doesn't come reasonably close to matching the rate and service offerings of a competing railroad, about how much business does KCS get?

A Again, it's hard to say, because it depends on the market split, the exact traffic that we're looking at. If you want to generalize, possibly a range of 10 to 30 percent.

Q Now, where KCS is handling traffic over less efficient routes, is it more concerned about that traffic shifting to truck?

A Again, it's hard to say, because we're talking about given market pairs. Now, for certain markets that KCS participates in where truck competition is really not a factor, rail competition is our greatest threat.

And by rail competition I mean rail competitors who are direct line service, either on an origin-destination pair or origin-destination junction pair.

Where we have trucks involved -- I mean truck competition involved -- yes, we are concerned with that and we are concerned about losing it to that operation.

Q Where KCS is handling traffic over less efficient rail routes, is it more concerned by the shipper terminating the movements altogether?

A Could you say that again, please.

Q Where KCS is handling traffic over less efficient rail routes, is it more concerned about that shipper not staying in its markets and therefore not shipping?

A If KCS is the sole serving carrier for that shipper and there are other markets that could displace that shipper's market, yes, we have a concern.

Q Now, on page 3 at the top, sir, you state that you observed a situation where the need to compete intramodally outweighs the need to compete intermodally. My first question is, what do you mean by the phrase "need to compete" in this sentence?

A In this particular paragraph or set of paragraphs, I was referring to the fact that, if true competition exists and the rail carrier is concerned

about losing his market to a truck operation, and there is a more efficient joint line route for him to utilize to bring his cost factors down to the point where they can make a rate that is competitive with the motor carrier, then the propensity should be to engage in that joint line route-making with his joint line connector.

If there is no truck competition or if there is minimal truck competition, the carrier's propensity is to take his long haul route on what margin of traffic he can participate in and forget about trying to get a short-haul joint line route.

Q Okay, sir. And you separately identify a need to compete intermodally and a need to compete intramodally.

A Yes.

Q Now, focusing first on competing intermodally, does KCS compete intermodally for containerizable traffic? That is, freight that can be handled either in a trailer or in a container?

A Generally, yes.

Q And you distinguish this competition from competition for other types of traffic that KCS handles, is that right?

A Vis a vis intramodal, yes.

Q And now, in what ways does KCS compete

differently for this containerizable traffic, the traffic that could move in trailers or containers, compared to how it competes for the other traffic that it handles?

A And when we're speaking of movement in trailers, you're talking about truck competition or traffic that is truck competitive; is that correct?

Q Yes.

A For the truck competitive traffic, we would compete even on a TOFC basis. We may compete on a boxcar basis or we may compete on a tankcar basis. It depends on what the truck competition is and the degree of flexibility that we have with each type of equipment, TOFC, boxcar, or tankcar.

If we're competing with a trailer, over the road trailer movement, and we can do it with a boxcar, we would prefer to operate with a boxcar. If we can't get the profit margins out of the boxcar, if there is perhaps a joint line connector that won't join with us, they prefer to be in TOFC, whatever, we will go to TOFC.

If we're competing with a tank truck, we will try to compete with a tankcar. Usually we can do better with a tankcar because a tank truck has less flexibility in securing empty return movements.

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Q And you say competing with a tank truck, the tank truck is the source of the competition for the chemical movements that the KCS is involved in originating in Louisiana and Texas?

A That would be one, yes.

Q Now, does KCS compete differently for traffic that would move by truck in LTL shipment sizes? By that I mean, does the need to consolidate these shipments before rail handling require KCS to offer somewhat special departure times in order to attract LTL type traffic?

A KCS presently does not compete head to head with LTL type truckers. What we utilize is shipper asscciations who do the consolidating of freight, and the shipper associations pretty well indicate what our transit times should be.

Most of the shipper association traffic that I'm familiar with is competitive not so much with trucks, but with other rail carriers.

Q Now, on the shipper association traffic, through the shipper associations they do consolidate LTL shipments, right?

A Some do, yes. Some consolidate straight trailer loads into multi-trailer shipments.

Q Right. And through the shipper associations,

KCS does compete head to head against trucks who would want to try to move that traffic in LTL shipments, don't they?

A I'm not sure that we compete head to head with trucks. The shipper associations compete more with the trucks. But there, of course, is a profit margin built into their handling as well, and I'm not sure what the specific degree of competition is.

The LTL trucker is a breakbulk type operation which uses complex terminals, hauling into the terminals. They use teamster labor, they use local distribution methods, and I'm not too certain that there really is a lot of competition for that at the low margins of TOFC movements.

Q You say TOFC is moving at a low margin on the KCS?

A I think in all carriers there's a lower margin for TOFC traffic, given the nature of service that we attend to that traffic.

Q Is the basic reason for the low margins the intense competition for that traffic?

A The intense competition between rail carriers, I think, yes.

Q Now, turning to KCS's other traffic, for which KCS competes intramodally, this would be freight such as

grain or chemicals or sand and gravel, is that what you're referring to?

A Or the complete range of traffic mix of all carriers.

Q Okay. And by saying that KCS competes intramodally, you are not saying, are you, that trucks don't compete trying to handle this traffic?

A Again, we're trying to make a generalization, something I hesitate to do, because truck competition is available for every type of movement at one point or another. It's the degree of that competition that is unknown to generalize on.

Q Now, turning to the manner by which KCS competes for the other types of commodities that we were talking about, does KCS offer special expedited service for automotive traffic that it handles down to the Shreveport facility?

A I wouldn't say that we provide it on a regular basis. There are times when we have to move a car expeditiously because it's been delayed in transit or something like that. But normally those cars go into our regular train service.

Q Sir, could you describe the train service that KCS offers today for traffic moving on your line southbound from Kansas City?

A Describe it in what manner?

Q Well, what type of train service does KCS offer to shippers for traffic moving southbound from Kansas City?

A I can't give you any specifics. I don't have the train schedules. I would say generally that from Kansas City to Shreveport, maybe 24 hours; and then from Shreveport to New Orleans, maybe about another 19 or 20 hours.

Q How many trains a day does -- how many departures from Kansas City does KCS offer daily?

A It varies upon the amount of traffic that we receive at Kansas City. We have trains where we put on extras. As I understand it, we have some trains that don't go because there's not a sufficient amount of traffic to haul.

It's hard to say. I'm not an operating man and I find it difficult to answer your questions.

Q I know, and I just wanted to get a feel for this in a general sense. How many schedules does Kansas City Southern offer southbound from Kansas City daily?

A I can't answer that specifically.

Q Okay. What types of commodities do you handle on your trains southbound from Kansas City?

A I would think grain would probably be the

number one commodity. We do handle some automobiles down there, general traffic, boxcar traffic, and some TOFC traffic.

Q By general boxcar traffic, you're not really distinguishing between commodities. It's just traffic that moves in boxcars?

A Yes. KCS's southbound mix is pretty general.

Q Now, could you describe briefly in terms of the number of schedules being offered and type of service the train service KCS offers today for traffic moving on your line northbound to Kansas City?

A The northbound times would approximate those that I gave earlier on the southbound. The times of departure I really hesitate to say because I don't know for sure.

Q Okay. But what types of commodities do you carry on those trains?

A Usually petrochemicals, papers, paper products. By petrochemicals I'm referring to a full range, all the way from sophisticated hazardous materials to plastics. Paper products is usually pulpboard and fiberboard, some newsprint out of the paper mills that we serve.

There's steel that originates at a couple of our steel mills that comes northbound. We bring up TOFC

traffic from New Orleans into Kansas City which is imported at New Orleans. That about covers the majority of it.

Q In these commodities that you mentioned, sir, the iron and steel, the paper products, the chemicals, do they all move in mixed train service, the same trains, northbound to Kansas City?

A Yes.

Q Now, sir, on pages 4 and 5 of your verified statement you list some train schedules. Those train schedules for ATSF/SPT that you list are not Santa Fe-Beaumount-Southern Pacific schedules that are available today, are they?

A Excuse me, I'd like to read this a second and make sure I'm understanding where we are.

(Pause.)

A I believe the transit times that are on page 5 are times that we extracted from the work papers of the Southern Pacific.

Q Right. Those are the post-merger operating times in the Applicant's operating plan, aren't they?

A Well, on the first line where it shows eastbound and then Santa Fe-BN and Santa Fe-SPT, Santa Fe-BN I believe is the current time schedule and the Santa Fe-SPT is the proposed time schedule.

Q That's what I am referring to, the Santa Fe-SPT schedules that are listed on pages 4 and 5. Those are all schedules from the operating plan reflecting the schedules that would be possible after the merger is in place?

A That is correct.

Q Now, the merged system train schedule that you show from Los Angeles to Memphis on page 4 would not even go through Beaumont, Texas, would it? Or do you know?

A Are we speaking of the proposed now?

Q Right, the proposed train doesn't even go through Houston and Beaumont, Texas, does it?

A From Los Angeles I thought it did. From the Oakland territory, I was under the impression it would not.

Q I don't believe it does from Los Angeles to Memphis either. From Los Angeles to New Orleans it does, but I don't believe it does from Los Angeles to Memphis.

But be that as it may --

A Well, I was under the impression that it would go into Houston and break off and go up through Memphis, up into the Memphis territory.

Q Now, the Los Angeles to New Orleans schedule

that you list at the top of page 5 is made possible, according to our testimony, by several yard consolidations in the Los Angeles area, the specialization of one of the yards on TOFC service by rerouting a number of Southern Pacific trains off the Southern Pacific's route, the Sunset Route, and onto Santa Fe's double track route through Arizona and New Mexico.

Now, could Santa Fe and Southern Pacific realistically consolidate their yards and shift all of this traffic in order to achieve these new service schedules without merging their railroads?

A That calls for a decision that I can't make at this time, not knowing the specifics of how you run the train, how both carriers run their trains in connection with each other. I have to look at how we operate the Santa Fe over Dallas and make the determination that we are able to compete in a market where we have a slower transit time, over the road transit time, by having run-through operations, direct interchange, and certain refinements.

So I would have to presume that the Santa Fe and SPT could do the same thing if they are trying to work together.

Q Well, you're not testifying here, are you,

that Santa Fe and SPT could consolidate their yards as separate companies and move the Southern Pacific traffic off of the Sunset Route in order to achieve these schedules that are in our testimony?

A Operating independently?

Q Right.

A I think they could do some of those things to achieve a transit time similar to that. I would have to go back to the work papers, which I don't have with me, to see what the present schedule is. But if I recall right, it's only within a few hours of the one that's demonstrated here as far as direct service by the SP. Now, I don't know what the Santa Fe can do.

Q Okay, so you don't know whether these schedules could be achieved by the railroads or not? You haven't studied that?

A That's correct.

Q Now, sir, the purpose, the stated purpose for putting these new schedules in, these TOFC schedules, was to divert truck traffic to SPSF. Do you agree that these schedules will enable SPSF to compete more aggressively against trucks for current truck traffic moving in these markets?

A Again, I have to get to the point that you can't make a generalization on it. There are truck

movements that you would get, there are truck movements that you wouldn't get.

Q Okay, but these schedules will enable us to get more truck traffic, don't you think?

A I can't say that because I don't know all of the specifics of what you're competing with on an individual market basis at the time.

Q As a rule, when you improve TOFC service to give yourself an effective arrival a day earlier between given city pairs, that does enable you to take truck traffic, doesn't it?

A Again, there are times when it does, yes.

Q Now, do you know -- well, okay, I'll word it this way. Isn't it true that the schedules that you set forth in your testimony and those that you set forth in your exhibit, your Exhibit IWP, the three-page exhibit at the end of your statement, were designed specifically to make the new system more competitive with trucks in terms of the departure times from the origin cities and also in terms of the arrival times at the destination cities?

A I understand that's what you're offering, yes.

Q And you can tell that, too, can't you, by looking at the schedules, that the departure times are

rather late in the day, to permit the traffic to make the train, with generally early morning arrivals at the destination cities?

A Could we talk about each one individually that you want to address?

Q All right. In that case, let's just move to another topic. I'd like to discuss some other ways that KCS is competing with trucks to handle freight traffic. What type of traffic did KCS target when it built the bulk unloading facility at Kansas City?

A We targeted direct haul covered hopper car plastic movements off of our line. We targeted some movements that were moving by truck.

Q What kinds of shippers use these facilities? Is it generally smaller shippers?

A I would guess about 50 percent of the shippers that presently utilize or receivers that presently utilize that facility are small lot shippers.

Q And those shippers, absent this facility, how would those shippers take delivery of their product?

A Prior to us establishing the bulk facility, it was moving through another bulk facility over in St. Louis, with truck distribution beyond that. There were some receivers that were receiving direct shipment by truck until we acquainted them with the economics of

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using high rail density car shipments on a longer distance basis.

Q Does KCS compete directly against trucks for sand and gravel movements?

A Not really. KCS really does not serve the sand and gravel market to a large extent, or even to a small extent.

Q KCS has basically withdrawn from that market in the past few years?

A Yes.

Q And that's because the trucks are handling all the sand and gravel today, isn't that right?

A No, it's because we don't have any quarries on our line that make shipments of sand and gravel to points that utilize it.

Q Does KCS compete directly against trucks for wood chip and pulpwood traffic?

A For wood chips and pulpwood, yes.

Q Is the truck share of this traffic increasing over time?

A I would say in the past three to four years we've felt that we have lost 50 percent market share to these trucks. They are a very peculiar breed of truck, however. You can't consider them the normal type of truck operation people visualize as being the type of

competitor that railroads compete with.

Q In other words, this truck operation has been designed specifically to try to take traffic away from you railroad, for example?

A These type of truckers are the mom and pop type that will go out and spend maybe $5,000 for a complete rig, which includes the tractor and the trailer, which is nothing more than a wheel with a bar down the middle, with upright bars welded onto it for loading pulpwood.

The investment is very small and the rate of return for those people is very minimal, because they are not -- don't have the business acumen with which to price their product. And as long as they make a couple of dollars a day, they're happy.

But they're not the type of competitor that we really visualize on a long haul basis.

Q But the result of their entry here into this market has been to take about 50 percent of your market share of this product?

A Yes.

Q Is this a phenomenon you think is peculiar to KCS in your region or do you think that that's a sort of thing that's going on and that all of the railroads in the U.S. are facing today?

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A I would suspect that for pulpwood, chips and pulpwood, that all the rail carriers are facing the same thing. You have to bear in mind, though, that we're talking about relatively short distance haulage by the truck, anywhere from 15 to 30, to 40 miles.

Q Now, has truck competition been a factor in innovations that have been made in railroad service for paper shippers, in terms of improving the equipment type, for example, or improving loss and damage control?

A I'm not sure I can allocate those improvements to truck competition. Certainly trucks do offer some degree of safe handling that the railroads wouldn't offer in a very general service type boxcar, with no cushioned underframe devices.

However, these cushioned underframe devices have come across for all types of traffic, not just pulpwood or paper products. And I would be very reluctant to say those designs were caused by truck competition. They're caused by rail carriers trying to offer better service and to offer a better transportation vehicle.

Q But the effect of those designs in the new vehicle has improved the railroads' competitive position vis a vis the truck competition? Now trucks no longer

can offer a substantially better safety factor to the shipper, isn't that right?

A For that type of equipment, generally I can say that is a correct statement.

Q Now, are you familiar with the concept of just in time inventory, Mr. Ploth?

A Yes.

Q Would you explain your understanding of that concept?

A The concept as it relates to transportation is the desire by the shipper to reduce his inventory cost by making shipments from a given origin to a given destination so that the goods will arrive at the destination in time within maybe a 10 to 24-hour time frame for usage at the destination.

Q And has the impact of this system as it's been adopted by various corporations led to smaller shipment sizes and increased importance on rapid and reliable transit time, and also an increased awareness of loss and damage by the shippers?

A Yes.

Q Do you agree that this just in time inventory concept is a growing phenomenon among manufacturing companies today?

A I would say it's a growing phenomenon more towards someone that is actually engaged in the manufacturing process like a motor vehicle.

Q Now, has this just in time inventory concept and the shift, well, in emphasis that has followed from

it given trucks a competitive advantage vis-a-vis the railroads in competing for manufacturers' business, do you think?

A There certainly is an advantage when an truck has an over-the-road transit time and the shipment size is small, such as a truckload shipment, unless the rail carriers can match that.

Q Do you expect the trend toward just in time delivery to continue in the future?

A Again, we're trying to make a generalization with that specific market knowledge, and I would have to say generally you could probably say that; but I would have to look at each particular market to find out whether or not they have the capability or even the need for using just in time inventory.

Q Now, sir, is there a trend in the United States today toward a decentralization of production facilities; that is, locating manufacturing plants closer to the areas of consumption?

A I hate to keep saying this, but it again depends on the industry. If the industry costs of relocating are too insurmountable, they will not relocate. They will use the existing facilities. If it's a smaller industry or they have an obsolete facility and they need to produce a modern facility,

yes, they may move it.

Q My question is more general. It wasn't industry specific, as you pointed out. Isn't it true that in many industries there is a move toward this decentralization of production facilities?

A If you want to generalize, yes.

Q And would you say that where this has occurred that this trend is leading toward shorter haul movements of manufactured commodities?

A I couldn't make that generalization because it results in short haul movements for one segment of the product, but longer haul movements for the other segment of the product. If you have a raw material that has a cheaper cost and a cheaper transportation cost than the outbound material which is of a higher value and a higher transportation cost, the trend, in my mind, would be to take advantage of a longer haul for the cheaper inbound raw product and take a shorter haul for the outbound product.

But again, it depends on the location of where the markets are, what markets they are targeting for growth. You just can't make a generalization like that for any particular industry.

Q Okay. Sir, in Appendix A of your verified statement you cite a number of statistics.

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MR. DREILING: Again, are we on KCS-14?

MR. WILSON: Right.

BY MR. WILSON: (Resuming)

Q You cite a number of statistics concerning various truck traffic levels in recent years. Almost all of your statistics come from the regular common carrier conference. What types of motor carriers belong to this conference?

A These are normally the people like Yellow Freight, Transcon, et cetera, which are identified with brake bulk type operations.

Q These are the regular route common carriers?

A Regular carriers, right.

Q What other types of motor carriers are there that do not belong to this conference?

A Clearly, there's the independent truckers which do not belong to an organized conference like this. You have the irregular route carrier conference which covers probably two of the greatest groups of truckers.

Q Right. And you also have specialized commodity carriers, don't you?

A That's correct.

Q And private carriers where shippers are actually providing their own truck transportation,

right?

A Yes.

Q Now, is the traffic for each of these other types of motor carriers increasing, declining or staying the same?

A It's hard to get a handle on it. That's why we were limited to only using the common carrier conference information.

Q But the statistics you have used is only reflecting one of these five types of motor carriers.

A That's right.

Q And they don't reflect truck traffic growth overall; isn't that right?

A That's correct.

Q Now, sir, on page 21 of your statement you discuss some of the potential dangers you see in new rail ratemaking freedoms, and near the bottom of the page when you list what you're concerned about as being possible adverse effects on shippers, one of the things you list is the ability of large carriers to exit from given markets.

Do you see that, sir?

A Can you point me specifically to the line?

Q It's the large paragraph on page 21, about four lines from the bottom, where you discuss the

ability of large carriers to exit from given markets. My question is how would a railroad's ability to exit from a market be an adverse effect on shippers?

A Excuse me for the delay. On my sheet it shows on page 22, paragraph 4. Is that correct? I mean part 4 of that paragraph that's identified by number 4.

Q It may have been changed.

VOICE: I think it's on pages 22 and 23 of the revised statement.

BY MR. WILSON: (Resuming)

Q Right. Okay. Yes. I'm talking about going on to the top of page 23 in the revised statement.

A Excuse me. This isn't reading right to me in the rereading.

MR. DREILING: Your Honor, off the record.

(Discussion off the record.)

THE WITNESS: The commentary about improved revenues or exit from profitable business segments refers back to your witness Kloss' statement.

BY MR. WILSON: (Resuming)

Q Do you have my question in mind? I think I probably should repeat the question now that you've read the paragraph. My question is how does a railroad's ability to exit from a market, how does that adversely affect shippers?

A If a railroad is the sole source of transportation for a given shipper, and he exits from the market, and the shipper has no other resource other than perhaps some type of a high cost motor carrier which prohibits him from marketing his goods, that will hurt a shipper.

Q Well, the railroad's ability to exit from the market would not be anticompetitive, would it?

A Yes, it could be anticompetitive. If you have a rail carrier, you have two rail carriers in a given market and one exits from the market and the other carrier becomes dominant and is in a position to employ monopolistic pricing, monopolistic-type services, I would say that would be anticompetitive for the shipper if he is not able to market his goods in a given area where he's in competition with another shipper that has reasonable transportation.

Q So by exiting from the market, here you're not referring to an abandonment; you're just referring to a situation where a railroad might just stop competing for traffic. Is that your reference?

A I'm just using that as an illustration. Abandonment could be another one.

Q Okay. But if there was an abandoment, of course, any proposed abandonment would have to be viewed

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and approved by the Interstate Commerce Commission.

A That's agreed.

Q You're not predicting here, are you, that this merger would result in abandonments or any merged carrier exiting from any market that it's now in, are you?

A I can't comment on that, Mr. Wilson. I don't know.

Q Now, you also state in this same sentence that large carriers can lock shippers into markets of the carrier's own choosing. Do you have any examples of cases where a railroad has forced a shipper to ship its traffic to a market that the railroad chose rather than a market that the shipper chose?

A I don't have any that come directly to mind.

Q Now, sir, on page 8 of your December 8th verified statement, your KCS-15, you describe the KCS-Santa Fe-Big D connection as equal to or better than the proposed SPSF route between Los Angeles and New Orleans; and I have a few questions about that.

Is the SPSF route from Los Angeles to New Orleans about 200 miles shorter than the Santa Fe-KCS route?

A Excuse me again, Mr. Wilson. Can we go back to where you're looking at this? Page 2 you said?

Q Page 8.

A Page 8. I'm sorry.

Q Your assertion there is that the Big D route is equal to or better than the proposed SPSF single line operation. My first question is isn't the SPSF route between Los Angeles and New Orleans going to be over 200 miles shorter than the Santa Fe-KCS route via Dallas?

A I'm not familiar with the mileage on that. It would be somewhat shorter. I don't know the degree of how short it will be.

Q Does an interchange occur between Santa Fe and KCS on Big D traffic?

A There is an exchange of equipment between the KCS and the Santa Fe. The KCS prior to the recent change by the Santa Fe was taking our equipment at Shreveport, running it through to I believe it was Brownwood, at which point the Santa Fe crews came on board and took the trains all the way to the destination. With the recent change that's occurred, that's no longer in effect.

Q Does a crew change take place at the Santa Fe-KCS interchange?

A At Brownwood a crew gets on, and there is a crew change, yes. A KCS crew gets off.

MR. DREILING: Excuse me, Your Honor. Could

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we go off the record for a minute?

(Discussion off the record.)

JUDGE HOPKINS: Back on the record.

BY MR. WILSON: (Resuming)

Q Sir, I believe there may have been a misunderstanding there. Does a crew change take place at Dallas between Santa Fe and KCS?

A Yes. I was transposing Dallas and Brownwood in my mind.

Q All right. Does a change in power from Santa Fe to KCS or KCS to Santa Fe take place at some point along the route?

A I believe the exchange of power occurs at Brownwood.

Q Now, do both Santa Fe and KCS have to enter all of the waybill information and car information in their computers?

