

STB    FD    32760    (Sub 26)    12-14-98    D    192687



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**ORIGINAL**

**BEFORE THE  
SURFACE TRANSPORTATION BOARD  
WASHINGTON, D.C.**

ENTERED  
Office of the Secretary

DEC 14 1998

Part of  
Public Record

STB Finance Docket No. 32760 (Sub-No. 26)

Union Pacific Corp., et al.  
-- Control and Merger --  
Southern Pacific Corp., et al.

and

~~STB Finance Docket No. 32760 (Sub-No. 29)~~

Burlington Northern and Santa Fe Railway Company -  
- Application for Additional Remedial Conditions  
Regarding Houston/Gulf Coast Area

**[HOUSTON/GULF COAST OVERSIGHT]**

**ARGUMENT SUMMARY OF  
BROWNSVILLE & RIO GRANDE INTERNATIONAL RAILROAD**

Pursuant to the Board's Decision No. 8 in the above-captioned proceeding, Brownsville & Rio Grande International Railroad ("BRGI") submits the following written argument summary in lieu of oral presentation.

BRGI's interests in this proceeding are closely linked to two particular portions of The Burlington Northern and Santa Fe Railway's ("BNSF") requests for additional remedial conditions as set forth in BNSF's Sub-No. 29 filings. Specifically, BRGI wholeheartedly supports BNSF's proposal for improved operations and competition in the Brownsville/Harlingen area. (Included in BNSF's request is the proposal that BRGI serve as BNSF's agent for all traffic south of Harlingen, TX -- an element of BNSF's proposal that is crucial to the efficient and competitive movement of traffic between Mexico and the Port of