A Yes.

Q Do both Santa Fe and KCS have to pay per diem on cars moving over the Big D route?

A Yes.

Q So two sets of car movement records have to be maintained for all this traffic; isn't that right?

A That's correct.

Q Now, do both Santa Fe and KCS have to analyze

the settled waybills on Big D traffic to make sure that they receive their correct division or revenues?

A I would presume so, yes.

Q Will the filing of a loss and damage claim involve an investigation by both the Santa Fe and the KCS claims department to determine who caused the damage?

A Where those claims are filed, yes.

Q Now, are cabooses -- do cabooses have to be interchanged and switched at some point in the route?

A In past practices, yes, there are movements within the yard to totally eliminate cabooses.

Q Don't Santa Fe and KCS salesmen often call on the same shippers to solicit the same traffic over the Big D route?

A Yes and no.

Q There's an overlap?

A That's right.

Q I understand. And don't Santa Fe and KCS have to agree to joint rates and divisions in order to compete for traffic moving by the joint line route?

A If it's a joint rate, yes. Sometimes carriers establish their own proportion of the rate so you don't have joint rates; you have the combination of rates on the deregulated TOFC traffic.

Q And isn't a portion of the KCS part of the route from Dallas to New Orleans an unsignaled railroad?

A What do you mean by unsignaled? We have CTC or ABS along all of our track.

Q All right. But not CTC, correct?

A There are segments on our road that just has ABS.

Q Are you aware of any segments of the SPSF route from New Orleans to Los Angeles that is not CTC signaled?

A No, I'm not.

Q And none of the extra activities that we were just discussing would be required, would they, in connection with service by SPSF's new single line route?

A They would not be required by a single serving carrier, that is correct. There are things, though, that can be done for joint line service if they become burdensome and restrict competition where two carriers could work together and correct some of those deficiencies of each having carrier working separately by itself.

Q Does the current Big D service serve faster or slower than the proposed new SPSF single line service?

A It's slower.

Q Would more per diem rental be paid, where the Big D route is used?

A In instances where you have per diem cars, yes.

Q Would the cost of operating locomotives via the Big D route be as low as the cost of operating locomotives on the SPSF route?

A That I can't say.

Q Well, assuming the Big D route is slower and requires more locomotive time and also longer, then the cost of operating locomotives would be higher on the Big D route, would it not?

A But it gets into your crew times, how long you're paying your crews paid for. If they get paid by the day and you fall within the day period of time, whether you take 24 hours or 10 hours, they get paid the same; if the locomotive utilization isn't affected by having your locomotive there 8 hours sooner and just sitting around waiting for other loads to return -- there are two many tangibles upon which to make a judgment like that.

Q Aren't some crews paid on a mileage basis?

A Yes.

Q All other things being equal, wouldn't crew

costs be higher via the Big D route than via the SPSF route?

MR. DREILING: Objection, Your Honor. I think the question has been asked and answered.

JUDGE HOPKINS: I'll allow it.

THE WITNESS: You would have to assume that there would be a degree of disparity between the two. Now, what that degree is it's hard to say.

BY MR. WILSON: (Resuming)

Q And the disparity would be that the Big D route crew costs would be on the high side?

A Based on a mileage assessment and crew costs, yes.

Q And also, since the Big D route is longer than the SPSF route, wouldn't it require more fuel to operate trains over the Big D route?

A Again I can't say because I'm not familiar enough with the grade distinctions between the two. Grade distinctions will make a large variance in your fuel consumption.

Q Okay. Assuming that grade distinctions are either equal or Southern Pacific's line has better grades than the Santa Fe-KCS route, then you would agree with my statement, wouldn't you?

A All the way from origin to destination, yes.

Q Don't all these factors indicate to you that the new SPSF route would be more efficient than the Santa Fe-KCS route?

A If all of those factors were present and all of them were in favor of the SPT route or the SPSF route, I would have to say there is a degree of efficiency there that we wouldn't have with the Santa Fe-Big D route. Again it gets into how does that translate into being competitive.

Q Now, sir, you testified in the Union Pacific control case, did you not?

A Yes.

Q And you performed a traffic diversion study in that proceeding, didn't you?

A I performed one, yes.

Q And you are familiar with the competitive impacts, generally familiar with the competitive impacts of the Union Pacific merger on the KCS, are you not?

A I am. Yes, I am.

Q Now, is one of the benefits of the Union Pacific merger Union Pacific's ability to provide new single line service between markets in California, on the one hand, and in the southeastern United States on the other hand?

A That's what was in their testimony and

presentation, yes.

Q Right. And you, in your analysis of the traffic impact of the merger, did you not predict losses of traffic which KCS handled between Kansas City and New Orleans; that is, traffic moving to and from the southeast?

A Traffic from and to the southeast was involved. I don't recall the exact points, the counterpart of the movement.

Q Okay. But you do recall, do you not, diverting KCS traffic where KCS was participating in joint line hauls or traffic moving between California and the southeast?

A It seems that there was some traffic in there, but I can't say specifically what it was or to be positive that there was some.

Q Okay. Now, in competing for traffic via the Big D route, do you regard yourself as competing in part against Union Pacific's train service through the Memphis gateway to California?

A Again, we have an overlap here. There is some degree of competition that the Union Pacific affords through Memphis. From the analysis that I went through in this merger proceeding, I found it to be very minimal.

Q So you don't think Santa Fe and KCS, when we're competing to try to get traffic to and from the southeast, you don't think we're competing with UP's single line service off the Memphis gateway?

A The competition would be very minimal. There is some degree, yes, but it is very minimal.

Q Sir, I have a couple other questions about your December 8th verified statement.

A Is this 15?

Q This is KCS-15. First, on page 4, you state in the eleventh line that movements in applicants' traffic study which were reviewed by applicants' traffic experts were not a representative sample. What is a representative sample?

A In other words, from what we were able to find, there was no evidence that the movements that were pulled for evaluation between these different iterations were designed on a sampling basis or sampling technique basis. They were simply selected on the basis of occurrence or frequency of occurrence with no backup as to whether or not that was going to be representative of the total universe within that pull.

Q Well, now, if applicants' selection procedure was one which ensured that there would be in the output report at least ten examples of each rule that was used

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in the traffic study and also ensured that there would be at least 3, 4 or 5,000 movements for the traffic evaluators to examine, wouldn't you say, sir, given the fact that it is a computer and it therefore automatically has consistent evaluations, that the evaluators had available to them enough information to determine that the study was working the way they wanted it to work?

A No.

Q You don't think so?

As a marketing expert, isn't a review of 4,500 movements good enough to ensure that the diversion judgments are reasonable given the uniform procedures in the computer?

A I can't make that judgment, because as a marketing expert it has no reality as being a statistically valid sample. I would have to confer with a statistician to find out whether or not the representation of those movements would in fact statistically represent the universe that was being studied.

Q Oh, so you don't know one way or the other whether this was a big enough selection of movements. Is that your testimony?

A I'm saying that I do not know, yes.

Q Further down on page 4, Mr. Ploth, you refer to market power issues. Where does KCS have market power on traffic today?

A The sole market power that we have would be between two local points that we serve on a direct line basis, and I'm not aware of any shipments that move like that. In other words, KCS doesn't really have much market power.

Q You don't think you have market power on shipments that move from exclusive KCS origins?

A If they're exclusive KCS origins, no competition involved from other carriers, no way of installing translating operations to pull the traffic away from us, there may be market power there as long as there is no other competing market in which those shippers are engaged in marketing their goods.

Q But you're not aware of very many examples where that is in fact the case, is that right?

A I can't recall one right now.

Q What about KCS' market power for chemical traffic that originates at KCS-served facilities? Do you think KCS has market power with regard to that traffic?

A Could you give me an illustration of what you're speaking of?

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Q Could KCS force chemical shippers shipping traffic from KCS-served facilities to give KCS long haul routings on their shipments?

A Just about every petrochemical that we haul is competitive with another source. As you know, the Gulf has a huge concentration of petrochemical plants, and I can't recall of any petrochemical that we originate that isn't competitive with another petrochemical. And the other petrochemical carriers are such as the Missouri Pacific and the Southern Pacific which have a much broader range of coverage than what we have.

They create the competitive situation that we face, and our shippers are also confronted with the competition from the other shippers served by the Missouri Pacific and the Southern Pacific. Therefore, in order for our shippers to participate in the market, we may have to short haul ourselves.

Certainly, there must be instances where we can secure a long haul because we originate the traffic; but I can't generalize, again.

Q Your testimony is that generally for chemical traffic there is tense source competition and that traffic being handled by the Missouri Pacific, for example, operates as a constraint on your ability to have any market power over this chemical traffic; is

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that right?

A Not only the Missouri Pacific, but the Southern Pacific and the Santa Fe, the ICG. It's a very delicate balance as to how all these interactions are involved with each other.

Q Well, basically doesn't KCS have to price its transportation rates to these chemical facilities in a way that these shippers are kept in their markets?

A That is our major intention, yes.

Q So as long as some other chemical shippers somewhere else are getting low competitive rates from say a common point out of Houston, then you're going to have to give your shippers similar rates or else the traffic isn't going to move; isn't that right?

A That's correct.

Q I assume you are aware, Mr. Ploth, that the term "market power" has a precise meaning to an economist, and in one of your testimonies you specifically state that you don't want to become an economist. As you use this statement in your testimony, what does the term "market power" mean?

A I use the term "market power" from a marketing perspective, and that is what limitations are placed upon a rail carrier in marketing the goods or the services he offers given types of shippers as opposed to

the services offered by a competing carrier.

Normally, market power evolves to whether or not a rail carrier can be price competitive or have route availability from joint line connections. As an illustration, if we are, as we are, a regional carrier, we must deperd primarily on our connections.

We compete with two giants of the industry who have direct service to just about every market that we serve on a joint line basis. If we can't establish a competitive rate, if we can't establish a joint line rate to be competitive, we are excluded from that by what I call market power. And I realize it's not the same definition that the economist has.

Q All right. You have several pages of testimony talking about market power in the new SFSP rail system, and isn't this essentially the same argument that KCS made in the Union Pacific control case?

A I can't say that, Mr. Wilson, because when we argued the issues of the Union Pacific, our market power illustrations were based upon the movements that we found that would be affected within that proceeding.

MR. WILSON: Your Honor, I'd like to have marked for identification at this time Exhibit SFSP-C-99.

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JUDGE HOPKINS: That will be marked for identification.

(The document referred to was marked Exhibit No. SFSP-C-99 for identification.)

MR. WILSON: This is a memorandum which we obtained from the Kansas City Southern in discovery in which Mr. Ploth is reporting to Mr. M.F. McClain concerning the Santa Fe-Southern Pacific merger.

BY MR. WILSON: (Resuming)

Q First, sir, who is Mr. M.F. McClain?

A Mr. M.F. McClain is the senior vice president of marketing for the Kansas City Southern Railway Company to whom I report.

Q Sir, let me read into the record part of a paragraph on the second page. You write to Mr. McClain, "Also, we again see where KCS needs a short route between the Beaumont-Lake Charles areas and New Orleans. However, we have the same problem here that we did in the MP-UP merger. The need would not be a direct result of the geographical alignment of the merger.

"In my opinion, we would suffer additional traffic losses similar to what we predicted in MP-UP due to market power gains resulting from the merger. Given the fact that we got nowhere with the market power

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argument in that case, it doesn't seem likely that to repeat the same would give us any different results. However, I am unable to think of any other logical explanation of why we would need trackage rights due to the merger of the ATSF-SP."

This seems to me to be a rather revealing document on the KCS case.

Sir, my question is why didn't you take your own advice and not raise these market power issues in this proceeding?

A Mr. McClain pointed out to me after we got this memorandum or he received the memorandum of the need for having those trackage rights associated with the movement of the mini-land bridge traffic and the intermodal traffic. This particular paragraph was referring strictly to traffic that originated in the Beaumont area going to New Orleans. So the trackage rights --

Q So you weren't thinking of intermodal traffic when you wrote that paragraph?

A That paragraph was specifically addressed to the Beaumont-Lake Charles movements that presently go via Shreveport to New Orleans that we would be in competition with the Missouri Pacific and Southern Pacific between Beaumont and New Orleans.

Q Now, sir, KCS's concern about the merger, as you state in your testimony and as Mr. Carter also stated, is that SPSF would close the existing joint route KCS-Dallas or downgrade the quality of the rail service that it provides with KCS on the Big D.

I'd like to refer you, sir, if I could, to a copy of the Interstate Commerce Act. I have just given you a copy of 49 U.S.C. Section 10705(e), the provision in the Interstate Commerce Act dealing with joint route and rate cancellations.

Sir, isn't this the provision that sets out the standards that the ICC and the Commission's tariff review and suspension board is required to apply when determining whether a proposed joint route and rate cancellation is in the public interest?

A Mr. Wilson, I can't answer the question with just this small segment. I'm not a lawyer, I'm not a commerce attorney, and I don't know how all of the other components within the act relate to this particular provision.

Q Well, we'll start out with the procedure. Are you aware of the procedure that a railroad needs to go through when it proposes to cancel a joint rate?

A Generally, yes.

Q Could you describe it?

A The first step would be if it's a single line system rate to just cancel it out of the tariff.

Q Well, my question is with regard to the joint rate. Doesn't the railroad that wants to cancel a joint rate first have to publish notice of the cancellation 20 days in advance of when the cancellation is to occur?

A I believe it's 20 days.

Q And cannot affected carriers or shippers petition the Commission prior to the effective date of the cancellation and ask the Commission to suspend the joint rate cancellation altogether?

A Yes.

Q So a procedure is in place today, is it not, that would prevent a joint rate cancellation from taking place if the joint rate cancellation were to be inconsistent with the public interest?

A Now we're talking just right now the cancellation of the route or the rate? Generally, that is, from what this says, that is correct.

Q And isn't one of the standards that the Commission is specifically required to use in reviewing joint rate cancellations the one that's set out in the provision that I gave you where the Commission is directed to "consider the overall impact of cancellation on the shippers and carriers that are affected by it?"

MR. DREILING: I object, Your Honor. The witness has already said he doesn't know exactly what the standards are. He has the statute in front of him, but as he indicates, there is a lot of other areas of the statute.

There are Commission rules and regulations and rulemaking proceedings, ex parte proceedings with which Mr. Wilson hasn't established Mr. Ploth is familiar.

JUDGE HOPKINS: This witness has already stated --

BY MR. WILSON: (Resuming)

Q I will withdraw the question and ask this question. Are you aware of the standards that the Commission uses in determining whether a proposed joint rate cancellation is in the public interest?

A No, I'm not aware of them.

Q Is it your concern that after the merger the Commission would permit the SPSF to close joint rates with KCS over Dallas?

A Not only close the joint rates but also downgrade the service, which has happened right now. And we have had a service change in our route to the point where if it continues, there may not be a route any more.

Q Sir, is KCS involved in the industry effort to

develop a new standard for review of proposed joint rate cancellations?

A Yes.

Q Are you aware of KCS' position in that effort?

A No. I'm not involved with that. Someone else is. I just know that generally we're involved with the proceedings that are currently in progress.

Q Do you think that an industrywide solution to the problem could resolve KCS' concerns about joint rate cancellations over Dallas with SPSF and also protect against Union Pacific rate closings at Kansas City?

A It's too late to protect against Union Pacific route closings. They have already occurred. And I don't think you can go back and cancel things after they have occurred. Insofar as what you're proposing for the Santa Fe-KCS as being protected, there may be something that comes out of those proceedings, but I think at this stage, given what we've seen happening in the past few years as to the opposition for some of the positions that I would like to see occur, that we will not have much of a chance.

Q Okay. Well, then, I gather, sir, that from your testimony that you would need specific protection of the Dallas gateway. In fact, on page 11 of your

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statement, KCS-15, you specifically say that, I think. You say, "This slight gain alone" -- and your reference there is to the new system's proposed service improvements on the Southern Corridor -- you say, "This slight gain alone, presuming applicants would continue present schedules, routing, and would join KCS in rate levels comparable to their single line rates, would have no impact upon the ability of KCS, a joint line competitor, to continue participating in its present traffic volumes for any particular market."

Is it true that this is a fair summary of your position in this case?

A That statement is absent merger on the Santa Fe-SP.

Q Either absent merger or a protection over the Dallas gateway that would guarantee that applicants would continue present schedules, routing, and would join KCS in rate levels comparable to their single line rates?

A Mr. Wilson, all I'm saying there is that we still can be a viable competitor in the marketplace over Dallas if those conditions exist.

Q If these conditions are met, you can be a viable competitor in any market in which you participate? Is that what you're saying?

A If those conditions exist, if there's no downgrading of service, if there is no preferential treatment for a merged entity of the new system versus us, yes.

MR. WILSON: I'm about to move into the traffic study. Maybe this would be a good time for a break.

JUDGE HOPKINS: This would be a good time for a break. We'll take 15 minutes.

(Recess.)

JUDGE HOPKINS: Back on the record.

Mr. Wilson.

BY MR. WILSON: (Resuming)

Q Mr. Ploth, turning to the subject of traffic studies, in your opposition traffic diversion study you, as the final evaluator, finally had a choice of a nondiversion or a 100 percent diversion for each of the movements that you looked at, is that correct?

A Yes. We did have partial, what we called partial losses, but it was on a whole car basis.

Q Right. And then what you called a partial loss is when KCS was short hauled in the route.

A That's correct.

Q Were you involved in the decision to give yourself only the all or nothing choices when you looked

at the study movements?

A I'm not sure that we really had a decision, but that's what would occur. That's the way that we conducted the study in the MP-UP, and I think it was just kind of an evolvement that we studied this particular opposition study.

Q I noticed in going over the study movement sheets that there were a number of instances in the opposition traffic diversion study where evaluations were changed during the course of the study from no change to diversion, and sometimes the other way.

Don't you think that if you had choices available to you of, say, a 25 percent, 50 percent and 75 percent diversion in addition to the 0 and 100, that you would have been able to express your judgments about the divertibility of these movements more precisely?

A I don't believe so. On this particular study the reason for some of the changes that you saw, because we had different information coming in from different sources, we had two individuals that first evaluated this who are not in possession of information that our second evaluator was in possession of.

And then when I became the final evaluator, there were certain things that I used such as the market power issue that we described earlier to overcome the

information that they possessed in making the judgment that they made.

I did not feel in any case that I can recall in making this evaluation where we couldn't make the evaluation on a whole car basis.

Q Well, sir, when you were looking at a sheet and the factors surrounding the movement convinced you that some of the traffic with the characteristics of the car you were looking at would be diverted to SPSF, and some of the traffic would be retained by KCS, how did you mark the study movement sheet?

A The traffic or the study movement sheet was marked either on a whole car loss or whole car gain -- not gain but retention. There were instances where it was difficult to make a decision on whether or not we would retain the whole movement or not. But in every instance that I can recall, after discussing it with the various people, we decided it could be made on a whole car basis.

I would have just as much difficulty making a decision based on a given percent of 25, 50 or 75. It's still an arbitrary decision. And I think it may be even more arbitrary on a whole car basis in a lot of instances.

Q Well, when you looked at a movement sheet and

said to yourself 25 percent of this traffic is going to shift to SPSF's new long haul route, did you go ahead and mark the movement sheet as a diversion on a whole car basis?

A I don't think we would ever have made a determination that 25 percent would have shifted. Probably a more normal thought process would be do we think we can get all of this, do we think we can retain some of it, or do we think we'll lose all of it, or we will lose some of it. But we couldn't make the definition of a percentage.

And then after discussing it with ourselves, we finally said yes, we can retain it. If there was a question where we couldn't make a judgment about divertibility, we wouldn't have diverted it.

Q Well, now, the way you described it you said sometimes when you were asking questions to yourself, one of the questions you asked is is there a possibility that we would retain some of the traffic.

Now, in that situation what did you do?

A We would look at the particular movement sheet. We would also look at perhaps if there was a group of movement sheets of similar characteristic, try to make a determination of whether or not there was an element of question in making that diversion. If there

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was an element of question and I didn't feel I could make the diversion on a whole car basis, I said well, we won't call it a diversion.

Q Yeah. When we were talking to Dr. Bardwell yesterday, he described the process of grouping movements together in the evaluation process, and that at times the evaluator -- he didn't refer particularly to you -- but he said at times the evaluator could then decide after he grouped the movements together which whole car movements in the group would be diverted and which whole car movements in the group would be retained.

Now, is that the kind of process that you used on some of these traffic flows that you looked at?

A It fairly well comports with the process we went through, yes.

Q Now, sir, you testified earlier that you were the final evaluator in the Union Pacific control case. By my calculations, the ICC found in the Union Pacific control case, the KCS diversion loss estimate was overstated by 39 percent. If KCS' estimate in this case is overstated by 39 percent, KCS' loss estimate would be a little over $16 million in gross revenues annually compared to applicants' projection, which is about $15 million gross revenue annually.

Is there any reason in your view, Mr. Ploth, why the ICC should be concerned whether the diversions from KCS would be $15 million, $16 million or maybe even $20 million annually as a result of the SPSF merger?

A You've made a lot of statements in that presentation. First of all, I was not the final evaluator in all of the studies for the UP. As to the specific relationship of the percentage between UP in this case I think is without merit.

We have to deal with what we have here, and the percentage variation that we have between the KCS and the SP I think revolves around a lot of issues that the Commission has to make the decision on whether or not what we specify as our rationale for making the diversions is proper, or whether or not the procedure used by the SP is proper.

Q You're right. I agree we do have to look at this study here, and therefore, regrettably, I ask that some steady movement sheets be marked as an exhibit to go through the cross examination on them. I believe the number this time is SFSP-C-100.

JUDGE HOPKINS: That's right. It will be marked for identification.

(The document referred to was marked Exhibit No.

SFSP-C-100 for identification.)

JUDGE HOPKINS: Off the record a minute.

(Discussion off the record.)

BY MR. WILSON: (Resuming)

Q I have assembled here in the packet, Mr. Ploth, 27 study movement sheets. I do not have attached the waybill and settled revenue information which you had. I don't think any of my questions would require reference to that, but if at any point they do, I suppose you can look at it.

A I have copies of our original with me so I can refer to those.

Q Okay, sir. This first movement, study movement sheet 878, is the first in a group of movements I'd like to talk to you about that involve chemical traffic from Texas and Louisiana points. This first movement was chemical traffic generically, I think, originating in West Lake Charles, Louisiana, as it states on the upper lefthand side of the page, destined to Decatur, Illinois.

It's a shipment by Firestone Tire and Rubber, as it's filled in after consignor, and the routing prediversion, which is immediately under the consignor's name, is listed as KCS-Kansas City-ICG.

Now, sir, on this sheet you diverted it a hundred percent, and that's what you meant when you checked "whole loss" at the bottom of the page and wrote in the figure of how much money would be lost to KCS on the movement; is that right?

A Yes, that is correct.

Q And the diversion route that you selected is written under number 4, probable new route, SPSF-Kansas City-ICG; is that correct?

A Yes, sir, that's correct.

Q And reason 3 is where you list the reasons for the judgment that you had; is that correct?

A Yes. Those are general categories that we assigned four reasons so that we could computerize the thing.

Q Right. And one of the general categories is numbered C, other factors utilized in deriving diversion decision, and when you used reason C, you would write information in the lower lefthand side of the page; isn't that correct? You did not do that on this sheet, but you did on some of the others.

A I believe there were some where there was some commentary made, yes.

Q So an effort was made then, was it not, to list all of the reasons on the sheet that were in your

mind at the time you made your diversion judgment?

A At the outset there was an attempt to do that, and as we got into the procedure, it was determined that there were so many variables being shown for G, and actually G was actually meaningless to our aggregation of reason codes, that we finally discontinued doing that.

Q So what does that leave us? Does that leave us with a number of movements where you didn't show your reasons?

A Now, I think the reasons more specifically would be A, D or C, and then there was personal knowledge that was used at the time to make one of those three identifications. Sometimes the other categories were used, but as I recall, very rarely.

Q Okay. Now, this particular movement would be a third party gain to the SPSF system; by that I mean neither Santa Fe nor Southern Pacific is in the pre-diversion route. I assume you would agree with me that that type of traffic where neither Santa Fe or Southern Pacific is involved is the most difficult type of traffic for the merged carrier to try to get after the merger occurs; is that right?

A I don't think I could call it the most difficult type. I think you have to go back through the

history of how the shippers' and the carriers' interactions occurred in the past and then look at what the current competitive climate is and how that climate will be impacted by a given merger.

Q Right. But when looking at a move -- my question is when looking at a particular move, and not necessarily this particular move, any particular move, where neither Santa Fe nor SP is in the pre-diversion route, isn't that a move where it's going to be rather difficult for the merged system to get that, because after all, there's no present relationship with the shipper on that move. The present relationships are with competing railroads.

A But the shipper is involved with the Southern Pacific at this origin. I mean we are head-to-head competitors with the Southern Pacific at this origin, and Firestone makes shipments via KCS, and it makes shipments via the Southern Pacific.

Q Okay. Excuse me. Go ahead.

A If I could kind of illustrate this, contract rates are very prevalent today, and it's not unusual for a carrier to engage with a shipper in a contract that calls for 85 or 95 percent of his business out of a given point at that particular time. Even though one carrier may not have participated in a move that his

competitor did, as soon as that contract is signed, he becomes heir to that particular traffic.

Q Okay. This move, sir, was originally evaluated as a no change, and the reason for that original evaluation, which is crossed off on your number 3, is "present route not affected by proposed application."

My first question is what was meant by that reason, "present route not affected by proposed application," when that reason was used in your study?

A That meant that regardless of how the merger was implemented, we would still be able to have available all of the routings that we presently were using for that particular traffic, and that all the rate conditions would exist to allow those routings to be utilized.

Q Okay. So in this case, that reason was originally checked because of the fact that KCS as an origin line could still have available a routing with the ICG via Kansas City and could still offer competitive service with the ICG via Kansas City; is that right?

A That was the initial evaluation. That's correct.

Q And then you changed it to a diversion and

citei as one of your reasons routes and rates. What was meant by the reason routes and rates?

A This is a perfect illustration of what I just described generally. Firestone ships to a majority -- a number of given destinations. Some of them are tire plants. Some of the destinations are people that use rubber for other purposes than constructing tires. But Firestone in most instances pays the freight, particularly to the tire plants.

Southern Pacific offers service direct to one gateway that we compete with, which is New Orleans. They offer service to another gateway with which we do not compete, which is St. Louis.

We also have the ability to work with our carriers over Kansas City and St. Louis and Chicago for Firestone's traffic. Now, once the merger is accomplished, the Southern Pacific-Santa Fe will be able to offer full gateway coverage single line service to those gateways and more expeditious service.

Our competitive options, such as with the ICG, will no longer be there. We will not have the single line ratemaking capability to offer a contract to Firestone to say we offer you a contract, it covers all of our gateways, and here is the allowance that we will give you for each of these gateways, and you can take

your choice.

If we have a contract, KCS has a contract with Firestone, we would be able to offer only one direct interchange gateway at New Orleans. So if I were in Firestone's shoes, I would sign a contract with the Santa Fe-SP.

Q Well, you say your competitive route with ICG would not be there. But it's true that you would still have routes and rates via KCS, Kansas City, ICG, after the merger, would you not?

A We would have a route with some rate, but I do not expect that that rate would be competitive with the SP -- with which the Santa Fe/SP could offer, particularly since the Santa Fe/SP has an additional service for Firestone at Orange, Texas which we do not. There, it's possible for them to put in an aggregate contract for Orange, Texas and to Lake Charles, Louisiana which again offers Firestone something that we coulin't.

Q Well, wouldn't ICG have an incentive to work with KCS and propose a contract to this shipper?

A But it would be meaningless if the SP/Santa Fe has a broader coverage contract to offer than what we have.

Q Doesn't Firestone, as a matter of traffic routing policy, like to split its traffic between the two railroads that serve its facility?

A Firestone in the past has utilized some type of routing policy, but again it's my experience that it depends solely on the offerings of the carriers serving them, and again you get back to the contract.

If they are faced with a situation with getting a minimal amount of return on a contract with KCS and being able to maximize all the returns from what the SP/Santa Fe could offer, Firestone's no longer going to observe their traffic study if there is one.

Q But your observation is that there are going to be efficiencies at lower rates via SFSP, and as a result Firestone's going to use that service because the rates would be lower.

A The rates will be lower on a broad-spread basis. In other words, Firestone will be able to enjoy more savings on a short-run basis.

Q Well, from a shipper's viewpoint, aren't there advantages in using routes offered by both serving railroads at a facility such as this?

A Most shippers try to take advantage of competition where it exists between two carriers?

Q Why do shippers do that?

A Because they love to keep one carrier in the marketplace so that they have a wedge for gaining something off of another competing carrier.

Q So, in your experience, shippers will sometimes go out of their way to route some traffic via one carrier just to keep the competition there? Is that right?

A That's correct. Now, on this particular instance for Firestone, that wedge could be allowing us to have the traffic into the southeast via New Orleans since that's our competing gateway, and the traffic into the east, the upper midwest, and the upper southeast where they would not have us.

Q Now, in making this evaluation, did you consider the fact that KCS's special equipment was used on this movement?

A Yes.

Q Why wouldn't Firestone want to give a route to a railroad that supplied it with a specially equipped car for the move?

A The uniqueness of the car is nothing peculiar to KCS. The Southern Pacific has the same equipment to offer, and there is no reason to expect that if the contract is entered into between Firestone and the new merged system that they wouldn't offer the same car.

And if I was Firestone, and I had two carriers offering me the same car, but one had this contract to give me which better situated me than the other carrier, I'd take the car from the competing carrier.

Q So your assumption in looking at this move was that it would not be a KCS car after the merger; that instead, SPSF would substitute its special equipment for

KCS's special equipment? Is that what you're saying?

A That's correct.

Q Now, you also listed long haul as a diversion reason. What does long haul mean as a reason in this particular evaluation?

A That means to me that the merged system will be able to take advantage of their long haul route.

Q Well, doesn't the SPSF system have a longer haul route available via Chicago, say, via SPSF-Chicago-ICG?

A Yes, it does.

Q Why didn't you select that route?

A We should have selected that route, but we didn't. The reason was on a conservative basis, we let the Santa Fe and the ICG work it out.

Q Let's move to the next page, SMS-880. Another movement from Firestone at West Lake Charles, Indiana to Decatur, Illinois, this one routed KCS-Kansas City-N&W.

This is another prediction of a third party gain to SPSF, a whole loss of a KCS movement, even though Santa Fe and SP, neither one were involved in the prediversion route. Is that right?

A That's correct.

Q Now, this was originally marked as a no-change, and there were two reasons that were marked

to support the original no-change judgment. The first one is service.

Do you see that there?

A I see what you are referring to, but I think your assumption is erroneous.

Q Oh, okay. Why don't you explain? What does the check by service mean?

A The service and equipment, where it was crossed out, were first evaluations made after it was changed to a divert.

Q Oh, these were checked after you decided it would be a diversion?

A That's my recollection.

Q Well, how would KCS's special equipment support a loss of this movement to KCS?

A That wasn't my evaluation. That's why it was crossed off.

Q Oh, okay. So KCS special equipment was originally checked to support the original judgment of no change, and then when the original judgment changed, you scratched off the reason; is that right?

A No. The equipment was scratched off because the secondary evaluator assumed that the new merged system would have the equipment to use at Lake Charles, and that that would the primary reason for changing this

from an undivert to a divert.

And I made the decision that equipment would not be the primary reason. It would be strictly a rate and route consideration and a service consideration.

Q Okay. I understand now.

A I'm sorry. I said service. I meant a long haul consideration.

Q Also then, when you crossed off service, you were also assuming that service would not be the primary consideration for the diversion; is that correct?

A That's correct.

Q Okay. Now I understand. But in any event, this is another KCS special equipped car. As a participant in the Union Pacific control case, do you recall what the ICC said about KCS traffic evaluations of movements in KCS equipment in its Union Pacific control case decision?

A No. I didn't read the final decision.

Q The ICC said at page 729, "there were 21 sample shipments that moved in KCS cars where Applicant --

MR. DREILING: Objection, Your Honor. Is he now introducing evidence for the record?

JUDGE HOPKINS: Are you going to ask a question?

MR. WILSON: I'm going to ask a question.

JUDGE HOPKINS: Go ahead.

BY MR. WILSON: (Resuming)

Q The ICC said at page 729, "There were 21 sample shipments that moved in KCS cars where Applicants contend that protestant ignored car ownership when making its diversion judgments.

"We agree with Applicants that KCS did not take into consideration the fact that these shipments moved in KCS equipment. It is apparent that KCS's equipment was one of the primary factors that caused these 21 sample shipments to be routed over its lines. We foresee no reasons why KCS will not be able to continue to supply the equipment for this traffic and remain in the routing."

And my question is, won't KCS, after the merger, still be able to continue to supply special equipment for Firestone's traffic in order to stay in this route?

A KCS does not lose the opportunity to place special equipment for this particular shipment. However, the shipper is the one that chooses which equipment into which he will put his shipments.

If there is a contract outstanding between the Santa Fe, Southern Pacific, and the shipper for a given

portion of his traffic, he will not choose to utilize KCS equipment. He will choose to utilize Southern Pacific's equipment.

Now, the equipment that we have for this particular movement may be shifted to another movement to New Orleans. So yes, we could use that same equipment in another movement, but not for that particular movement.

Q Would this other movement to New Orleans be a movement that SP, for example, is handling today?

A I don't know.

Q All right. Let's go on to page 877. This is a Cities Service Chemical Company move West Lake Charles, Louisiana to Chicago, Illinois, routed KCS-Kansas City-N&W.

This movement was also originally evaluated as a no-change, and was later changed to a whole loss. I guess my first question is, there were a number of these changes in the chemical traffic. Do you know how many chemical traffic movements you changed from nondiversions to 100 percent diversions?

A No, sir; I didn't keep track of them.

Q Do you recall that there were a sizeable number of those movements?

A We had approximately 1,870 movements that we

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evaluated, and I have no ideas as to how many of those that were petrochemical were changed.

Q Do you think the KCS-Kansas City-N&W route used for this shipment offers the shipper better service than he would get from the new SPSF single line route?

A Could you say that one more time? I know your question, but I want to make certain that I answer it properly.

Q Do you think the KCS-Kansas City-N&W route used by the shipper for this movement offers better service than the New SPSF single line route would offer?

A No.

Q So then, do you think that the better service on the SFSP single line route would have been one of the factors which would cause a KCS loss?

A No. Service by itself would not have caused the loss.

Q Is this another situation where both KCS and Southern Pacific serve the shipper's facility at West Lake Charles?

A Yes, it is.

Q Wouldn't Cities Service be likely to divide its traffic between SPSF and KCS after the merger instead of shifting all of it to the SPSF system?

A If everything was equal, and history is a teacher of our experience, we would anticipate to get a very small share of Cities Service business. Cities Service has historically preferred the Southern Pacific, even where there is comparability of rates, routes, and services.

This particular evaulation was made because of the single line ratemaking capability of the new system which the Southern Pacific did not have premerger, and the fact that KCS would need to acquire the concurrence of any other connecting carrier to move into Chicago, most of which would be more circuitous than the Santa Fe route prior to the merger.

We also had the option of working with the Santa Fe, which was the most direct route, the most service-sensitive route. We won't have that after the merger.

Q So after the merger, you think that KCS will only handle a very small percentage of Cities Service Company traffic, and that will be because Cities Service wants to keep KCS around as a competitive option and a check on the SPSF.

Is that right?

A If Cities Service was still in business, that may be the case. They are no longer there. Southland

AAAS 8048

Industries has taken over the business of the refinery.

Q Are these shipments still moving about the same areas, or have they changed their distribution?

A No. They're still making the same shipments to about the same areas, but you have a different shipper involved.

Q Let's skip a page and move to page 5 on this booklet, SMS-887, another Cities Service's move here from West Lake Charles to Macomb, Illinois. Prediversion route is KCS-Kansas City-Burlington Northern.

Now, this evaluation you didn't change. You left it as a nondiversion. What is your reason why KCS will retain this move?

A Because Macomb, Illinois is the local Burlington Northern point and we feel that the Burlington Northern would still entertain routings with the KCS over Kansas City.

In that sense, we have the more direct route to Kansas City than the Santa Fe/SP would have. We could compete on a cost basis, and that the Burlington Northern wouldn't prefer one over the other. It still was a question in my mind as to whether or not we could take a diversion on it, and I decided there is more going for us than not, so we will not take a diversion.

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Q Okay. Now, what did you mean by present route not affected by proposed application, then? Is that what you just described?

A That's essentially what I just described. You will notice that track location is also checked, which means the track location at the destination.

Q But the fact that the destination shipper here is served by Burlington Northern wouldn't prevent, would it, a route of SPSF-Kansas City-BN?

A That's correct. It would not prevent that route.

Q Okay. But it was your judgment that the merged system could not get this move up to Kansas City?

A It was my determination they didn't have what I call marketing market power enough to overcome the advantage that we have, the short cost advantage that we have.

Q Well, sir, looking back to page 3, for example, is the distinction in this evaluation -- well, what is the distinction between the two evaluations?

A I'm not sure I know what you mean by page 3.

Q It's my page 3. I think it's SMS-877.

A Okay. Would you repeat the question, please?

Q What is the essential distinction between

these two evaluations?

A That the Burlington Northern has a local station and that the Burlington Northern has fairly direct routing to this station.

Q Okay. Now, if you look to my page 2, SMS-880, now I know we're dealing with another shipper, but why wouldn't the reasoning that you just described in connection with the Burlington Northern destination move for Cities Services also apply to this Firestone movement on page 2 and prevent SPSF from getting this all via the Kansas City Gateway?

A Because the Firestone issue revolves around a contract issue. Southland, the distribution for Southland, even though it involves approximately the same destinations as Cities Service had in the past, we're not familiar enough yet with the competitive characteristics that will be exerted on Southland and upon which I can make a judgment that a contract would be utilized with this company.

A lot of the shipments from Cities Service -- I shouldn't say a lot -- on 877 and 887, both shipments are prepaid. That indicates to me that Cities Service will make the shipments on a direct basis.

Q Yes, sir, but on page -- on study movement sheet 877, page 3, you check routes and rates as a

reason for the diversion. I thought you told me that you were assuming that there would be a contract.

A No. I'm assuming singl line ratemaking capability on that one.

Q Okay. Let's move on to my page 6. It's study movement sheet 898, a movement of chemical traffic from West Lake Charles to Detroit, Michigan that is shipped by Hercules Chemical.

This movement was originally called a 100 percent diversion, and you altered the evaluation and made it a no-change.

Can you state the reason why this would be a no-change?

A This is a perfect illustration of what I was trying to get to with the Firestone testimony. The Southern Pacific serves two origin points for Hercules. One is at West Lake Charles and the other one is at, I believe, Bayport, Texas.

We engaged in contract negotiations in competition with the Southern Pacific with Hercules. After a series of months, we finally lost all of the Hercules traffic to the Southern Pacific because they were able to engage in a contract from a point at which we had no capability to compete.

Therefore, all of Hercules traffic has been

lost to us. It will not be recovered, and therefore I didn't feel like we should take a diversion on something that's already been lost.

Q Okay. So this is a no-change because it was diverted as a result of something that doesn't have anything to do with the merger.

A That's correct.

Q And you've already lost it. Okay. I didn't understand that.

And that reasoning applied to all of the Hercules Chemical traffic in your evaluation?

A Yes, sir.

Q Turning to the next page, study movement sheet 976, shipment by Olin Corporation this time, prediversion route of KCS-Kansas City-Burlington-Northern-Chicago-CSX. This shipment was originally judged to be a no-change with the reason A checked, present route not affected by proposed application.

Can you explain the reasoning for the original, the no-change evaluation?

A I don't believe I discussed this one with the initial evaluator insofar as why they made that particular indication. I have to presume that it was their opinion that we would have sufficient market power

of our own to retain the movement.

Q I see. How does the reason routes and rates that you check here support your judgment that this is going to be a KCS loss?

A The destination is on the Baltimore & Ohio Railroad, the B&O. The present route utilized is a three-party route: KCS, BN, Chicago, B&O. Once the Santa Fe and SP merge, you will have a single system route to Chicago.

We are constantly finding in this day of deregulation that because of our inability to have single line routing to some of these gateways, such as Chicago and St. Louis, we need to work with an intermediate carrier, and the revenue requirements for that intermediate carrier are not such that they will join us in these routes to meet single line rates.

Q So in effect, you've been having divisions problems when you can't get to the gateway. Is that what you're saying?

A I wouldn't say it's a divisions problem. We have a problem that the single line carrier is able to make a rate to a gateway at a lesser charge than what we can make with a connecting carrier.

Q Okay. Would you say that the diversion route listed is a better service route than the route by which

the shipment moved in 1982?

A I don't believe it is.

Q Well, it does avoid one extra railroad and the extra interchange at Kansas City, doesn't it?

A It avoids it, but I don't believe that the time in transit would bear up. They may be comparable. We may have a slight advantage. But as far as the time element, there may be six to eight, maybe 12 hours difference in the time frames of delivery.

Q Did you consider the fact that a KCS covered hopper car was used on this movement?

A It came into question as in all evaluations but it wasn't given much importance.

Q Was your assumption here, too, that the merged system would substitute one of its covered hopper cars for the KCS covered hopper car and divert the traffic?

A I see no reason why they wouldn't. And yes, that was the decision, that they wouldn't use our equipment, they'd use theirs.

Q All right. Turning to study movement sheet 991, a PPG Industries shipment from West Lake Charles to Barberton, Ohio, routed in 1982 KCS-Kansas City-ICG back down the St. Louis Gateway-Conrail. You diverted this car away from the St. Louis Gateway and through the Streator Gateway.

This diversion gives Conrail a lower division to Barberton, Ohio, doesn't it?

A Yes, it does.

Q For that reason, wouldn't Conrail use its influence as the destination carrier to try to keep this traffic moving over the St. Louis Gateway?

A This is a tank car, and on tank car carload traffic, Conrail has yet to engage in gateway routing restrictions for southwestern traffic. They allow open routing over -- not open routing, but routing over St. Louis or Chicago.

Q Yes, sir. I'm not talking about closing the Streater route or not agreeing to joint rates over that. I'm just talking about soliciting the shipper.

Wouldn't Conrail use its influence as the destination carrier to try to keep the St. Louis Gateway routing for this PPG shipment?

A I would presume they would. The shipment is prepaid, so it indicates to me the routing is with the shipper, not the receiver.

Q Right. But in this case, the shipper and the receiver are the same company. It's PPG; right?

A It's PPG, but it's actually received by anothe receiver other than PPG. It's a third party billing type shipment.

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Q In any event, you don't think that Conrail's influence as the destination carrier here and it's desire to use the St. Louis Gateway is going to be suficient to enable KCS to retain this move. Is that right?

A Well, I don't think the option is for retainment by KCS, because we again have run into a situation where we need an intermediate carrier. And the option, more than likely for Conrail, is to solicit for Cotton Belt over St. Louis or Santa Fe over Chicago.

I don't think there is going to be any solicitation by Conrail over St. Louis for KCS's account.

Q Well, you mentioned the option of soliciting for Cotton Belt over St. Louis, but that route's a route that is available before the merger. The merger wouldn't have anything to do with the shipment shifting to that route.

Isn't that right?

A The merger gives the Cotton Belt an advantage they don't have today, the ability to offer routing, alternative routing via Chicago and St. Louis. Prior to this, we were in head-up competition with the Cotton Belt between Lake Charles and St. Louis.

Granted, we had to use the intermediate carrier, and there may be a point in time when we would have to forego that business if the Cotton Belt put in routes over St. Louis and generated cheaper charges than what we would be using.

But by offering a contract over Chicago, having the additional capability of offering a contract over Chicago, we get into a situation where KCS would be excluded from the ability to make an equal contract.

Q Well, sir, my problem is that if this move is going to divert, it seems to me that the route that it's going to diver to is going to be SPSF-St. Louis-Conrail. That's a lot more efficient route. And it would be a logical route that the shipper would use, rather than shifting the gateway from East St. Louis to Streator, don't you think?

A Not necessarily. If I were the Santa Fe and I had a long haul route on a shipment that produced $3,000 worth of revenue, I would very sincerely look at using my long haul route into Chicago to get the benefit of those higher per-car charges and make a contract offering the shipper some kind of an incentive to use that gateway instead of a short haul St. Louis Gateway.

The divisional break for the Santa Fe is greater over Chicago than over St. Louis, as you have

already said.

Q Okay. Let's go to the next sheet, then, SMS-709, the movement by Exxon Chemical from Baton Rouge, Louisiana to Los Angeles, routed KCS-Dallas-Santa Fe.

You have diverted this movement to a route of KCS-New Orleans-SPSF. My first question is, does KCS serve Exxon Chemical?

A We serve one side of it. The ICG serves the other side. And it's open to reciprocal switching to the Missouri Pacific.

Q Why would Exxon Chemical short haul its origin railroad, the KCS 100 percent of the time?

A We get into another situation of what I call marketing market power. We have to rely, in this particular case, on the Santa Fe for our route to get this to Los Angeles. We would have a route with the Southern Pacific over Shreveport, I believe, and possibly Beaumont, Texas.

But we've also encounted Southern Pacific route closings to us in -- for this particular traffic that will preclude us from using Shreveport or Beaumont. They're now telling us we have to use New Orleans as the gateway for all Southern Pacific traffic.

So that means for us to get our long haul, we have to use the Santa Fe. Once the merger comes about, the Santa Fe is going to, I would presume, adopt the same route restriction that the Southern Pacific has, and limit us to moving our traffic via New Orleans.

Q Well, why KCS agree to a route via New Orleans when it had the longer haul route available?

A We wouldn't have any option. We would be either taking the New Orleans route or none at all.

Q This is traffic, sir, coming from a KCS-served facility, Exxon Chemical. It's KCS traffic. You're delivering the traffic to us.

A That's correct.

Q Obviously, the new merged system is going to want to handle the traffic and get some revenue for handling it over some route or another. If you don't want to give it to us at New Orleans and you tell us we should take it at some other junction, don't we have to agree to you, as rational businessmen, don't we have to agree with you to handle it by that other junction in order to make any money at all on the move?

A Again, it gets to who has the most market power. If you're sitting there in the catbird seat and saying KCS is either going to have to move this via us or they won't have the movement, and we have other plastics movements, plastics producers that can ship the same commodity to this destination and we serve them directly, KCS is going to have to join with us over New Orleans or lose the movement.

And, very likely, we can work with one of our shippers to displace that movement if they so choose not to work with us on New Orelans.

Q So that's your rationale here. Even though on this move KCS has or may have market power compared to

Santa Fe, it certainly has more influence with the shipper than Santa Fe does.

A I won't disagree with that. We have marked on there number D, or I mean letter D and letter C, which says rates and routes and long haul, single line route. Now, that long haul, single line route means long haul from the gateway or from the junction point of New Orleans.

Q Also, another player in this game is going to be Exxon which, of course, is a very large and influential shipper. Would not Exxon itself make sure that Dallas routing stays in place so it could route its traffic this way and give a reasonably long haul to its origin-serving railroad?

A It's been my experience that Exxon doesn't get involved in these types of harrangues unless it directly impacts them. Now, Exxon also makes plastics at their Baytown facility or Bayport facility, and rather than get involved with that type of a situation, it's very likely they could just switch the supply source to Baytown.

Q By checking service as the reason for the diversion here, are you saying that the shipper would receive better service via the route that you chose, KCS-New Orleans-SPSF, than it recevies via

KCS-Dallas-Santa Fe today?

A I'm not sure why the service was checked. Excuse me a minute. Let me refer to the original. It looks like it was checked by the primary evaluator, and I didn't question it. I don't think that service -- there's a big service differential in this case, since it's non-TOFC type equipment.

So you would handle it in your general manifest trains and so would we.

Q The next move on the sheet is study movement sheet 1479, Mobil Oil Corporation, chemical shipment, routed KCS-Kansas City-Santa Fe in 1982.

This is one of 25 movements in your study from Mobil Oil Corporation moving from Chaison to Los Angeles. All 25 movements seem to have been diverted at 100 percent. Does that sound about right to you, Mr. Plot?

A Yes, sir.

Q Now, doesn't the fact that the KCS could influence Mobil to route this traffic several hundred miles out of line, moving it from the Texas Gulf Coast straight north to Kansas City before giving it to Santa Fe to haul back southwest to Los Angeles, doesn't that fact indicate that KCS has a lot of influence on the routing of this traffic of Mobil Oil Corporation?

A Given the conditions that prevailed at the time of the movement, yes.

Q Wouldn't Mobil want to retain its rail choice by using the KCS route for some of its shipments?

A I would think, as rational businessmen, where they had a choice that yielded them the same results, yes, they would.

Q Would you expect Mobile, like Firestone and Cities Service that we discussed earlier, would continue after the merger to give KCS, to route some of its traffic via the KCS so that it has -- so that it's using both railroads and it keeps both options open to itself?

A After the merger, on this particular shipment we're assuming the same thing happens as has happened with the Southern Pacific as I alluded to with Baton Route, the closing down of the gateways to the long haul routes.

Chaison can be reached by the Southern Pacific on a direct service basis. I see no reason for the Santa Fe, after the merger, that it will want to continue any open routes with the KCS. And the Southern Pacific would simply handle the business without any alternative to the KCS.

Q So again, here, you're assuming that the

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merged system will close the route?

A I'm assuming there will be a disparity created between KCS and the SP by some mechanism where it could be a creation of a differential in the rates, a closing of the route, th downgrading of service with KCS, all are possible options.

Q Wouldn't Mobil Oil have enough influence to persuade SPSF to keep this route open?

A No. I think on the reverse, they would have little influence because of the number of places at whch they require service from the Santa Fe/SP system. Both singly today and when the two become merged, there will be an even greater concentration of service by the Santa Fe/SP at those points, some of which are local.

Q Turning to the next page, sir, SMS-1509 is another Mobil Oil Corporation move from Chaison, Texas, this time to Chicago, Illinois, routed KCS-Kansas City-Santa Fe.

This move was originally determined to be a KCS loss, and then changed to a nondiversion. Why did you change this evaluation?

A Because the receiver is the router of the traffic. And after questioning the people that made the initial evaluation, they couldn't come up with enough information to convince me of what the routing practices

or the impact would be upon that particular receiver.

Therefore, I said we won't take that as a diversion.

Q I see. And that's what you meant when you said that this move is not affected by the proposed transaction?

A That was just more or less of a general category to indicate that it was not a lost movement to us.

Q Okay. Let's go to the next page, then. Page 1714. We have a chemical shipment again, this time from Texaco. I think we've hit almost all the major shippers down there, routed in 1982, KCS-Kansas City-ICG.

You diverted this movement for a reason you list under G; that Texaco supports merger. What did you mean by this reason?

A Excuse me for a minute. That was kind of a secondary comment to indicate that since we had indicated rates and routes were our primary -- and long haul were our primary reasons, then Texaco has supported the Santa Fe/SP merger, it just seemed to us natural that there would be one more reason for us to expect we wouldn't receive any participation in that traffic.

Q Are you aware that over 330 shippers support the Santa Fe/Southern Pacific merger?

A I know there's a great deal; yes.

Q Do you think that all of these shippers will divert all of their business to the SPSF system whenever it's reasonably possible to do so?

A With everything being equal, I'm sure a lot of those shippers will try to maintain some competitive options.

Q Okay. And would not Texaco also want to try to maintain some competitive options and use KCS on some of its shipments?

A It's very possible. However, KCS participates in other Texaco traffic today, where the Santa Fe/SP merger would not hinder our ability to compete, and Texaco may just think, well, that's enough for KCS.

Q It's also possible, isn't it, that because KCS participates in other Texaco traffic, that KCS and Texaco have a better relationship perhaps than SFSP and Texaco would have, so that it would be easier for KCS to write a contract with Texaco and link these movements together and thereby enable itself to retain the business?

A No, I don't agree to that, because one of the major movements that Texaco has is out to Wilmington, California. And I don't think we would be able to write a contract on that.

We only have access to one or two gateways, to one gateway where the Santa Fe/SP will have access to many more gateways and other connecting points. So I think Texaco would write a contract with the SP/Santa Fe before they would with us.

Q Do you know why Texaco is supporting the merger?

A I believe I read their statement, but I'm not sure as to how it reads. I think it was somewhat along the improved efficiencies.

Q Mr. Ploth, we identified over 60 Texaco shipment diversions in your sample. Was Texaco's support of the merger one of the diversion reasons for all 60 of those evaluations?

A I can't tell you unless we go through them individually. I don't believe it was. It's probably listed on most of them because that was something that our people thought was important to note.

It could be that the maker of the decision for gain or no gain where everything else may be equal --

Q So for some of the movements, the key turning point that caused you to go ahead and call the movement a whole loss was the fact that Texaco supports the merger. Is that what you're saying?

A No, no. I'm saying there could be a situation

that arose where, if we had the decision would it be a whole carload gain or a whole carload loss, and because Texaco supported the merger, that very well could have been a pivotal point or pivotal issue.

Q Okay. Let's turn the page to No. 1248. Here is another chemical movement where Texaco is the consignee. It moved in 1982 ConRail-Chicao-C&NW-Kansas City-KCS. You diverted it to ConRail-Streator-SP&F.

One of your reasons here is that Texaco, as the consignee, supports the merger and that's going to help cause this diversion.

Was the consignee controlling the routing on this traffic?

A Excuse me while I get the original.

Q Here's one where you may want to look at the waybill.

(Pause.)

A Now, this was prepaid, so it looks like the shipments were paid by Exxon and routed by Exxon.

Q How would Texaco, as the consignee on this movement, have more influence on the routing than Exxon as the shipper?

A I don't think that that particular comment, as put down by the evaluators, was the deciding factor as to whether or not we made this evaluation

Q Okay. So the deciding factor here is probably the routes and rates reasons?

A Route and rates and the long haul again.

Q Now, this movement was originally evaluated as a no change. But there was no reason checked to support that.

What was the reason for the original no change evaluation?

MR. DREILING: Which are you on?

MR. WILSON: 1248.

MR. DREILING: I don't see no change.

MR. WILSON: It was originally evaluated no change, and that's been marked off.

THE WITNESS: I have no idea as to why that wasn't marked number A. I think usually A was marked when there was no change and indicated on the first round.

BY MR. WILSON: (Resuming)

Q Doesn't the fact that KCS got its Kansas City haul on this movement indicate that KCS has quite a bit of influence over how this traffic gets routed?

A Again, we have a situation where the Southern Pacific and the KCS compete at a given point, which is Port Arthur, Texas.

We have another situation where they have --

will be able, postmerger, able to offer more gateways than the KCS can offer. The movement for KCS required the use of an intermedial carrier, C&NW. After the merger, Santa Fe/SP will have a single line route from Chicago and that's the junction at which ConRail interchanges to the C&NW.

It's going to be very difficult, if there's a downward pressure on the rates or any type of a contract offering by the Santa Fe/SP on a multiple gateway condition contract, for KCS to compete.

There is more going for the Santa Fe/SP merger partners on offering gateway contracts than the KCS can offer, and with that type of weight against it, I couldn't see not taking a diversion.

Q Okay. So again here, you're pegging your diversion on the lower rates and contracts that the SPSF would offer to the shippers?

A The ability to offer more diverse contracts.

Q Okay. Now, study movement sheet 1730. On the next page, a movement from Port Arthur, Texas to Rock Island, Illinois. This is one of only two Texaco nondiversions that we found in your study.

It was KCS-Kansas City-Milwaukee, and it stayed that way. What's the reason why this is a no-change?

A I would guess it's because the Milwaukee was utilized, and the fact that the Milwaukee has service to Rock Island, Illinois, probably is better than anyone else, and the fact that from Port Arthur to Kansas City, the KCS has a slightly more direct route than what the SP and Santa Fe would have to interchange with the Milwaukee, and that there is a chance that we would be able to retain that traffic on a cost basis method of competition.

Q Okay. Well, now how would you distinguish this evaluation from the evaluation two pages back, the SMS-1714 which you diverted to SPSF?

A Because the routing of the Illinois Central Gulf is more circuitous via Kansas City than it would be via Chicago and by the fact that Santa Fe can reach Vermont, Illinois on a direct service basis, whereas they can't reach Rock Island, Illinois on a direct service basis.

Q I think you may have convinced me on that one, sir. Why don't we move to the next page? SMS-1784. Here is yet another Texaco movement. This time it's from a KCS local point, I believe; Port Neches, Texas. Is that a KCS local point?

A Yes, it is.

Q Okay. It's routed KCS-Shreveport-LA. Okay.

So KCS-Dallas-Santa Fe in 1982. And you diverted it to KCS-Beaumont-SPSF.

This is a route that severely short hauls the KCS, does it not?

A Yes, it does.

Q How long would the KCS haul be on this postdiversion route?

A Fifteen or 20 miles.

Q As opposed to a several hundred mile haul on the 1982 run?

A Yes.

Q Now, now is KCS local origin a reason for KCS's loss of this business?

A It's a puzzle to me, too.

Q I thought it might be. Okay.

Why don't you think that Texaco wouldn't continue to favor KCS with long hauls to Dallas coming from this local point?

A Excuse me a minute. I need to get the original of that. I just thought of a question.

(Pause.)

I'm sorry. Go ahead.

Q Why wouldn't you think Texaco wouldn't continue to favor KCS with its long haul to Dallas coming out of this local point?

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A For the same reason identified in New Orleans at Baton Rouge, where we have the same type of situation existing, the SP route closings to KCS on a long haul basis.

Q Well, since this is a movement from a KCS exclusive origin, couldn't KCS simply refuse to join in a route over Beaumont? And then if SPSF wanted to handle the business at all, it would have to do it over Dallas? Isn't that right?

A There are very few movements for Texaco that -- for this particular product -- that move to other areas that don't have competition with the Southern Pacific.

If we refuse to agree to the Southern Pacific's requests, it's very likely this traffic wouldn't move for us at all. There are other producers of the same commodity at other Texaco facilities that we don't serve. And the transition could be simply to move from that facility.

So I think in order for us to handle anything, we're going to have to capitulate to anything that the Southern Pacific would request.

Mr. Wilson, we're talking about market power in a marketing sense.

Q You don't seem to have much confidence in your

own salesmanship it seems.

A It's not salesmanship.

Q We'll move to the next page. SMS-948. Another chemical traffic move from PPG Industries, Westlake, Louisiana to Greeley, Colorado, routed in 1982 KCS-Kansas City-UP.

This move is a nondiversion, and the reason listed in the lower left-hand side of the page is movement would have been diverted, account UP-MP-WP system merger.

Could you explain what you meant by that?

A Well, under the traffic parameters that we had for the UP merger, and I'm not sure, but I think one of the individuals that were evaluating this said this particular shipment actually came up -- we evaluated it as a loss to the system or as a no-change. I don't recall which, but in any event, it would have been evaluated in the Union Pacific merger as directly related to the movement within that merger geographical configuration.

Here, it would not be affected by this merger as much as it would be affected by the UP merger.

Q Okay. So your assumption is KCS would have already lost this move to Union Pacific, so it wouldn't have it available to lose to SPSF?

A If that was the decision to lose it.

Q Did you assume the full impact of the MP/UP merger would already be in place by the time the SPSF merger is consummated?

A No. I don't think it was that as much as looking at the long range conditions that would exist.

Q Okay. But the way you did your study, you first determined how much traffic you would lose to the MP/UP merger, and then if the car was still on KCS, you decided whether or not you would lose it to the SPSF merger? Is that right?

A No. I think the way we would probably have looked at is, given the two options or the two mergers, who would be the residual carrier with the most market power and they would be the one to take it away from us.

Q There you go again. Well, we'll go to the next page, No. 1126. SMS-1126 is a Cargill, Inc. move to Pilgrim Industries at Pittsburgh, Texas. It moved from Kansas City to Pittsburgh, via KCS single line.

You judged this move to be unaffected by the proposed transaction. Can you elaborate on your reason why this is a no-change?

A Because the point of origin is Kansas City, Missouri, and we have probably the most direct route

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from Kansas City to Pittsburgh, Texas. The fact that this grain was not in transit so it came out on a flat rate and that indicates that in the past few years, flat rates have been made more on a basis of cost than anything else, so since we have the shortest route, should have the lowest cost advantage between the two points that we serve, there should be no reason for us to lose it.

Q Okay. And you call this a nondiversion, despite the fact that a Santa Fe covered hopper car is used for this grain shipment; right?

A That's right, because we have plenty of covered hopper cars sitting around in Kansas City that we'd love to use for them.

Q Turning to the next page, and we've finally left chemicals, by the way, in the last few, and we're into the grain traffic now. Here we have another Cargill shipment from Wichita, Kansas to Pittsburgh, Texas, routed MKT System-Dallas-L&A in 1982, and you diverted this to SPSF, despite the fact that neither Santa Fe nor Southern Pacific was in the prediversion route.

That's correct?

A Yes, sir.

Q Did you take into account in looking at this

move the fact that the origin railroad in the prediversion route, the MKT supplied a covered hopper car for the move?

A I'm not sure whether or not that was taken into consideration.

Q Well, just thinking about the factor of equipment supply, wouldn't the fact that the MKT supplied the car to Cargill influence Cargill to keep using the prediversion route?

A Here again, you get into a situation where things have changed since that point in time. If the merger is accomplished, the Santa Fe/SP will again have single line service between origin and destination. KCS must have participation with the origin carrier, as well as the Katy must have participation with us in competition with that single line service.

The grain rate structure in the past three years has been coming down, down, down. There is a downward price on it, and the only survivor in that price war, if I can call it a price war, is the single line carrier that has direct service between two points.

We're finding more and more instances where the KCS cannot compete against single line systems with that downward price mobility.

Q Have you noticed in the grain price war that you allude to, that the MKT generally has lower or lowest grain rates for movements?

A I know they have a significant number of low grain rates. I don't know the exact number because the only time I would become associated with them is when we have to deal with them.

We have also found out lately that we can't even compete with their -- I mean compete connecting with their low rates.

Q Now, you considered the fact that Texaco and other shippers support the merger in making your diversion decision.

Did you consider the fact that Cargill is a strong supporter of the MKT's position in this case when you were looking at this movement sheet?

A My impression of Cargill's support is that they are not opposed to the merger, and they are supporting rights of other carriers where it results in uncompetitive situations arising.

Q Sir, you checked service as one of the reasons to divert this traffic. Doesn't KCS serve the destination at Pittsburgh, Texas?

A Yes. It's open to reciprocal switching.

Q Okay. Wouldn't the fact that KCS is doing the

actual switching at the destination influence the shipper not to divert this traffic?

A Not if he has a single line rate to call on from origin to destination and we don't participate in it.

Q Sir, in the Union Pacific control case again, the ICC refused to accept 12 diversions of sample cars to Pittsburgh, Kansas, stating at page 729 of the decision again, the terminating carrier which serves the consignee exclusively, KCS-LA, has enough influence over the routing of these 12 sample movements to be able to handle this traffic from the present interchange points.

Now, in light of that ICC finding in the Union Pacific case, don't you think that in fact KCS will be able to maintain its junctions on traffic moving into Pittsburgh, Texas in response to the SPSF merger?

A I can't make a judgment on that because I don't know all the particulars that they took into account when they made their decision or what those movements were.

They may be related to this; they may not.

JUDGE HOPKINS: Mr. Wilson, I think this would be a good time for a luncheon break.

We'll be in recess until 1:30.

(Whereupon, at 12:30 o'clock p.m. the hearing recessed, to reconvene at 1:30 o'clock p.m., this same day.)

AFTERNOON SESSION

(1:30 P.M.)

JUDGE HOPKINS: Let's get back on the record. Are you ready again, Mr. Wilson?

MR. WILSON: Yes, sir, I am.

Whereupon,

I. WILLIAM PLOTH,

the witness at the time of recess, having been previously duly sworn, resumed the stand, and was examined and testified further as follows:

CROSS EXAMINATION - RESUMED

BY MR. WILSON:

Q Mr. Ploth, turning to Page 19 in the booklet of study movement sheets, we have a study movement sheet number 504, an Agri Industries movement routed in 1982, N&W, Kansas City, KCS, Shreveport, Southern Pacific. This movement was originally diverted to a route of C&NW, Kansas City, SPSF, but you scratched that off and changed it to a non-diversion.

What was your reason for that?

A In the Missouri Pacific/Union Pacific merger, there was a settlement agreement between the C&NW and the UP. Part of that was called the pooling agreement, and because of that agreement, it initiated some further exploration on our part of whether or not there would be

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lost traffic.

Because of the way the pooling arrangement was structured, it had indicated to us that there would be a capability of loss of peculiar type traffic, mostly grain, out of Iowa, and because of the study parameters involved with that particular study, had this traffic shown up, it would have been classified as a diversion, so therefore we decided there would be no diversion in this case.

Q Okay. Now, sir, we found 18 study movements from C&NW origins to Agri Industries at Houston, and they were all listed as no change, usually with the notation of MP/UP in the lower lefthand side of the page, like it is on this sheet.

Was it true that the rationale for all of these movements was your evaluation that KCS would not lose the traffic to SPSF because KCS already had lost the traffic to the MP/UP merger?

A I don't know that I can say we looked at every piece of -- I am sorry, that we looked at every shipment and made a judgment that it had already been lost to the MP/UP merger.

I think the reason it wasn't considered is because we would have already evaluated them in the MP/UP merger, and had there been a diversion it would

have been due to that pooling agreement, and not the Santa Fe-SP merger.

Q Okay, and that was your rationale for all of your Agri Industries movements in your sample going to Houston?

A Yes.

Q I think we are ready to move to the next sheet, SMS Number 587, another grain shipment on Continental Grain this time from Hutchinson, Kansas, to Beaumont, Texas, routed Cotton Belt, Kansas City, KCS.

You list as the reason for your diversion here the fact that Continental Grain supports the merger. Could you elaboarte on that reason, please?

A Again, it goes back to what I said earlier about Texaco. This was just put in there as a notation for us to keep in mind so that we knew what type of response this particular shipper had to the Santa Fe merger in the event that we needed to rely on that as, say, a tiebreaker.

I don't know we made a decision that this movement was diverted because of that. In fact, I wouldn't have made that decision.

Q Do you know why Continental Grain is supporting the merger?

A Not really. We didn't look into it, because

it wasn't necessary on this particular sheet.

Q Cannot Santa Fe move this shipment by its single line route from Hutchinson to Beaumont, Texas, today?

A Yes, it can.

Q What about the merger will cause Continental Grain to shift the routing of this traffic?

A Excuse me. I am looking at the settlement records and the waybill record.

(Pause.)

A I thought this was all backed by transit, but I don't see the indicator on here.

Q In light of the lack of a transit reference, wouldn't no change be a better judgment here?

MR. DREILING: I think there was a question pending, Your Honor, and I don't know whether I heard an answer to it.

JUDGE HOPKINS: There hasn't been an answer yet that I know of. Then we can go on to the next one.

THE WITNESS: I don't see the transit here, and if that is the case, that there is no transit behind it, I may have to disavow our diversion due to the merger.

BY MR. WILSON: (Resuming)

Q Thank you. We are making progress. Let's

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move to SMS Number 1657, Georgetown Steel movement from Korf, Texas, to Joliet, Illinois, routed KCS, Kansas City, Santa Fe, in 1982.

At the bottom of the page Mr. Byrd, it looks like, wrote, "We hope we will have -- we hope to have as much power" -- let's see. I'll try it again. "We will hope to have as much market power after merger as before. Georgetown Steel does not like SP."

Do you agree with Mr. Byrd's first sentence here, that KCS will have as much market power after the merger as it does now?

A On this particular shipment, I would have to say no. It again is a situation where, yes, we will have some market power in certain instances; in others we will not.

This particular shipment was tendered by us to the Santa Fe at Kansas City, and I don't believe the Santa Fe would join us in our route and rate in the future. Georgetown Steel rates are constantly changing because of competition from other steel makers into the area that they are trying to penetrate.

It requires usually less rate than what is existing in the tariff, which means there is going to be a reduction at some point in time, and if I remember right, this particular rate was adjusted at one time,

and we got the Santa Fe to join us.

I don't think they will join us in the future, now that they will have a single line system route all the way to Chicago.

Q As the rail carrier for Georgetown Steel on this iron and steel move, your ratemaking is constrained by the fact that your shipper is competing with other steel companies to try to serve these markets. Is that right?

A On this particular movement, they were competing with steel out of Minneapolis.

Q Okay. So if you wanted this movement to move at all, you had to quote a rate, so the delivered price into Joliet would be such that Georgetown Steel could get the business, right?

A That's correct.

Q Now, do you think when Mr. Byrd was referring to the market power of KCS, that he was reflecting the fact that KCS had gotten its long haul on this movement in the pre-diversion route?

A I think Mr. Byrd really was talking about our relationships with the shipper had had a tremendous turnaround in the past, within the past year, and we have been concentrating on our efforts at this individual shipper, and because of that, we have enjoyed

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a tremendous surge in the outbound tonnage.

I think Mr. Byrd was primarily talking about our relationships with the shipper rather than our market power.

Q Okay. All right. Well, let's turn to Study Movement Sheet 706. Wait a second. I have another question still on that one.

I still have another question on the Georgetown Steel move. You checked equipment as one of your reasons for the diversion. In light of the fact that the equipment used for this was just a plain gondola car, how does the equipment influence the shipper's routing?

A Well, I think the answer is the Santa Fe equipment. The Santa Fe does not get into Korf, Texas. Only the Cotton Belt or the SP. And after the merger, the SP and Santa Fe equipment will be considered as one.

So, as the applicants will have single line service, they will also have the same piece of equipment to use in this particular movement.

Q In your experience, does the provision of gondola cars, plain gondola cars, influence shipper routing decisions?

A It depends how you define a plain gondola

car. For wire rods, which is the product here, which is a coiled steel product, they need a certain type of configuration to get the maximum loading in that particular car, and just any type of gondola won't work. It has to be a high-sided gondola.

It has to be of the 60-foot variety most of the time. It has to -- some gondolas at times are required to have wooden decks or wooden planking put in. So, you can't say generally that if a man seeks gondolas, any goniola will suffice tor his needs.

Q Okay, and on this movement you think that the fact that it is Santa Fe's gondola is one of the reasons why the shipper will shift his traffic to the merged system. Is that right?

A No, I am just saying it is already in a Santa Fe piece of equipment, and that the Santa Fe will then after the merger become one and the same as the Southern Pacific, so there will not be a need to bring in new equipment for them.

Q Okay. Now let's move to the next sheet, sir. Study Movement Sheet 706 is a move from North Baton Rouge, Louisiana, to Hanford, Connecticut -- Hanford, California -- I am sorry -- routed KCS, Dallas, Santa Fe.

KCS provides the origin service on this move,

and also furnished special equipment for the shipment, did it not?

A It is a KCS car. Yes.

Q Wouldn't these factors tend to influence the shipper to keep KCS in the route and continue to give KCS its Dallas haul on this traffic?

A No, because we go back to the same situation we were discussing earlier with Exxon. The Southern Pacific routing policy that has already been issued in the tariffs restricts our routes out of Baton Rouge to apply only via New Orleans.

Now, our alternative in this particular shipment was to use the Santa Fe. Once the system becomes merged, I have no reason to believe they will change their routing policy of restricting the routes over New Orleans.

Q Well, why would the shipper agree to a short haul route for its origin carrier, KCS?

A The routing restriction is already in the tariff. We have had shippers come to us with rate requests that we have had to turn down because we can't get our maximum revenue, or we can't get a profitable revenue over New Orleans.

And they didn't bring any pressure to bear on the Southern Pacific at that time, so I don't see why it

would change in the future.

Q Why would KCS agree to a short haul route here instead of just forcing the merged system to take the traffic at Dallas?

A The only thing that would need to be effected is a change in the tariff, which was done with the Southern Pacific route. We had no say in that matter whatever. One day we woke up and there's the tariff restricting our participation.

Now, I don't see why that's any different than what we can expect to happen in the future.

Q Well, you are aware of the merged system's routing policy in this case in that Mr. Fitzgerald testified that in fact the merged railroad would not do that, that the merged railroad would maintain all through routes?

A At the same rate levels? You could maintain the same routes, but not at the same rate. And you are in the same non-competitive situation.

Q Are you familiar with Mr. Fitzgerald's testimony?

A No, I am not.

Q Let's move to SMS Number 390, a movement from Florida to Kansas City, Missouri, in which the KCS gets it at New Orleans and takes it to Kansas City. Here you

mark the fact that the consignee was served by Santa Fe as a reason for the diversion. Why would that influence the shipper's routing of the traffic?

A Since the Southern Pacific-Santa Fe would have single line route capability from New Orleans to Kansas City, and since Thompson Hayward is served by the Santa Fe, and we have, I would say, a very great degree of difficulty in getting shipments out of Thompson Hayward on an outbound basis, that I can't see why Thompson Hayward would not agree to routing it by the single line route into Kansas City.

Q But KCS has a single line route from New Orleans to Kansas City, too, right?

A Yes.

Q If Santa Fe had influence with the shipper, how come it is not already getting a haul, say, to Dallas on this move?

A I can't answer that question.

Q Is the consignee controlling the routing of this movement?

A The only thing that I see on the way bill indicates the car is trip leased to the consignee, but I don't see the terms of payment on here.

Q Let's move on. The next move is SMS Number 642, a movement from Bayou Pierre, Louisiana, to Los

Angeles, California, an International Paper Company movement.

You diverted this movement, sir, to a route of KCS, Beaumont, SPSF. Again here my question is, why in your opinion would International Paper shorthaul its origin railroad on this movement?

A If all things were equal, International Paper would not shorthaul us.

Q They would not?

A That's correct.

Q Let's move to Number SMS 637. This is a COFC movement from Baton Rouge, Louisiana, to Oakland for export. You have routed this movement via, I believe it is KCS, New Orleans, SPSF. And in part your reason is service. How much better service would the new route offer for this movement than KCS, Dallas, Santa Fe?

A I am not sure what the service would be from -- in comparison to the service we would offer out of Baton Rouge. This is a steamship container which would move in an expedited service train.

Formerly we handled this with the Santa Fe over Dallas using the Big D connection. We would run this in our runthrough train operation from Shreveport through Dallas, where the Santa Fe would pick it up, run it out of Brownwood all the way to the destination.

Q I understand that, but now on this particular movement you have got it routed in what is sort of a backhaul where KCS would haul it from Baton Rouge back down to New Orleans, and then it would move SPSF out to the west coast.

Is that right?

A But I haven't finished with my explanation as to where we are going.

Q Well, I have a question pending on that anyway.

MR. DREILING: Had Mr. Ploth finished his answer to the prior question, I guess?

JUDGE HOPKINS: That is what I was saying. He hadn't finished his answer.

MR. WILSON: But I don't think his commentary was responsive anyway.

JUDGE HOPKINS: Go ahead and finish your answer.

THE WITNESS: After the merger, we expect the train transit times in the runthrough operation to change drastically, so that there very definitely will be a preferred service advantage from New Orleans to Oakland.

We also, the way this was evaluated was a KCS shorthaul to New Orleans, since this is a container.

After looking at it again, I don't think we will even see that particular movement. It would be more costly to run it over our railroad down to New Orleans than it would be to dray it over the highway down to New Orleans and put it on the TOFC train.

BY MR. WILSON: (Resuming)

Q Okay. So if this gets diverted, you think it would be diverted by some kind of a truck-rail joint service and originate on the railroad at New Orleans?

A I think the cause of the diversion would be the downgrading of the Big D service that will occur, and in fact we have evidence right now that that downgrading of service has occurred, and we no longer have the option of doing some of the runthrough operations that we had prior to some time in November.

Q Let's move next to the last page, Page 27, which is a movement from Mead, Georgia, to Kansas City, Missouri, routed Southern, Memphis, Cotton Belt, Texarkana, KCS in 1982.

This was originally called a diversion. It then changed to a non-diversion. Was the reason for this the fact that SPSF's route from Memphis to Kansas City that would be used here is the same route that SP already has today between Memphis and Kansas City?

A The reason I took this or changed the

diversion or we changed the diversion was the fact that I felt we had an equal chance of getting this traffic over New Orleans as the applicants would have getting it over Memphis.

From this particular point, Southern Railway engages in routing over New Orleans and Memphis on an equal basis. There is a breaking point within the south where the Southern Railway does not allow traffic to go over New Orleans, and will only allow the routes to apply via Memphis.

So, where there is a possible equality of service over New Orleans with Southern Railway to this particular point, I felt that it was not proper to take the diversion.

Q Well, when you said that the present route is not affected by the proposed application, were you also thinking about the fact that SP's route and service between Memphis and Kansas City will be the same after the merger as it is today, before the merger?

A No, they will have -- after the merger they would have more routing availabilities than they would prior to the merger.

Q But not for this movement, not between Memphis and Kansas City, would they?

A Today they have the opportunity to route that

from Memphis up through East St. Louis and over to Kansas City, where after the merger they will have the other option of routing it in through Dallas and up via the Santa Fe.

Q Right. But if this were to have been a diversion, the Southern, Memphis, SPSF, what was written there and crossed off, the way that it would be handled would be the way SP would handle it today, through St. Louis and over to Kansas City.

That is a much shorter route than going over to Dallas, isn't it?

A I can't say they would handle it that way. They have to pay trackage rights to handle it from St. Louis over to Kansas City. I have no idea the cost of those trackage rights, and it may indeed be cheaper for them to run it over their existing system routes into Dallas and up through into Kansas City based on the traffic flows and the volume characteristics.

Q Okay. So you don't know how the SPSF would handle that?

A That's correct.

Q Okay. Now let's go back to Page 26, SMS 1424, a movement from South Carolina to Kansas City by Southern, Memphis, Cotton Belt, Texarkana, KCS, and this shipment was diverted to the SPSF's route from Memphis

to Kansas City.

A I haven't located the sheet yet, Mr. Wilson. What was the sheet number that you said?

Q SMS 1424, Page 26, the next to the last sheet in the exhibit.

A This movement you did divert, sir, and the route that you chose for SPSF is the route from Memphis to Kansas City, which as we were discussing on the last move is a route that Southern Pacific has available today, is it not?

A Yes, it is.

Q You also list here MoPay's support of the merger as one of your diversion reasons. Do you know why MoPay is supporting the merger?

A No, I don't. You'll be happy to know that after looking at this last night, I decided that this was improperly taken as a diversion.

Q I will be happy to know that. Thank you very much.

I think on that note I will stop. That is all the questions I have.

JUDGE HOPKINS: Mr. Dreiling? Justice Department?

BY MS. BUDEIRI:

Q Good afternoon, Mr. Ploth. My name is

Priscilla Budeiri, and I represent the United States Department of Justice.

For traffic moving between California and the southeast, is SF-KCS joint line service competitive with SP single line service?

A It is competitive by the fact that we are able to offer service and participate in traffic today of large volume characteristics. Insofar as transit times, it depends upon where the shipments are originated and terminated, but we have found for the most part when we are talking about New Orleans, for example, and the New Orleans gateway, we are very competitive with the Southern Pacific.

Q From a shipper's perspective, what advantages of single line service are lost to joint line service, if any?

A What advantages of single line service are lost to joint line service?

Q Do you understand the question, Mr. Ploth?

A I am not really sure what you are trying to get at.

Q What advantages of single line services are lost to the shipper through joint line service?

JUDGE HOPKINS: If asked to move joint line service? Is that what you are saying?

BY MS. BUDEIRI: (Resuming)

Q Yes.

A It depends what the advantage of single line service is. If you take transit time, for instance, and we are dealing with a situation where transit time is very critical in the distribution process, and you have a joint line carrier that cannot provide a competitive transit time, then the short line system has the competitive advantage.

On the other hand, if the transit time is not critical, then there is nothing lost by having only joint line service or having joint line service and single line service.

Usually joint line service does not take away anything from single line service. If you have a joint line, a combination of joint line competition and single line competition, and you have the removal of joint line competition, then the single line system has the tendency if it is a local movement or if there is no other competition, the single line system then has -- I will call it a lock on the marketplace, so that the joint line -- there is no opportunity for joint line traffic to occur.

I don't know if I have answered your question, because I don't really understand what you are trying to

get to.

Q Given the same transit times, not looking at the transit times, are there advantages that a shipper receives from single line service that he doesn't get from joint line service?

A Yes, there are advantages. There, for example, would be single line billing. You have direct handling of equipment. No interchange is required. There should be some less transportation resources consumed by a single line route than a joint line route.

But that doesn't mean that a joint line route can't overcome those disadvantages. If there are two parties to a joint line route and working together, they should be able to fairly well approximate the same characteristics as a single line movement.

Q How can participating carriers on a joint line movement overcome those advantages of single line service?

A Again, by working together. I think the example of the Big D that we have talked about throughout this whole proceeding is an illustration of that. We have had joint sales efforts between the KCS and the Santa Fe. We have complemented each other. We have utilized their force on the west coast. They have

utilized our force in the Gulf coast and in the east.

We have developed runthrough train operations and refined them to the point where costs of operating are not much different than running on a single line basis, and sometimes they could be better by the fact that you are coordinating your efforts for a given traffic pattern, and on a single line system they are trying to accommodate all traffic patterns.

There is a lot of variabilities that come into play here, but by just plain ccoperation, a joint line system can work out things that are just as efficient as the single line system, or at least close to them being the same efficiency.

Q What does the cooperative preferential solicitation that you have discussed in your testimony in reference to the Big D route mean?

A I think if you refer to the market impact analysis, you will see where we refer to sales blitzes, and what happens is, we may join another carrier sales force and design our sales approach for particular shippers, for particular segments of traffic, for particular markets, and we will give preferential treatment to those shippers for the tendering of large volumes of traffic.

I don't mean preferential to the exclusion of

someone else. I am saying it is a package that is designed for that particular shipper. He may have a large volume of traffic, such as a freight forwarder.

And if he offers us a large volume of traffic with a significant savings that we can incur because of less car handlings, or he has some other shipments in the reverse direction and we can backhaul the traffic, that is the kind of things that I have reference to.

Q In reference to the requirements in the proposed IRMA agreement designed to ensure KCS receives non-discriminatory and coordinated service, what costs would be associated with monitoring compliance with the terms of that agreement?

A There certainly would be costs of personnel. We would need to utilize some type of inventorying system or information tracing system, which I imagine would be our computer network, so there would be a cost associated with that.

From my perspective, they are somewhat intangible as to being able to identify the specific costs.

Q What do you mean by intangible?

A It would depend upon the degree of monitoring that would have to take place before we would be able to -- and not only the monitoring, but the people

associated with that, and the tasks involved, and the resources that would be used before we can say we expect this is the cost that it is going to be.

We know there are going to be at the outset about six or seven people associated with the endeavor. Therefore we can identify what those costs are. But the intangible costs of exactly what their day-to-day responsibilities would be are something I can't identify.

Maybe that has been covered somewhere else. I don't know.

Q What costs would be associated with enforcing the agreement?

A Again, I don't expect that if the agreement is entered into, that there would be much of a cost associated with enforcing it. Of course, we would have to go through the monitoring techniques that we touched on earlier, but I think once it is in place, we wouldn't have to do a great deal of policing.

Q If the merger is approved, will KCS be satisfied if it can maintain the traffic it has at present?

A I don't think any company can be satisfied with the status quo. I certainly wouldn't be. I think the most important thing here is, do we bring something

to the merger to offer the interests of the public, and we are willing and able to try to offer ourselves to be the public protector, if you will, but I wouldn't be satisfied with the status quo, no.

Q If the merger is approved and KCS is granted the IRMA it seeks, will KCS prefer to interline with SP through the Big D connection or use the IRMA across the southern corridor?

A In certain instances, we probably would prefer the Big D operation, but in order to really appreciate the reason for the IRMA request, we would have to, for certain traffic, utilize the IRMA route.

One of the big reasons we need the access to Houston is for container traffic, export and import container traffic, and we wouldn't want that -- we would not require or want that running by Dallas, because we are competing with the Santa Fe-SP, and if we don't have access to the same route, we would lose that competitive situation.

Q In which instances would you prefer the Big D?

A I think in instances where the traffic is more geographically parallel to our operations from Dallas to Shreveport. If we are talking about traffic on the lower cost, such as Houston and New Orleans, I think we

would prefer the SP's operation.

Q In the instances when KCS would prefer to use the IRMA, if the applicants prefer to continue interlining, would you insist on using the IRMA?

A We would have to be very much assured that everything else would remain equal before we would agree to the use of the Dallas interchange, or Fort Worth. Actually what we are talking about is Fort Worth post-merger.

But there are such things as train schedules that would have to be matched, rates, and equipment service that would have to be honored and equalized. It is hard to say without looking at the specific application of the traffic that would be involved.

If we are talking about container traffic, I don't think so. I think we would prefer that lower coast route.

Q What do you mean by remain equal, that you would have to be sure that everything would remain equal? Equal to what?

A Equal to what the SP would be able to offer. We would need to be able to offer the same rate coverage, the same route coverage, the same gateway coverage, the same service capabilities.

Q Thank you, Mr. Ploth. That is all we have.

JUDGE HOPKINS: Does the Department of Transportation -- I don't see anyone. Mr. Dreiling?

MR. DREILING: I have a very few number of questions on redirect, Your Honor.

REDIRECT EXAMINATION

BY MR. DREILING:

Q Mr. Ploth, would you refer to Page 3 of your statement, marked KCS-14?

The last complete sentence on the first incomplete paragraph, do you see it, starting, "In the past," at the top of the page?

A Yes.

Q I am referring specifically to the phrase which Mr. Wilson asked you about: "I have observed the situation where the need to compete intramodally outweighs the need to compete intermodally."

Do you recall in the course of your cross examination with respect to that phrase Mr. Wilson's discussing containerizable traffic?

A Yes.

Q And with respect to containerizable traffic, would that be what we would call TOFC/COFC traffic?

A Yes, it would.

Q Now, is all of the containerizable traffic which KCS participates in exclusively truck

competitive?

A No, there is intramodal competition as well for that same type of traffic.

Q The next question was going to be, is some of it rail competitive traffic?

A Yes.

Q Is some of it exclusively rail competitive traffic?

A Yes.

Q Now I would like you to look at Page 4 of KCS-15, in the middle of the page. You made a statement which Mr. Wilson inquired of which goes, "Furthermore, the movement selected for review and contained in the work papers are not a representative sample of all movements treated."

You are not putting yourself forth as a statistician, I take it, in that regard.

A No, I am not.

Q Have you, however, in the course of the various traffic studies in which you have participated worked with a statistician toward developing a representative sample of traffic to study?

A Yes.

Q And are you familiar with the steps which you were required to take and the information which you were

required to provide that statistician to allow him to develop the representative sample?

A Yes.

Q From your knowledge of the manner in which the primary applicants selected the movements -- would you refer to the movements contained in the work papers? Were their activities consistent with what your activities would have been had you been working with the statistician to select a representative sample?

A I didn't find anything in the work papers that indicated they followed the same types of procedures we would.

Q Now, Mr. Wilson asked you a question with regard to routing conditions via Dallas. I guess protective conditions is what we would call it. And I am going to ask you this question.

Would KCS be willing to accept and consider itself adequately protected should the applicants be allowed to merge with traffic protective conditions requiring them to maintain open the Big D gateway?

A No.

Q Could you explain why not?

A Simply because just having protection for a route still does not give you adequate protection by virtue of the fact that if you are dealing with certain

types of traffic such as TOFC or other types of traffic, non-TOFC traffic, if you don't have the same routing capabilities as your competitor, you would not have the capability of serving the shippers' needs.

And I mentioned not too long ago that we had already experienced this type of an operation where the Santa Fe has, prior to November, I believe, has been operating with us on the Big D runthrough, and the Big D runthrough is characteristic of single line service.

We have an equipment pool established by the Santa Fe and the SP that runs between Shreveport and Brownwood and allows the trains to be handled on a runthrough basis. After leaving Brownwood, they are off towards -- to the California shores.

Since November -- well, I don't recall the specific date, but since November, anyway, they have notified us that they no longer will accept our Train 54 and run it through on their Train 579 at this point, and also Train 54, which was our expedited service train, was limited to only TOFC traffic.

Therefore we no longer have a Big D runthrough train operation over Dallas on westbound traffic. Now, what that means to us is, there is going to be a downgrading of schedules, a downgrading of service to the point where we may not be in competition, be

competitive with the Southern Pacific any more. It is kind of like a self-fulfilling prophesy.

Q One question. You said that 54 was confined to TOFC traffic. Do you mean was prior to November, after --

MR. WILSON: Your Honor, I object to this question. This is way beyond the scope of my cross examination. It is a new subject KCS is introducing here.

JUDGE HOPKINS: You are going beyond.

MR. DREILING: I think, Your Honor, it is within the scope. Mr. Wilson inquired a great deal on the question of route closings.

JUDGE HOPKINS: As of this point, but now you are going far beyond what he was questioning about.

MR. DREILING: Then I will withdraw the last question.

JUDGE HOPKINS: Thank you.

MR. DREILING: With that, I have no further questions.

JUDGE HOPKINS: Anything further?

MR. WILSON: I have one question now in light of this new subject you brought up.

RECROSS EXAMINATION

BY MR. WILSON:

Q Were you informed that the reason why the train operations had been modified at Dallas was a lack of business?

A The only thing that I am aware of is, we received notification one day that the service was changing without any identification of reasons for the changes.

MR. WILSON: Okay. Thank you. That is all.

JUDGE HOPKINS: That is all?

MR. DREILING: Your Honor, I offer Mr. Plath's three verified statements, KCS-12, KCS-14, and KCS-15 as corrected and KCS-16 and 18 into evidence.

JUDGE HOPKINS: Any objection?

(No response.)

JUDGE HOPKINS: They will be received in evidence.

JUDGE HOPKINS: You are excused. Thank you.

(Witness excused.)

MR. WILSON: Your Honor, I move admission of Exhibits SPSF-C-99 and C-100.

JUDGE HOPKINS: Any objection?

MR. DREILING: No.

JUDGE HOPKINS: They will be received in evidence.

(The documents referred to,

previously marked for identification as Exhibits Number SPSF-C-99 and 100, were received in evidence.)

JUDGE HOPKINS: The next witness?

Whereupon,

OTIS C. BURGE

was called as a witness, and having been first duly sworn, took the stand, and was examined and testified as follows:

DIRECT EXAMINATION

BY MR. DREILING:

Q Mr. Burge, would you state your name for the record?

A My name is Otis Burge. I am the assistant vice president of operations of the Kansas City Southern.

Q Have you prepared and submitted a verified statement in this proceeding on behalf of KCS in KCS-14?

A I have.

Q And do you have that statement in front of you?

A Yes, I do.

Q Do you have any corrections which you wish to

make to that statement?

A Yes, I do.

Q Would you tell us what that correction is?

A Page 3, Line 10 from the top, the word "Barstow," the third word from the left, should be changed to "Brownwood."

Q Do you have any further changes or corrections?

A Yes. Page 9, the fourth line from the bottom, where it says "average daily train" should be "average cars per train."

In the appendixes, Appendix A, Page 1 of 6, in the caption of each of those bar graphs the word "daily" should be changed to "train average."

That is all the corrections I have.

Q With those corrections, does this constitute your testimony?

A It does.

Q Are the facts therein stated true and correct to the best of your knowledge and belief?

A Yes, they are.

MR. DREILING: With that I offer Mr. Burges' testimony in KCS-14 as corrected.

MR. MOATES: No objection.

JUDGE HOPKINS: It will be received in

evidence.

Thank you very much.

(Witness excused.)

MR. RAKER: Your Honor, KCS calls Hilary Rawert.

Whereupon,

HILARY RAWERT

was called as a witness, and having been first duly sworn, took the stand, and was examined and testified as follows:

DIRECT EXAMINATION

BY MR. RAKER:

Q Mr. Rawert, have you filed a verified statement in these proceedings which is contained in KCS-12?

A Yes, sir.

Q And is that the verified statement which bears your verification dated September 6th, 12984?

A Yes, sir.

Q You also submitted errata to that verified statement, which errata are set forth in KCS-16 and in KCS-18?

A Yes, sir.

Q Have you any further corrections or other modifications which you wish to make at this time in

your verified statement?

A Yes, sir. At Page 7, under Item 1, that should read "from the per diem and mileage rates as contained on the sample study records."

Q Now, is this in the second line of Item 1 on that page?

A Yes, sir.

MR. MOATES: Would you repeat that, Mr. Rawert?

THE WITNESS: After the comma it should read, "from the per diem and mileage rates as contained on the sample study."

MR. MOATES: Are you meaning to delete the word "actual?"

THE WITNESS: Yes.

BY MR. RAKER: (Resuming)

Q So after the comma it reads what as corrected, Mr. Rawert?

A It should read "from the per diem and mileage rates as contained on the sample study records."

Q Anything else?

A No, sir.

Q As modified by the correction which you just made, and by the other corrections contained in KCS-16 and KCS-18, is your verified statement to the best of

your knowledge and belief true and correct?

A Yes, sir.

Q Do you adopt it as your testimony?

A Yes, sir.

MR. RAKER: That completes my direct examination, sir.

JUDGE HOPKINS: Thank you.

CROSS EXAMINATION

BY MR. MOATES:

Q Good afternoon, Mr. Rawert. My name is Moates, and I am attorney for one of the Applicants.

On page 2 of your testimony you indicate in the third full paragraph the purpose of this verified statement. I want to make sure what that is.

I take it there that the purpose is to do two things, to develop appropriate unit costs to be applied to the traffic that Mr. Ploth projected the Kansas City Southern would lose if this merger were approved, is that right? Is that task number one?

A Correct.

Q Task number two was to do the same thing, namely, to develop appropriate unit costs associated with traffic that he projected would be diverted in what we will call his gain studies, which I hope you and I will understand means the so-called recaptured traffic and the traffic from IRMA.

A Yes, sir, that's correct.

Q Now, you have, have you not, at pages 4 and 5 of your traffic, on Tables 1 and 2, summarized the results of your analyses for those two different tasks, haven't you?

A Yes, sir.

Q And you have changed the numbers in both of those tables twice in the last few weeks. I think Mr. Raker just referred to your first changes, were first on December 18, and you changed them again on January 8.

Let me ask you first of all, directing your attention to Table 1 on page 4, how is it, sir, in the most recent iteration of your changes -- I think I have got the right numbers, and if I misstate one, correct me because I went out of the room to write these things in there -- if I have the numbers right on the most recent change, you have indicated that you reduced the gross revenue gains on the IRMA traffic by about $3500, but at the same time you managed to reduce your expenses by about $1.8 million.

Can you explain to me how that phenomenon happens?

A Yes, sir. That was a result of the KCS gain study, as I recall, where we -- where only partial gains were going to be realized by KCS, and it involved really a reroute type analysis, and we had to go through and look at the old route and the new route after the merger and come up with the differences, and that was what resulted.

Q Well, how is it that you didn't discover these partial reroutes and the revenue effects of those

reroutes until January 8 or shortly before then?

A Well, sir, the timing in this whole study was very tight, and after our data was submitted, we reviewed and reviewed and reviewed, and several things came up, and we tried to get everything we possibly could corrected. It certainly wasn't intentional, I can assure you.

Q Now, let me make sure I understood again. You said this was a result of certain partial reroutes? Did I understand you?

A Well, it was in the Gains 2 study where it involves really a reroute analysis comparing an old route with a new route. It was partial, had to do with partial gains.

Q Well, again, recognizing that that is what it had to do with, what was it about those partial gains that resulted in your determining that there should be only $3500 in gross revenues added to the figure you had previously submitted, but that for some reason, these partial gains caused KCS to identify an additional $1.8 million of expenses with this traffic?

A What $3500 are you referring to?

Q I am referring to the difference between $90,956,016 and $90,959,564, which is the difference between your second and third errata.

A Now, that has to do with revenues, and that comes from Mr. Ploth. I developed the cost.

Q All right. Then let's look at the cost number.

The difference, you would agree with me, roughly between $86.9 million and $85.1 million, that is the $1.8 million I am referring to.

A Yes, sir.

Q Where did that come from?

A That, as I previously explained, was the difference in the cost from the present route and the proposed route. The first submission looked only at the new route.

Q I see. The first submission didn't look at the rerouting at all.

A No, sir.

Q I see.

Didn't you think it appropriate to draw that fact to the Commission and parties' attention when you filed that statement?

A We did as soon as we discovered it.

Q Oh, I don't mean that. I mean, would it have been appropriate to put in a footnote at least or something indicating that the number that you showed in Table 1 for expenses didn't contemplate or include any

reroutes, that you planned to look at that later?

A Well, I assumed this was all part of the gain study, and this is what you have to go through to come up with the gains.

Q Mr. Rawert, were you instructed by anyone at ACS involved in this project that it would be most helpful if the calculation of net revenues from the IRMA would show the IRMA would be profitable?

A No, sir.

Q Were you instructed that the IRMA, as Mr. Carter desired it to be implemented, would fully compensate SPSF for its out-of-pocket costs, and in addition, provide them a -- please note my fingers -- a small profit?

A Yes, sir, I think that is the policy.

Q When were you told that?

A Well, I heard it yesterday in the hearing room.

Q Is that the first time you heard it?

A Yes, sir.

Q Were you given any similar kinds of direction or instructions or policy guidance, if I can call it that, before you initiated these studies?

A No, sir, only that I had a general understanding of what the IRMA was.

Q Was there any discussion of which you are aware or in which you may have participated at any time about the desirability of the gains that KCS would show it would enjoy as a result of IRMA and trackage rights not exceeding the losses that you project that you would suffer as a result of the merger?

A I don't know that I understand that question.

Q Well, I thought it was clear, but let me try it again.

Are you aware of any discussions, or did you yourself participate in any discussions or receive any directions or give any directions, any of those possibilities, about the desirability of the net revenue effects of KCS's conditions, we will call them in this case, generating net revenues to you that would be greater than or less than the net revenue effects that you project would occur from diversions from KCS?

A No, sir, I had no such discussions.

Q All right.

By the way, a detail question.

On page 5 under Table 2, you note in the last sentence, "KCS's 1983 costs, and thus its avoidable costs, were significantly lower in 1983 than in 1982."

Do you see that?

A Right above Caption 2?

Q Right, are you with me?

A Yes, sir.

Q How did KCS's 1984 costs compare with its 1983 costs?

A I don't know how its 1984 cost compares with itse 1983 cost yet.

Q You don't have any idea?

A No, sir.

Q Now, just so the record is clear and to make sure my understanding is accurate, Table 2, Mr. Rawert, represents a restatement simply of Table 1, doesn't it, under some different assumptions?

A Yes, sir.

Q Specifically, Table 2 represents a restatement of the first column, the loss study, to reflect 1983 as the base year, and the effect of depreciation accounting?

A That is correct.

Q Have you made a calculation of the gross revenue-to-expense ratio, I will call it, that is associated with your restated loss traffic study?

A No, sir, but I recall it coming up in the hearing the other day, and I believe it was 1.22 percent.

Q Yes, sir, that's correct. Good memory.

And do you recall the same figure being discussed with respect to the gross revenue-to-expense ratio of the recapture of the gains study?

A Yes, sir.

Q And do you recall that number that was 107 or 1.07?

A Yes, sir.

Q Were you aware of those revenue-to-cost relationships before that testimony yesterday?

A Well, I didn't specifically look at them, but it appeared to be marginal to me.

Q Okay.

Now, I would like to go to page 6 and start discussing some of the adjustments you made here, but I think we ought to have -- a time out while you recover your papers.

(Pause)

All set, Mr. Rawert?

A Yes, we will try it again.

Q All right, sir, I was going to ask you a foundation question before I commence this line.

A Did you refer to a certain page?

Q Sure, I'm going to be asking you about the adjustments that start in your discussion on page 5 and go on through the loss study.

A All right, sir.

Q All I want to do as a foundation is to state for the record that you confirm for the record that for purposes of developing unit costs applicable to the Loss diversion study, that you in fact created a modified Kansas City Southern Rail Form A, is that right?

A Modified costs that were developed from Rail Form A.

Q Were developed from Rail Form A, all right, that's a better way to say it, okay.

And that modification or those modifications, I take it, are discussed at pages 6 through 10, correct?

A Yes, sir.

Q Okay.

Directing your attention first to page 6 --

A All right.

Q In the second, well, maybe it is the first full paragraph, the one in the middle of the page, it says "Thus KCS's '82 and '83 Rail Form A variable costs were adjusted to exclude all general overhead expenses, capital costs, and the remaining way and structure maintenance expenses other than roadway track maintenance" -- and you give the account numbers -- "which are avoidable."

A Yes, sir.

Q First of all, let's talk about the elimination of general overhead expenses.

Briefly, Mr. Rawert, what is included in general overhead?

A Well, essentially it is the cost of accounting and traffic.

Q Sometimes referred to as supervision and administration?

A Well, administration I think more than supervision.

Q All right.

And did you eliminate that item, general overhead expenses, for purposes of your constructing or adjusting these Rail Form A costs? Did you eliminate them 100 percent?

A Yes, sir.

Q Okay.

What percentage of total variable costs, roughly speaking, what percentage of total variable costs are represented by general overhead expenses?

A Well, I don't know exactly what it is, but I would guess it to be around 10 percent.

Q Around 10 percent, okay.

You were here yesterday for my examination of

Mr. Carter?

A Yes, sir.

Q Okay.

A Not for the entire cross, but I was here for part of it, yes.

Q Were you here for the portion where we discussed the -- Mr. Carter's plans or Kansas City Southern's plans for staffing IRMA territory with seven additional supervisors?

A Yes, sir.

Q Specifically how did you account for the cost of those seven or more supervisory people that will be added under IRMA?

A Well, my purpose was to develop costs for pro forma purposes, and I came up with the additional, the avoidable cost to be lost, and the additional cost to be gained.

Now, that part that you are speaking about that involves the seven supervisors Mr. Graf has included in his pro formas.

Q Do you know on what basis he has included those numbers?

What figures did he use for the cost of employing those people?

A I would suggest that you talk to Mr. Graf

about that. I am not real sure just what numbers he used and where they came from.

Q All right. Then I will skip this series of questions and we will visit them with Mr. Graf.

Let me ask you this question: what would happen to your expense -- strike that.

What would happen to your gross revenue-to-expenses ratio that we just discussed on page 5 if you had factored back in that roughly 10 percent for general overhead?

A Well, first of all, I wouldn't factor it back in.

Q I realize you don't want to do that.

A Well, it is not applicable because we are dealing with pro formas.

Now, what additional costs did KCS pick up as a result of these gains, or what did we lose as a result of the losses, now, we are not going to change any of our general overhead costs as a result of this, so why should I add anything or take anything away?

Q Is the answer to my question that you don't know what the effect would be if you had not eliminated general overhead expenses on the expense number shown in Table 2?

A Well, first of all, I don't think it is

appropriate.

Q I understand that, sir. I will accept your statement you don't think it is appropriate.

Now, I am asking you to assume that you, for whatever reason, or someone else, didn't eliminate general overhead and put it back in.

A What it would do to the cost?

Q What would it do to the expenses?

A I don't really know. I haven't done that.

Q The next exclusion about which you speak on page 6 relates to capital costs.

Do you see that?

A Yes, sir.

Q And I would like to direct your attention in this regard back to page 4 for a minute, in the middle paragraph where you explain that the Table 2 which reflects 1983 in depreciation accounting, as we agreed a minute ago, was in your words mandated by the Commission.

Do you see that reference?

A Yes, sir.

Q How do you know what the ICC mandated? Did you review the appropriate orders for the presentation of costs and expense evidence in this proceeding?

A Well, I think I mentioned what I reviewed in

the first part of my testimony. It is on page 6. That is what I have reference to, and -- well, I'm sorry. That is not it.

Would you restate the question again, please?

Q Yes. I wanted to know whether that reference on page 4 was a suggestion to me that you had reviewed the various orders that the Commission has entered in these proceedings directing participants to do certain things in terms of how they state expenses and costs.

A This was what I was advised to do by counsel.

Q Did you yourself review any of these orders?

A I did review a two-page or three-page article at one time, yes, sir.

Q An article?

A Or a decision.

MR. MOATES: Your Honor, I would like to show the witness a couple of ICC orders. I don't think it is necessary to mark them. We have copies for counsel and Your Honor. These are decisions in this docket, and specifically Decisions 4 and 5.

The first decision was served February 28, 1984. Decision 5 was March 20, 1984.

BY MR. MOATES: (Resuming)

Q Mr. Rawert, on the first one, if you would turn to page 4, I think that is what we want to direct

our attention to. We are going to look at page 4 of the first decision and pages 2 and 3 of the second one.

Okay, let's look at the first decision, if we could, on page 4, in the top full paragraph. For context, I will just state this is under the heading that starts at the bottom of page 3 called Costs, which is underscored. It is a discussion of costing methodology that the Commission wanted the Applicants to apply in the proceeding.

A Yes, sir, I have read this.

Q You have read this, okay.

A Yes.

Q Well, let's just revisit for context some of the language here.

A All right.

Q Now, let me ask you first, when did you review this?

A Oh, I read this back in June or July or sometime. I don't recall just when, but I did read it.

Q Before you conducted the studies that we are discussing here?

A Yes, sir.

Q Okay.

On page 4 in that first full paragraph, it must be about two or three sentences from the end, the

sentence starts as follows: "Additionally, Applicants' variable costs should be adjusted to reflect return on road and equipment property at the current before-tax cost of capital level. This includes both existing plant and equipment and any new plant or equipment required as a result of the consolidation. Variable costs include cost of capital at the imbedded debt rate. Therefore, it will be necessary to adjust variable costs to reflect the current cost of capital."

And again, a similar kind of comment at the bottom of this page, the Commission says "Once Applicants have identified shipments as being divertible to their lines, the variable costs associated with the handling of each shipment or aggregates should be calculated. This would include variable expenses as well as the return on road and equipment property at the current pretax cost of capital."

Now, so you say you reviewed this decision. Did you also review the Applicants' petition to this Commission following this decision seeking a waiver of clarification?

A Yes, sir, I did, but what I used was primarily based on Footnote 2 here, and if you will read this, it says "This is not necessary to the case, however, for Protestants. While this may be true for the Applicants,

the Protestants don't have time in a three-year period to adjust for" -- merger type -- "for post-merger operations as the Applicant would do." And consequently the Commission suggested that we look at this analysis on an avoidable or direct variable cost approach, as I understand it.

Q Well, it is that understanding that I am driving towards, Mr. Rawert.

A Well, I tried to follow the Commission's guidelines.

Q I am trying to see if you did.

Did you review Decision No. 5 that was served on March 20 in response to the Applicants' waiver petition that you have just said you saw?

A Well, it has been some time ago, but yes, I did see it.

Q And again, you saw all these documents we are referring to before you commenced the study?

A Yes, sir, I did.

Q All right. Would you look at this decision at the bottom of page 2, "The Commission has allowed the applicants in this decision to use 1982 and government accounting, essentially because they had already done their studies that way."

But then the Commission also says this: "Although we have replaced the RRB accounting system with depreciation accounting, we will allow RRB to be used in the initial applicants' cost and financial data. We will require that protestants' opposition evidence to the initial application use the same accounting system elected by the applicant."

All right. Then I'm going to skip the next sentence or two, turn the page. The Commission says, "However, in filing and supporting any responsive applications, protestants should use 1983 as the base year and use depreciation accounting."

A Yes, sir.

Q Those are the directions that you say you followed here on page 4.

Now, my question is did the Commission in its decision number 5 do anything to modify what it said in decision number 4 about the use of the current cost of capital?

A Well, I think for the applicants the

Commission was making that direction. I don't necessarily think they had reference to that to the protestants.

Q That's your interpretation of these orders?

A Yes, sir, that's my understanding.

Q Did you consult with counsel at the time to make sure that your understanding was correct?

A I don't recall as to whether I discussed it specifically with counsel, but I think we had several discussions.

Q It is true, is it not, Mr. Rawert, that throughout your studies here that when you deal with cost of capital, you use cost of capital at the embedded debt level; isn't that right?

A That is correct.

Q You do not state it in terms of current cost capital?

A No, sir, I do not.

Q Have you at any point, sir, done an analysis for yourself, for your own purposes or for KCS purposes, that created an adjusted Rail Form A that did use the current cost of capital?

A Have I ever developed or worked a Rail Form A that uses the current cost of capital?

Q No. My question wouldn't have caused you to

answer that. Let me restate the question therefore.

Have you, for purposes of this case or for purposes of understanding the impacts of this merger on your company, either done personally or at someone's direction a modified Rail Form A that would be just like the one you have discussed here, with the exception that you used current cost of capital rather than embedded debt levels for capital costs?

A Yes, sir. We do that as a matter of year to year cost development.

Q I think you still may not be getting my question. I'm not asking you what you do for your own internal business purposes. I'm asking whether you did one, whether you made a modified -- let me see if I can do it this way. Look at page 6.

A Look at page?

Q Page 6 of your statement. The paragraph in which this discussion is proceeding is the one that starts, "Thus, KCS' '82" and so on. Do you see that?

A Yes, sir.

Q You say your '82 and '83 Rail Form A variable costs were adjusted to exclude the second thing, capital costs.

A Yes, sir.

Q All right. And those were capital costs

stated at what level?

A At the embedded debt level.

Q Okay. And just so we don't go through this again, when you later created SPSF Rail Form A for other purposes that we're going to come to, you stated those capital costs as the embedded debt level, too, didn't you?

A That's correct.

Q Okay. Now, with respect to these capital cost items --

A Yes, sir.

Q -- my question is specifically have you done, for your own purpose or because someone in the company instructed you, have you done these same kinds of analyses using current cost of capital rather than embedded debt?

A No, sir.

Q Do you have any idea what the effect on your Table 2 expense numbers would be if you used the current cost of capital?

A I don't think that the current cost of capital is applicable for Table 2.

Q Do you have any idea what the effect would be on the pro forma effects of the transaction as stated by Mr. Graf if you used the current cost of capital?

A No, sir. I don't have any idea.

Q All right. Then the last set of exclusions that you discuss on page 6, and again for context, exclusions from the KCS Rail Form A that you used in the loss study, is in the category way and structure maintenance expenses other than roadway-track maintenance in accounts 202 through 221?

A Yes, sir.

Q That category of way and structure maintenance expenses, does that not account for such items -- and this isn't meant to be inclusive, just examples -- as maintenance of station and office buildings?

A No, sir.

Q No?

A That's rails, ties, ballast, other track material, track-related accounts.

Q All right.

A What I'm excluding is just what you mentioned, those types of costs which won't change, at least for a short period of time.

Q Okay.

A So for pro forma purposes, there was no need for me to add those costs, in my judgment.

Q All right. Recognizing, then, that they are expenses of the type you just stated, did you

reincorporate those expenses in the SPSF Rail Form A, which you created for purposes of expensing the IRMA gain?

A Yes, sir. I costed the SPSF IRMA-type traffic at the variable level exclusive of general overhead but including 100 percent cost of capital at the embedded debt level.

Q All right. Recognizing your answer before that one, why you thought it was appropriate to exclude this at this point, if any IRMA traffic actually turned out to be incremental in nature as opposed to simply a substitution of KCS for applicants, wouldn't some of SPSF's expenses in that category be increased as a result?

A I don't know that I understand your question.

Q Did you hear my examination of Mr. Carter yesterday about whether IRMA traffic would be incremental?

A No, I didn't hear that.

Q Well, let's pass over the question. On page 7 now I want to ask you about some of the specifics where you have summarized the expense unit cost items that you adjusted here.

First, with respect to car hire costs -- this is in the paragraph where you made the correction.

A Yes, sir.

Q Okay. The last sentence in that paragraph says, "Mileage rates were multiplied by the loaded and empty car miles generated by each sample car."

A Yes, sir.

Q The question, Mr. Rawert, did you use the mileage rates applicable to particular cars for all car types?

A Yes, sir.

Q Did you use the rate applicable regardless of car ownership; that is to say, whether it was a railroad car or a private car?

A We distinguished between railroad and private cars, yes, sir.

Q You distinguished between them.

A Yes, sir.

Q Did you apply this -- these rates to both loaded and empty cars?

A To both the loaded and empty miles, yes, sir.

Q Why did you distinguish between railroad-owned and private cars?

A Well, because -- well, when I say I applied it to loaded and empty miles, there are some private tank cars that would involve a one-way type loaded per car mile charge.

Q It's true, isn't it, that for private cars that the mileage rate only applies to the loaded movement?

A That is correct.

Q Okay. In your judgment, you appropriately took account of that factor in your adjustment?

A Yes, sir.

Q Okay. Isn't it also a fact that the TOFC rates in the UMLER file are for maximum costs associated with the minimum utilization of the equipment?

A Would you please restate the question?

Q Yes. Isn't it also a fact that the TOFC rates that are in the UMLER file for 1982 are rates for maximum costs associated with the minimum utilization of the trailer?

A Are you talking about the car or the trailer?

Q I think we're talking here about cars. I misspoke. Cars.

A Oh, okay. I don't know that that would be the case.

Q Is it then a fact that you applied this UMLER number without any adjustment to TOFC flatcars?

A What do you mean by adjustment? Whatever was contained --

Q Whatever was in there you used?

A In the sample study record, whatever car hire rate was there, that's what we used.

Q Now, under switching costs you indicate that with respect to inter/intra train switching, you included one I&I switch for each 500 miles of movement. Do you see that?

A That's correct.

Q What was the basis for your using the 500 miles?

A Well, it was a judgment that we had to make when we began the studies, and in connection with the loss studies, a lot of the Big D type traffic moved between New Orleans and Dallas with a stopover at Shreveport which would require one intertrain switch, so that would be approximately one switch every 520 miles.

And on other situations we looked at Kansas City to Beaumont, where there would be absolutely no intertrain switches. So we looked at many areas and made the judgment to use the 500 miles, and then later developed a study whereby we justified the use of the 500 miles. But it was a judgment. We had to make a judgment to do the loss study.

Q Tell me about the study you did later on.

A Well, we looked at all loss study records and all gain study records and determined one switch every

486 miles.

Q Did you ever do a study just for the loss records?

A No, sir. I think it was a combined look.

Q Is that study in your work papers? I don't remember seeing it.

A I don't know if it is or it isn't.

MR. MOATES: I would request, counsel, that study be produced.

MR. RAKER: Absolutely.

BY MR. MOATES: (Resuming)

Q Isn't it true, Mr. Rawert, that the number used for Rail Form A for I&I switching is 200 miles?

A That is correct.

Q Do you know what the Kansas City Southern system average is for frequency of I&I switching?

A What the --

Q How often, your system average for I&I switching.

A I would say the 500 miles is a good average.

Q Do you know what percentage of the lost cars in the loss KCS study were from traffic moving in the Big D connection trains from Dallas to New Orleans? And, since you've mentioned it, in trains from Kansas City to Beaumont?

A No, sir, I don't know specifically.

Q Now, with respect to the category of gross ton mile related costs --

A Yes, sir.

Q -- were these costs created or identified for average way or through train characteristics?

A This is for the average train.

Q Average train. Doesn't that number for average trains, then, include unit trains?

A Yes, sir. It includes unit trains, way trains, through trains and all trains.

Q And KCS does have unit train service, doesn't it; for example, coal trains, sulfur trains as two examples?

A That is correct.

Q Did you make any adjustment at all to this figure to reflect the presence of those unit trains?

A No, sir. I used the system average, which is the average train.

Q Turn the page, please. On page 8 under item 7, station clerical, do you know whether there were any multiple car movements in the sample that you studied in this loss study?

A No, sir, I do not know that. And --

Q If there had been, wouldn't that have required

appropriate adjustments to station clerical expenses?

A Well, it could have, yes.

Q Also on that page you discuss loss and damage payments. You indicate there, sir, that the loss and damage expenses per net ton mile were calculated from your records by a two-digit STCC. Isn't a two-digit STCC a rather high level of aggregation for considering loss and damage costs?

A I don't think so.

Q Well, as an example --

A All we have to go by is KCS experience.

Q At the two-digit level, Mr. Rawert, wouldn't you, as an example, get set-up automobiles and auto parts in the same STCC code?

A I don't know exactly all that goes into that, but you would have a more generalized --

Q Assume for the sake of my question that is true, that you're getting set-up autos and parts in the same STCC. Is it the experience of Kansas City Southern that your loss and damage claims on those two types of traffic are about the same?

A Well, both would carry probably a pretty high loss and damage.

Q My question was not whether they both were pretty high but whether they're anywhere near the same.

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A I don't know. I would guess they might be.

Q Isn't loss and damage a lot higher on set-up autos than it is on parts?

A I really can't say.

Q Would you look at your Attachments C and I, which I think are exhibits that show KCS loss and damage for 1982 on Attachment C, and the same thing for 1983 on Attachment I. Do you have those two there in a way you can sort of flip back and forth? I just want to look at a few of the numbers.

A Yes, sir.

Q You could almost pick any numbers at random. Let's just pick the first one. In 1982 for STCC 01 at the two-digit level, loss and damage -- what is NTM, by the way?

A Net ton mile.

Q The loss and damage per net ton mile was -- well, it was what it was, .000209. Let's just refer to the real numbers here. It was 209, and in 1983 it was only 47, as an example. And then I see that in STCCs 8 and 9 in '82, which were 7u, in '83 you show them as 0. And then STCC 21 in '82 was 3352, and then in '83 it's 8073.

There are other examples. I don't want to burden the record with all of these, but it seems to me

estimate of that.

Q Okay. Before we leave the recapture -- excuse me -- the loss study altogether -- well, let's leave it. Let's go to page 10 where you start your Roman heading III which deals with the costs developed for the gain study.

Now, here -- and I think we referred to this earlier -- here you did create an SPSF Rail Form A, did you not, Mr. Rawert?

A Yes, sir.

Q What source documents did you use to create that Rail Form A?

A Your R-1s.

Q Who's "you?"

A The SP's, the Santa Fe's and the Cotton Belt.

Q And the Cotton Belt's.

Now, we noted in your work papers you do have a Rail Form A input and output printout. Are you familiar with that?

A Yes.

Q It relates specifically to the SPSF Rail Form A we're talking about.

A Yes. We had -- in fact, I think we furnished you with a copy of that.

Q I think you did. That printout is numbered

sequentially pages 1 to 17 and 19 to 35. We appear not to have been provided pages 18 and 36. Do you know what would be on those pages?

A No, sir. You should have gotten a copy.

Q We didn't. We would request those pages.

A Pages?

Q Eighteen and 36.

A Eighteen and 36?

Q Yes, sir.

Would it be possible, Mr. Ravert, that those would be reconciliation pages?

A Could be.

Q Do you remember if the numbers reconciled in this study?

A I don't know. I think they did, but I'd have to check into the work papers.

MR. MOATES: In any event, you're willing to give us those pages?

MR. RAKER: Yes, sir.

Q When you created the SPSF Rail Form A which we are now discussing, did you eliminate interchanges between SP, Cotton Belt and Santa Fe?

A No, sir, there's no way we had access to that kind of data. We had to use what was available, and we did try to request that from the Santa Fe and the SP and they couldn't get them for us or they didn't have them developed. I don't know what was the case.

Had we had your information, we would have used that.

Q You would agree with me, understanding your problem, you would agree with me, Mr. Rawert, that the SFSF system wouldn't have interchanges between those three railroads that I mentioned, would it?

A No, I don't know if I would or not.

Q You don't know if you would?

A You still are going to have to -- you're not going to interchange the traffic? After your merger it's just going to be one railroad, is that what you're saying?

Q What is your understanding about that? Is it your understanding that this transaction to which your evidence responds is an application for authority for SFSP to control SP, SF, and SSW? Or do you understand this to be a merger case?

A It's to be a merger case.

Q And one railroad will result, correct?

A Right.

Q And then on that one question there won't be any more SP and there won't be any more Cotton Belt and there won't be any more Santa Fe, right?

A That's true.

Q I guess it's just as true, then, that if they don't exist they're not going to be exchanging traffic with each other, isn't it?

A Well, I guess you can make that assumption.

Q But you didn't?

A I used whatever records were available to us, in the absence of your furnishing them to me.

Q Would you look at your attachment K. Better yet, turn to the cover page. We can't look at it because it's one of these printouts, but let's turn to it. This is the table of estimated charges that KCS proposes to pay SPSF. It says loaded movements, right?

A Yes, sir. You'll see one of these for both loaded and empty movements, and it's a demonstration, so to speak, as to how such charges could be developed. They're in no way to set the actual IRMA charges if the Commission approves this merger.

Q In fact, I think you say a couple of times in

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your testimony that those charges would ultimately reflect the most current SPSF unit cost, don't you?

A Yes, sir. Probably if they approved it we'd sit down and negotiate such charges.

Q Okay. I'm not going to walk you through all the car types here. Neither you nor I have the patience for it, and I know the Judge doesn't. But I want to ask you about one car type as an example. If you would turn to the second page of the exhibit, this is a list, as all these are, in mileage categories from 50 miles to 2200 miles of railroad-owned plain 50-foot boxcars, correct? Are you with me on that?

A Well, I want to find the 50-foot box. I've got it.

Q I'd give you a page number, but they're all numbered page 1, so I can't.

A Sorry about that.

Q Are you with me?

A Yes, sir.

Q All right. Would you look at the interline, received interline forwarded columns, and just confirm for me what I think is fairly evident, namely that there is about, in rough terms, about a ten dollar per car difference as between the two traffic categories?

A Yes, sir.

Q All right. Then kind of keeping that in mind or holding your hand there or whatever, turn, I think it's the eleventh following page, which will give you, if I've done this right, the comparable exhibit for private line 50-foot plain boxcars.

If there was something on the page I could give you to identify it, I would, but I don't think there is.

A Okay.

Q Are you with me?

A Uh-hmm.

Q And just look there at the first category of 50 miles or, for that matter, down the list. The numbers are the same in those categories, aren't they?

A Yes, sir.

Q What explains the difference or the variability between the projected charges for private equipment versus railroad-owned equipment, Mr. Bawert?

A Well, the railroad-owned equipment, the forwarded traffic has train supplies and expenses in it, whereas the private car does not.

Q Okay. And is it true that train supplies and expenses, that a major portion of them -- excuse me. You said train supplies and expenses, right?

A Terminal train supplies.

Q That's right, terminal. TSE we call it, right?

A Yes, sir.

Q Is it true that a major component of that expense is car cleaning costs?

A I'm not sure whether it's major, but it certainly is a portion.

Q Do you have any idea at all what percentage of it is attributable to the cost of cleaning cars?

A No, sir.

Incidentally, that's your number, too.

Q What's that?

A That we developed.

Q Oh, what do you mean, it's our number?

A Well, it was a figure, something like nine or ten dollars, which seemed pretty high to me as I was reviewing it. But that's the way it developed.

Q Would you agree with me, sir, that one does not clean tankcars typically?

A You mean the railroad?

Q I mean --

A Tankcars would have to be cleaned.

Q Between movements?

A I don't know. I'm just thinking out loud. Tankcars have to be cleaned as well as any other car.

Q Aren't tankcars -- first of all, tankcars are normally owned by shippers, aren't they?

A That's right.

Q And aren't those shipper-owned tankcars usually used, normally used in a particular type of service, for example petroleum or vegetable oil or whatever it might be?

A Uh-hmm.

Q You don't typically shift a car hauling petroleum to the next load being vegetable oil, do you?

A I don't which?

Q You don't typically shift a car that just hauled a load of petroleum to carrying a load of vegetable oil the next time out, do you?

A Well, I wouldn't think so, no, sir.

Q Aren't those cars normally in something like dedicated service, at least dedicated to a particular type of commodity?

A Yes, sir.

Q So you don't clean them very often, if ever?

A Probably not.

Q You don't clean multi-level flatcars very often, do you?

A No, sir. But keep in mind that when you deal with a formula you're costing accordingly.

Q When you deal with a formula, that's the problem with the formula, that sometimes it causes you to do things that maybe don't reflect reality, isn't that it?

MR. RAKER: Mr. Moates, we're willing to stipulate we reduce the charge.

MR. MOATES: That's not necessary, counsel. I'm exploring something else.

THE WITNESS: These tables are not meant to set the charge. This is meant to demonstrate how it could work.

BY MR. MOATES: (Resuming)

Q Would you look at your attachment F. I just want to clarify what I think you've already suggested. Under terminal costs, you have a line item, "terminal TS&E per car origin or destination," and it's about $9.36, isn't it?

A Yes, sir.

Q That's pretty close to the differential we've been talking about, isn't it?

A Yes, sir.

Q Would you turn back to page 10, please. The first -- excuse me. The last paragraph on the page you say in the second sentence: "In connection with this operation under IRMA and the proposed trackage rights,

KCS contemplates no additional purchases of locomotives or freight cars and no significant increase in capital costs."

A Yes, sir.

Q Won't KCS need additional power to operate the trackage rights segments for which it seeks authority here, such as Houston and New Orleans?

A No, sir. Mr. Carter I think explained that, but we'll have to purchase no new locomotives or freight cars.

Q Even though you're going to be operating at greater distances?

A Even though we will be operating greater distances.

Q Okay. I guess that's what you can do when you're a lean little railroad.

Now, would you look -- ah, on page 11 -- now, you created yet another modified Rail Form A for the purposes of determining expenses associated with the trackage rights, did you not?

A Well, we took the Form A's and developed the trackage rights charges, yes, sir.

Q Okay. But it was a different Form A. It wasn't the KCS Form A you used for the loss study and it wasn't the SPSF Form A that you used for the IRMA,

right?

A No, we developed also an SP Rail Form A and a Cotton Belt Rail Form A.

Q Right, okay. Let's look at attachment G just quickly, because I think that shows -- attachment G, page 1, shows your SP Rail Form A, and page 2 is the SSW Rail Form A. And at the bottom of page 1 of the exhibit you do give us a number.

A Yes, sir.

Q The number is 12 cents a car-mile loaded or empty?

A Yes, sir.

Q Why do you keep using the different configurations of the Rail Form A, Mr. Rawert? Why didn't you use your SPSF Rail Form A for the trackage rights?

A Well, because I thought this would be, since it was SP trackage rights and Cotton Belt trackage rights that we were talking about, that this would make a little more specific cost application.

Q Isn't it true that SP unit costs are lower than SPSF unit costs?

A I don't know. I don't recall that.

Q You didn't make that analysis?

A Well, I just can't recall the two sets of unit

costs.

Q Did you ever do the comparable calculations?

A I would probably say that the SP could be higher than the combined.

Q You say?

A So far as trackage rights, if that's what your question is.

Q Repeat that last question?

A I'd say that the trackage rights on the SP, the development of that could be higher than the ertire SPSF. I don't know.

Q Or the SP costs could be lower than those of the SPSF?

A I doubt that.

Q You doubt that?

A Uh-hmm.

Q Did you ever do this computation to determine the appropriate trackage rights rental using your SPSF Rail Form A that you created for the IRMA?

A No, sir, I haven't done that as a specific item. That's more of a different operational requirement than is the trackage rights, than are the trackage rights.

Q But as we have already discussed and as you say in your statement a couple of times, this all being

illustrative of the actual unit costs that will be relevant when it gets around time to proposing an IRMA charge, if that day ever comes, will be the then existing SPSF unit charges, correct? Unit costs.

A For all -- it could be conceivably for all of them, and certainly for the IRMA.

Q But it will be the SPSF and not the SP and not the SSW?

A That's probably true.

Q On page 13, the second full paragraph, you say that you didn't use the SP's actual rate of return, thank God, in calculating -- in calculating from the standpoint of the trackage rights tenant an appropriate investment in equipment. Rather, you used 5.99 for SP's net investment in road property and 9.82 percent for its investment in equipment, is that right?

A Yes, sir.

Q Is that because you thought that using the actual rate of return for 1983 would, to put it mildly, have created a somewhat unfair result?

A Created an unfair result?

Q If you had used --

A I used that because I thought it to be appropriate.

Q Why? Why was it more appropriate than using

the actual rate of return of SP?

A Well, there was a wide divergent set of rules going on that the Commission had with the UP-MP case, and not realizing how that was going to turn out, I decided to use what the embedded interest rates were on the outstanding debt, applying it to the SP's net investment base.

Q By the way, I'm kind of curious. How did you manage to apply SP's net investment values to SPSF?

A The net investments are contained in your R-1's, and you merely add them up.

Q Yes, but wouldn't you really had have to have created a composite SP-SSW, ATSF investment number, rather than just using SP's and applying that to the SPSF?

A Well, I did that for the SPSF. I also did it individually for the SP and the Cotton Belt.

Q You did do it for the Santa Fe?

A I did it for a combination and I did it for the SP and I did it for the Cotton Belt.

Q Okay. On page 14 you again refer to the capital cost of the embedded debt level that you used for SPSF Rail Form A. Do you see that?

A Yes, sir. At the bottom of page 14?

Q Well, it's in the paragraph that says "capital

costs."

A I'm sorry. Item 2.

Q Yes. Do you see that?

A Yes, sir.

Q Do you agree with KCS witness Levin, who says that railroads must earn revenues substantially in excess of variable costs in order to remain viable in the long run, and that without an adequate contribution to fixed or joint costs, railroads cannot generate the funds sufficient to replace, maintain and improve their capital assets?

A I would agree with that.

Q Do you agree with Mr. Carter's statement yesterday that he believes it appropriate under IRMA that the Applicants be made whole and also receive a little profit?

A I agree with that.

Q Let the record show it's pretty little.

(Laughter.)

JUDGE HOPKINS: Excuse me a minute, Mr. Moates. Are there many more?

MR. MOATES: I'd say five minutes.

JUDGE HOPKINS: Go ahead, then.

BY MR. MOATES: (Resuming)

Q Having in mind your agreement with Professor

Levin and your agreement with Mr. Carter, is it your belief as a cost expert that the railroad, the Southern Pacific-Santa Fe Railroad, will be indeed fairly and fully compensated by determining an IRMA charge that is based on the embedded cost of capital, as opposed to current cost of capital?

A Yes, sir, I do feel that the costs that I have developed are a pretty accurate reflection of what should be included. But that's negotiable at some time later. This was done for costing and pro forma purposes.

Q This isn't a fair question, but I'll ask it anyway. If you were doing these calculations for the Southern Pacific-Santa Fe, would you have done them with the embedded debt level?

A Well, I'm not doing them for the Southern Pacific and the Santa Fe.

Q Good answer.

(Laughter.)

Q All right, almost finished.

On page 15 -- oh, one quick question on the footnote on 14. You note there, as you started to say a minute ago, that the Commission's decision in the UP -- with respect to the UP valuation matter came out just before you filed this testimony, and therefore,

according to the footnote, if you had had that earlier you would have developed the costs in accordance with the methodology set forth by the Commission.

A Yes, sir.

Q Does Kansas City Southern to your knowledge plan to revise this submission that you did in its rebuttal case to reflect those changes?

A We certainly would like to do such a study, but we'd have to request a good deal of information from the SPSF in order to come up with a contribution on the revenues and expenses by segment. And I think that definitely would have to be done, and that would involve a whole -- a good deal of interrogatories. But we'd be happy to.

Q That's one of the reasons I'm asking the question. All right.

On page 15, the same question, just to make this quick now. On switching costs, you say one I&I switch every 800 miles was used for our sample cars and one every 500 miles for your sample cars. Would your answers be the same about the basis on which you derive the 500 miles here as we discussed previously?

A Yes, sir.

Q Also, is this also for a composite created for an average train, as opposed to a way or through train?

A This would be for the average train, yes, sir.

Q Lastly, at the bottom of page 17 under "purchases and rentals." I simply want to ask you with respect to the items that you list there, did you -- were you the person responsible for deriving any of the expenses associated with any of those acquisitions and purchases?

A No, sir. That would be Mr. Graf.

Q Do you know how those properties were valued?

A No, sir, I do not.

MR. MOATES: Thank you, Mr. Rawert.

JUDGE HOPKINS: Any redirect?

MR. RAKER: I have a few questions, which I'm happy to do now.

JUDGE HOPKINS: Go ahead. We might as well finish with this witness at one time.

REDIRECT EXAMINATION

BY MR. RAKER:

Q Mr. Rawert, I think there may have been a failure of communication between you and Mr. Moates at the very outset of his examination of you and I'd like to try to clarify the record on that. He asked you about your most recent errata, do you recall that?

A Yes, sir.

Q He spoke with you about the substantial reduction in the amount of expenses that was reflected in the most recent errata.

A Yes, sir.

Q And I think you said that what was involved was a reroute of traffic; is that correct?

A Well, it was gained traffic that received an extended haul, so to speak, on KCS.

Q Now, were the gains from that traffic included in your statement as it was initially presented in KCS-12?

A It was included at the new routes, so to speak, so I had to go back through and determine what the whole route was to see the difference.

Q But as you initially submitted the initial form of your testimony, it included, it reflected, the gains from that traffic; is that correct?

A That's correct.

Q And did it also reflect the costs attributable to the extended or the reroute portion of the extended movement?

A Yes, sir, it did.

Q And did it also include, erroneously, the costs that had been attributed to the former movement of that traffic before it was rerouted?

A No. I think it included only the extended haul or the long haul at first, and we had to go back and look at the differentials. Whereas we looked at it just one way in the original submission, we had to go back and compare it both ways afterwards and come up with a reduction.

Q And that is the correction that resulted in your final errata; is that correct?

A That's correct.

MR. RAKER: Thank you. I don't have any further questions.

JUDGE HOPKINS: Any further questions?

RECROSS EXAMINATION

BY MR. MOATES:

Q One simple one. Is that explanation another way of saying you did some double counting the first time?

A No, sir.

MR. MOATES: Thank you.

MR. RAKER: Your Honor, we move the admission of Mr. Rawert's verified statement as amended.

MR. MOATES: No objection.

JUDGE HOPKINS: It will be received in evidence.

You're excused, sir.

(Witness excused.)

JUDGE HOPKINS: Let's take a 15-minute recess.

(Recess.)

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JUDGE HOPKINS: Let's get back on the record.

MR. BAKER: Your Honor, KCS calls Donald L. Graf.

Whereupon,

DONALD L. GRAF

was called as a witness, and having been first duly sworn, took the stand, and was examined and testified as follows:

DIRECT EXAMINATION

BY MR. BAKER:

Q Mr. Graf, have you submitted two verified statements in these proceedings?

A Yes, I have.

Q And is one of them a verified statement which is contained in KCS-12 and bears your verification dated September 5, 1984?

A Yes, it does.

Q And have you submitted corrections to that verified statement which are contained in KCS-16 and then subsequent corrections which are contained in KCS-18?

A Yes, I have.

Q Do you have any further corrections or other modifications which you wish to make at this time?

A No, I do not.

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Q As corrected, is your verified statement in KCS-12 to the best of your knowledge true and correct?

A Yes, it is.

Q And do you adopt it as your testimony in this case?

A I do.

Q Now, with regard to the second verified statement, is it contained in KCS-14, and does it bear the verification or your verification dated November 17, 1984?

A Yes, it does.

Q Do you have any corrections or other modifications which you wish to make to it at this time?

A I do not.

Q Is that verified statement, to the best of your knowledge, true and correct?

A Yes, it is.

Q And do you adopt it as your further testimony in this proceeding?

A I do.

MR. BAKER: That completes Mr. Graf's direct examination.

JUDGE HOPKINS: Mr. Moates?

MR. MOATES: Thank you, Your Honor.

CROSS EXAMINATION

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BY MR. MOATES:

Q Good afternoon, Mr. Graf. My name is Moates.

A Good afternoon, Mr. Moates.

Q Mr. Graf, I want to ask you some questions about your statement in KCS-12. Do you have it there?

A Yes, I do.

Q Do I understand correctly, sir, that the purpose of the testimony in that volume is really twofold, first to submit some historical financial information regarding Kansas City Southern, and second, to introduce and sponsor certain statements regarding the pro forma effects of revenue and expense changes projected by Witnesses Ploth and Rawert?

A That is a good summarization. Yes.

Q Okay. Thank you. And you also sponsor, do you not, three types of pro formas, first, pro forma income statements for the first three years following the transaction?

A Yes.

Q Then pro forma balance sheets for the three years following the transaction?

A That's correct.

Q And a statement of sources and application of funds?

A For the three years as well.

Q For the three years?

A Yes.

Q And those exhibits appear, do they not, in the Kansas City Southern's initial application in KCS-8, Volume 3?

A They do.

Q And you have corrected the -- you have received some corrected data from Mr. Ploth and Mr. Ravert in recent weeks, have you not?

A I have.

Q And having received those corrections from them, did you in turn make appropriate adjustments to your pro formas?

A I did.

Q Were those adjusted or amended pro formas and the amended statement of sources and application of funds submitted to the Commission and the parties?

A Yes, they were.

Q As formal amendments to the application?

A Yes, they were.

MR. MOATES: When did that take place, counsel, if you can tell me?

MR. RAKER: In KCS-18, which is dated January 8, 1985.

BY MR. MOATES: (Resuming)

Q Also, the corrected papers -- corrected pro formas appear in your work papers, do they not?

A They do.

Q All right. Good.

MR. DREILING: Well, Mr. Moates, I don't want there to be any confusion. KCS-18 was filed rather late. KCS-16 had also been filed as the initial errata. It had contained adjusted pro formas for the submissions made to them at that point in time.

The document and the pro forma shown in KCS-18 are different from those shown in KCS-16, and the ones in your work papers that he may be referring to, Mr. Graf can tell me whether or not -- is it true? Maybe the earlier pro formas or the later ones?

THE WITNESS: To the best of my knowledge, corrections were supplied for both changes.

BY MR. MOATES: (Resuming)

Q You concern me here. Let me have just a moment, so we don't clutter this record up.

(Pause.)

A Okay. I think the ones I got out of your work papers are the most recent ones.

Can we go off the record for a moment?

JUDGE HOPKINS: Off the record.

(Whereupon, a discussion was held off the

record.)

JUDGE HOPKINS: Back on the record.

MR. MOATES: Thank you, Your Honor.

BY MR. MOATES: (Resuming)

Q Would you turn to Page 5 of your testimony, Mr. Graf? This is in the section that is headed Review of Historical Financial Information.

A I have it.

Q You indicate in this section what Kansas City Southern's earnings were for 1982 and 1983. I would like to ask you, if you know, what the 1984 results were.

A I do not.

Q Okay. Perhaps we will get some mid-year results.

Could I have Your Honor mark as counsel's exhibit a three-page document produced to us in discovery by KSC? It is a news release dated July 16, 1984.

JUDGE HOPKINS: It will be marked for identification as SFSP-C-101.

(The document referred to was marked for identification as Exhibit Number SFSP-C-101.)

BY MR. MOATES: (Resuming)

Q Mr. Graf, I see in the upper lefthand corner you are listed as one of the two contact persons for this news release. Is that right?

A That's correct.

Q So you are familiar with this document?

A At the time I wrote it, yes. Of course.

Q And this news release highlights, does it not, the second quarter 1984 earnings of Kansas City Southern Industries?

A Yes, it does.

Q If you look on the first page under the caption Segment Review, it indicates, does it not, that transportation revenues increased 7 percent for the second quarter on a combination of higher general commodity car loadings, more ton miles of unit coal, and freight rate increases which became effective in January and April?

Then it goes on and says that these factors were substantially offset by increased expenses. As a result, transportation operating income increased only 1 percent.

A That's correct.

Q All right. Then would you turn to Page 3 and look at the actual numbers? Will you look under

financial information by business segment at the bottom part of that page?

A Yes.

Q Okay. To determine the income from operations transportation entry for the six months ended June 30, '83, and June 30, '84, do I simply subtract the railroad's expenses from the transportation revenues number shown above to derive the income from operations number?

A No, you would not.

Q Okay, how do you get to the income from operations number? What does that number represent?

A Well, the income from operations number constitutes the total expenses which are classified as transportation segment operating expenses deducted from the sum total of all revenues which are classified as transportation revenues, and the major portion of this is railroad, but it is not entirely all Kansas City Southern Railroad.

Q Can you tell me what proportion is not Kansas City Southern Railroad?

A It would be minor, but I cannot give you a specific answer now.

Q Can you give me a range? When you say minor, would it be 1 or 2 percent non-rail, or would it be 10

percent?

A I really don't know.

Q I note that the revenue shown under the transportation segment increased over $13 million from the year previous, for the six months ended June 30, 1984, and at the same time -- I think this is a phenomenon that we discussed with Mr. Carter yesterday in the annual report -- the associated expenses appear to have gone up significantly, which I think would be consistent with the sentences we read on the first page of your news release.

A Yes.

Q So the fact is, whatever the numbers might be, and I understand now we can't get the exact number from this document, but whatever the exact numbers are, the fact is that Kansas City Southern's expenses associated with its transportation activities did increase from 1983 to 1984?

A Yes, that's correct.

MR. MOATES: May I have another document marked, Your Honor? It is a one-page news release from the Kansas City Southern Industries dated August 17th, 1984.

JUDGE HOPKINS: That will be marked for identification as SFSP-C-102.

(The document referred to was marked for identification as Exhibit Number SFSP-C-102.)

BY MR. MOATES: (Resuming)

Q This is also a news release that is dated August 17, '84, Mr. Graf, and bears your name and that of Mr. Rowland as the contact persons?

A Yes, it does.

Q And this indicates, does it not, that notwithstanding the fact that there may have been some increase in expenses, that the company, board of directors of the company still saw fit to declare a 14-percent increase in dividends on the company's stock, correct?

A That's correct.

Q And further down it indicates that the board also declared a regular quarterly dividend on the preferred stock?

A That's correct.

Q And one other item of interest. The board authorized a stock repurchase of the company shares up to a limit of 75,000 shares.

A That is correct.

Q Did that stock repurchase occur, by the way?

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A It has not.

Q Mr. Graf, in your opinion are the projected gross and net revenue effects of the SFSP merger on Kansas City Southern significant and material enough for the company to report those to the Securities and Exchange Commission for disclosure to the investment community?

A Yes, I believe they are.

Q In fact, you have done that, haven't you?

A We did.

MR. MOATES: Your Honor, I would like to have marked as counsel's exhibit a two-page document. It is a Kansas City Southern Railway Company Form 8K to the SEC dated September 6, 1984.

JUDGE HOPKINS: That will be marked for identification as SFSP-C-103.

(The document referred to was marked for identification as Exhibit Number SFSP-C-103.)

BY MR. MOATES: (Resuming)

Q Mr. Graf, you have seen this document before, I take it?

A I have.

Q Your name appears on the second page as one of

the officers of the company authorized to submit this report, correct?

A That's correct.

Q Now, let's review briefly the other events that are being drawn to the SEC's attention.

The registrant will file on September 10, 1984, with the Interstate Commerce Commission a responsive application in the proposed merger of -- I will shorthand this -- SP and the Santa Fe. This application will oppose the merger and state that such merger will reduce annual revenues of registrant by an estimated $27.4 million and reduce annual net income by an estimated $2.7 million.

Registrant also requests that if the merger is approved, certain conditions be applied which would be favorable to registrant. Such conditions, if all were to be granted, would increase annual revenues by $91.1 million and increase annual net income by $1.3 million as offsets to the $27.4 million losses in registrant's revenues and $2.7 million losses in registrant's net income which the SFSP merger would cause.

Did you prepare that statement?

A Yes.

Q And just so we can put it in a temporal context, this was submitted to the SEC four days before

the application which includes your statement in KCS-12 was submitted to this Commission?

A I believe the timing on all those dates is correct.

Q Now, sir, the filing of September 10, 1984, by Kansas City Southern to this Commission did show a $27.382 million gross revenue loss, which I think you want to confirm in that blue volume in Mr. Rawert's testimony, Tables 1 and 2 that he and I discussed earlier.

Do you recall that number?

A Yes, I do.

Q Really I should clarify the record. It is really in Table 2, because it says "restated" on it.

Now, that Table 2 as submitted on September 10 -- I realize it has been corrected since then -- indicated a net revenue impact adverse to Kansas City Southern of $5.1 million. Do you see that?

A Please give me some time.

Q I am sorry. This is in the same volume as your statement, the dark blue volume.

A You are speaking of Mr. Rawert's statement. What page is that on?

Q Page 5.

A I have it.

Q Okay. Just confirming that as of the date of filing of this application the net revenue effect projected by Mr. Rawert from the merger, which is called here Loss Traffic Study Restated, was $5.1 million?

A Yes.

Q Now, does the $2.7 million net income effect which you report to the SEC four days previously, does that come from your testimony at Page 16 where you show net income impact?

A Yes, it does.

Q Would that be the Year Three number of 2.379?

A Right.

Q Was there some small adjustment made between the 2. -- we will call it 6 and the 2.7 in those few days between the two documents, or is this just some kind of a rounding error?

A Well, no, the number that appears in the original Exhibit 17 for Year Three is $2,681,000 loss under the losses column, and that number was pulled from Exhibit 17.

Q Oh, I am sorry. You are right, it was. So that is the $2.7 million you are talking about?

A That's correct.

Q Now, the corrected number in Mr. Rawert's table is about $4.9 million net loss, and the number in

your table has been corrected to 2.579, correct?

A Right, approximately $100,000 difference in my table.

Q Do you consider that to be a non-material difference that doesn't require amending the 8K?

A Absolutely.

Q Now, the figure, also referring to the 8K now, the figure of 1.3 annual net income effect, do you see that?

A Yes.

Q That is meant to represent, I take it, the net of conditions, number --

A Excuse me. Which are you referring to? You are referring to my verified statement now?

Q Yes, if we look at --

A The reason I am having a little trouble following you is that I am working -- I was working off of my amended verified statement.

Q An easier way for me to do this is, can you direct me to the appropriate place in your testimony or the application where I find the $1.3 million?

A Yes, that is in Exhibit 17, also the very same page, Page 3 of 4, which showed $1,294,000 net loss from the loss study. It is the exact counterpart to the 2,681,000 of gains in the gains study. In my filings

before the SEC, we rounded both of those numbers to 2.7 million negative and 1.3 million positive.

Q Just one more time. The page reference, you said Page 3 of 4 of Exhibit 17?

A Page 3 of 4 of Exhibit 17, of KCS-8.

Q Okay, and in particular what line number?

A It is the very bottom line under the column Gains of 1.3.

Q Okay.

A I said of 1.3, but the gains column.

Q Okay. Now, do you have the amended Exhibit 17?

A I do.

Q Has not the number you just pointed me to, the 1.3, which you reported to the SEC, has that not been adjusted to 2.147?

A That number has been adjusted to 2.147.

Q And again you consider that change so minor and non-material that it doesn't require amendment?

A I would respond twofold. First of all it is still minor and non-material, but the basis upon which the 8K was filed was related to the losses of 2.7 million.

Q Not the gains?

A Not the gains. That's correct.

Q Okay. One question on Page 7 of your verified statement, sir.

A Yes, I have it.

Q You indicate here and I think made reference to it later in your numbered paragraph 1 that on December 1, 1984, the company had a substantial amount of debt due, $27.9 million of first mortgage bond debt, and that you had accumulated a cash reserve of 33.6 to meet that.

Have you in fact retired that debt?

A Yes, we have.

Q And are your cash reserves, cash and short-term investments therefore now reduced to about $5 or $6 million?

A It is higher than that.

Q How much higher?

A I would refer to memory of approximately $7 to $10 million.

Q Okay. To your knowledge does the company have any similar -- I shouldn't say similar. Does the company have any other debt that will come due for payment in the next three years?

A Well, we have current maturities of debt on the railroad each and every year related to equipment obligations and capital leases.

Q Do you have any other mortgage bond debts that come in the next --

A We do not.

Q So you have no concern under present circumstances and with the expenditures that you plan to make for capital improvements associated with IRMA and trackage rights, that you would be required to finance those undertakings in a manner other than from working capital?

A The $2 million of capital expenditures clearly could be handled from working capital.

Q Do you have any idea of how much higher than $2 million that number would have to become before you had to reassess that judgment?

A I think the answer to that is twofold, Mr. Moates. It would partially based upon whatever cash reserves we had at the time and the amount of anticipated expenditures.

If it's helpful to these proceedings, it would be my judgment, based upon my experience, that we could finance probably as much as $10 million without considering additional debt or equity, depending upon the timing of the expenditure and the terms of payment that one might receive from suppliers.

The second aspect to that answer would relate to what we might deem to be prudent management of our financial resources. We try to match the purchase of long term assets with long debt, and it's conceivable

that we would not wait until we got to a $10 million level before we financed it with some form of indebtedness.

Q And that's all predicated on the fact that there is no other outstanding debt that is going to become due and payable within the next -- I said three years; what if I made it three to five years? Would the answer still be the same?

A We do have approximately $11 to $13 million of debt which matures each and every year. That represents the installment portion of capital lease and primarily equipment obligations of the railroad.

Q Do you typically pay that debt from your existing cash resources working capital?

A Yes, we have.

MR. MOATES: If could ask counsel, because it would avoid my marking something, are these amended exhibits, 16, 17, and 18 now part of the record? Are they part of your application?

MR. BAKER: Yes, they are.

BY MR. MOATES: (Resuming)

Q I would like to ask you some questions about those amended exhibits, Mr. Graf.

First of all, if we can look at the pro forma income statements in Exhibit 17 and, in particular, my

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questions emanate from pages 12 and 13 of your testimony, and I think the answers will come from this exhibit.

On pages 12 and 13, you make reference to the approximately six miles of Southern Pacific track from Texas City, Texas to Galveston, SP's Hodge Yard at Ft. Worth, certain additional connecting tracks that KCS would propose to construct if its application were granted.

And you are the witness, are you not, who has included the cost for those acquisitions and new tracks to be included in the income statement that's marked as Exhibit 17?

A I'm the witness for that. I have included the numbers.

Q You have included the numbers.

First of all, with respect to the Texas City-Galveston line, I note that note H to your Exhibit 17, which I am afraid we're going to have to go to the volume to refer to -- at least us out here because it's not part of your amended thing -- I misspoke. Note H to Exhibit 16 tells us that you have made an estimate that the purchase of that line would cost $492,000.

Is that correct?

A That's correct.

Q What's the basis for that estimate?

A The basis for that is information supplied to me which was provided to me by a combination of our real estate department and our operating department.

Q Do you know whether that number was predicated on a current appraisal of that line?

A Yes, I do. If I may refer to my notes --

Q Sure.

A The cost of track was estimated at net salvage, and the real estate was based upon an appraisal of adjacent and related-type properties.

Q Can I ask you, sir, what file you just referred to give me that answer?

A It's in my working papers on pages 61 and 70.

Q The entire file, or just the document that you referred to?

A Would you repeat the question?

Q Is the entirety of the file that you hold in your hand in your working papers?

A Yes. You should have copies of everything I have here.

Q That whole file?

A That entire file. That's correct.

Q Do you know by whom that appraisal was done?

Was it done by KCS real estate people?

A Yes, it was.

Q And do you know what the basis for the appraisal is?

A To the best of my understanding, it was based upon an estimate of comparable properties, and it is my opinion, although I did not ask, that it was based upon the experience of the people involved.

Q All right.

The next item is right above that. The purchase of Hodge Yard from Southern Pacific is valued at $405,000. Do you see that?

A Yes.

Q Again, was that number derived by an appraisal by Kansas City Southern real estate personnel?

A Yes, it was.

Q In making these appraisals, did your people go on the property?

A Yes, they did.

Q With permission of Southern Pacific?

A I do not know. I assume they had the permission.

Q Now, would your testimony be the same if this was also appraised on that salvage value of the yard tracks and an appraisal of the land?

A I don't understand the question.

Q How was the value of Hodge Yard derived?

A The value of Hodge Yard was based on an estimated fair market value by our real estate department in consultation with local realtors.

Q Was it fair market value of the yard as a going concern; that is, as a railroad yard; or fair market value of the land?

A I would have to refer back to and read the information supplied to me on this. It's several pages long, and in fairness there may be a variety of input parameters that were used.

Q Well, again, that information is in this file that we have?

A It is in the working papers provided to you.

Q And then there is also a figure in Note H to Exhibit 16 that indicates the estimated cost of constructing the connecting tracks that the operating plan provides for is $892,000. And I would ask you the same question. What was the basis for that estimate?

A The basis for that was input supplied by the operating department, part of which is in Mr. Carter's testimony on 13-31.

I don't know the exact document. The engineering department, which is a part of our operating

department which made the determination of the materials and supplies required, using inventory values necessary to determine the price of that, including labor components, et cetera.

Q All right, sir.

Then there was a Note G to Exhibit 16 right above that. Do you see that? It says "Increase in investments reflected purchase of one-half of Santa Fe's ownership in the Houston Belt & Terminal Railway Company."

A Yes, I see that.

Q The appropriate figure for that note is $165,000; is that right?

A That's right.

Q Isn't that the same number that was on a handwritten sheet that I introduced in my examination of Mr. Carter yesterday?

A I believe it is.

Q And he indicated -- were you here for this examination?

A I was.

Q He indicated, did he not, that it was his intention with respect to the interest of Santa Fe in the Houston Belt, that a fair price be paid for that?

A I think that's what he said. I would be

relying on my memory.

Q I think we could get the transcript, but I looked at it a while ago, and if I remember right, he indicated at transcript 7390 and 91 that -- well, I don't want to paraphrase it. Let me get that.

He said, "This sheet," referring to the handwritten document I showed him that had the number of $165,000 on it and an indication that that had been taken from the R-1 --

A That's correct.

Q For the Santa Fe -- he said, "This sheet was used by our costing staff in order to set some costs. I did not have this in the back of my mind when I made the offer. We're going to pay whatever the Commission tells us the value of that one-half of one-eighth" -- he corrects himself -- "one-half of one-quarter, which would be one-eighth, of HB&T's value minus all the real estate."

The question is, in your expert judgment, does $165,000 represent anything like the fair value for one-half of the Santa Fe's share of the Houston Belt?

A I think it was a perfectly logical and fair thing to use for purposes of preparing these pro formas.

Q Well, that's one answer. How about the answer

to my question, in your judgment.

A No. I have never seen the property. I do not -- I have never looked at the detail of the property that's involved. What we have here is an equity investment by a number of railroads in a company which is designed to provide switching services, and whose cost structure and income stream is reflective, if you will, of the services provided.

It is -- has been the judgment of both myself and my staff in using the equity investment of the Santa Fe in this number, that it is a non-income-producing asset whose primary purpose is to provide equity participation by all the railroads who switch in that area.

It's not unusual, in my judgment, to use a book value which is essentially the number that we used in this particular case. In no way would I dispute with Mr. Carter the fact that if there is a different value determined, we are not suggesting we have a precise number for the value.

Obviously, in a third party transaction, properly negotiated, one would expect that you pay whatever that perceived value is between two independent parties, be it a number higher than this or perhaps a number lower than this.

Q Isn't it true, Mr. Graf, that sometimes non-income-producing assets can be very valuable assets for a particular business?

A That is certainly possible; yes.

Q And isn't a very good illustration of that in the railroading business terminal railroads?

A I don't know.

Q Did you hear Mr. Carter testify that he had had a conversation with a trustee of the Rock Island Railroad about the possbility of acquiring the Trustee's interest in the Houston Belt?

A Yes, I did.

Q Are you aware of whether there was any price mentioned in that conversation?

A I'm not aware that any price was mentioned.

Q A couple of other questions about Exhibit 16 while we have it there. Can you confirm for me, sir, since I am not an expert on reading balance sheets, that the total assets in the last column on each of these pages, the total assets for KCS are projected to increase between the pro forma year and year three by something in the range of $[illegible] million?

A Would you repeat your question again now, please?

Q Yes. Could you confirm or tell me if I am

misreading -- which I may be -- these pro formas? Can you confirm that they do, in fact, demonstrate that the Kansas City Southern would enjoy an increase in total assets over this three-year period of approximately $16 million?

A At the end of year three, it would seem to me that the number would be approximately $20 million. And I am basing that on the fact that if you look at page 1 of 7 in Exhibit 16, in the lower left corner, you see a number of $552 million, which is the base number, and if you compare that to the lower right-hand number of page 6 of 7 of Exhibit 16, you see the number $572 million.

So, in answer to your question, it would be in terms of a quick response, approximately $20 million.

Q You're right. That's why I asked the question, because I had used the pro forma number on the third page, which was wrong.

Also, looking at the entry for temporary cash investments and accounts receivable, can you confirm that the sum of those two entries would be higher by year three than they are in the pro forma year?

I added the numbers. And I'll just ask you to see if it looks like it's about 81 million versus 76 million.

A The beginning number is, as you have said,

roughly 76 million. The ending number would be roughly 83 million. I didn't add it. But it meets the reasonableness test.

Q In any event, it is higher?

A It is higher. That's correct.

Q One other question about the exhibit. On year one -- yes, year one, page 1, under the annual net change for temporary cash investments, you show a decrease of about $18.4 million.

Do you see that?

A Yes, I do.

Q And we have a Note B that tells us that -- let me go back to the book for a minute -- tells us in essence that that's due to conversions. It says reduction of cash in accounts receivable due to diverted traffic from KCS to the SPSF merged system.

A Yes.

Q Where does the $18.4 million come from?

A The $18.4 million is the net effect of all of the other changes in the annual net change column which is designed to basically give us an indication of how the company's financial condition changed from the beginning of the year to the end of the year.

Q I guess my problem here -- and you'll have to excuse me because I'm not a financial expert -- is when

I look at Mr. Pawert's tables again, it appears to me that there is a greater contribution to net revenue as a result of the recapture and gain studies than there is a net loss as a result of the loss studies.

And, intuitively, that would suggest to me that you would be somewhat better off, and this tells me that you're going to be $18 million worse off in terms of cash investment.

A That is not the intention of the $18 million. That does not relate to the gains or losses study at all.

Q It's just the losses?

A No. It doesn't relate to either. It represents basically the mechanics that we would have to go through to reflect adjustments to our beginning year balances, so that we come up with the actual ending year balances in our balance sheet.

Q I got you.

A The Commission requires us to use the same year three times in a row. And for purposes of forecasting our balance sheet change, we have no way to do that except to reflect the same differential that existed during the year 1983 to each of three succeeding years.

And, unfortunately, on a balance sheet, those

numbers carry forward.

Q That's what I was afraid of. Just a few more questions if I may. On page 14, you indicate that projected reductions of federal income taxes were applied to the pretax losses associated with diverted traffic.

Those reductions were made at the statutory rate of 47.5 percent. Did KCS, in fact, Mr. Graf, pay 1983 income taxes at the statutory rate?

A What it paid and what it books for accounting purposes are two different things. We are required under the accounting principles, which is what these financial statements are based upon, to accrue the statutory rate or any other effective rate which takes into consideration the accounting elements that determine income and loss.

On a tax return basis, the amounts might differe.

Q In fact, do they differ?

A They do differ.

Q I assume they differ in that the actual effective rate is lower than the statutory rate?

A That's correct.

Q On page 15, your last paragraph, you say: "The pro forma projections of net income show that even

with the affirmative conditions sought by KCS, it's earnings will be negatively impacted over the three year period required to implement the operating plan."

That really isn't true for at least year one, now that you've made those changes, is it?

A That's correct. But my reference here is over the three-year period and the cumulative effect of a positive 118 and a minus 65 and a negative 432 would be negative.

Q Slightly negative. But when you first drew your conclusions in this verified statement, as your original exhibit showed, the percentages of losses recovered by gains was in year three less than 50 percent, and you now show them as being 83 percent.

A That's correct. However, my statement is still correct and therefore was not changed.

Q One question on Exhibit 18 which is the statement of sources of funds. Can you simply confirm for me that I'm reading this correctly; that in the corrected exhibit, that in year three you show a net increase in working capital for Kansas City Southern of over $10.5 million?

I think it's the last lower right-hand entry.

A That's correct.

Q By the way, have you ever constructed any pro

forma income statments to show the effects on KCS of the losses attributable to this merger only? In other words, not a netted kind of pro forma?

A No, we have not.

Q All right, then. Lastly, over on page 19 in your conclusion, I note that in your errata, you have stricken the words "revenue and," so that the conclusion is no longer that the revenue and earnings gains projected by KCS would offset approximately 83 percent of the losses; only the earnings.

Wasn't it true, even initially, that the revenue gains projected exceeded substantially the revenue losses projected?

A That's correct. That was strictly an error, very minor.

Q In fact, at this point, even with the corrected numbers, the gross revenue gains are something like 340 percent of the projected gross revenue loss?

A That's right. That's why the change was made.

Q Thank you, Mr. Graf. That's all my questions.

JUDGE HOPKINS. Redirect?

MR. MOATES: Excuse me. I'm sorry. Mr. Rawert kicked those few questions to Mr. Graf and I put

them aside and forgot about them. Just to clear things up.

JUDGE HOPKINS: Go ahead.

BY MR. MOATES:

Q Do you remember when I asked Mr. Rawert about the seven or more supervisory personnel that Mr. Carter indicates and your operating plan indicates would be added on the route?

A Yes.

Q How did you account for the cost of those people, or where did you account for it?

A We accounted for the cost. It's reflected in each of the three income statements which are a part of Exhibit 17.

Q Is there a particular input document, though, for the cost of these people?

A Yes, there is.

Q Is it in your work papers?

A It is.

Q Did you hear Mr. Carter testify that he would beef up the regional sales offices and add other employees if IRMA is successful?

A Yes, I did.

MR. RAKER: He said "if necessary," didn't he?

MR. MOATES: I assumed "if necessary" meant if IRMA was successful.

THE WITNESS: I accepted your statement as worded. I did understand, as counsel has said, that he would do it if necessary.

BY MR. MOATES: (Resuming)

Q But the only point I wanted to clarify is that the only expense that you have included for purposes of creating a pro forma are the seven additional supervisory personnel shown in the operating plan?

A That's correct.

MR. MOATES: Okay, thank you, sir.

MR. RAKER: No redirect, Your Honor.

We move the admission of both verified statements of Mr. Graf.

JUDGE HOPKINS: Any objection?

MR. MOATES: No objection.

JUDGE HOPKINS: They will be received in evidence.

MR. MOATES: I move my counsel's exhibits for this witness.

JUDGE HOPKINS: Any objection?

MR. RAKER: No objection.

JUDGE HOPKINS: They will be received in evidence.

(The documents referred to, previously marked Exhibits SFSP-C-101, 102 and 103 for identification, were received in evidence.)

JUDGE HOPKINS: Off the record.

(Discussion off the record.)

JUDGE HOPKINS: We'll be in recess until 9:00 o'clock.

(Whereupon, at 4:37 o'clock p.m. the hearing recessed, to reconvene at 9:00 o'clock a.m., the following morning, Thursday, January 17, 1985.)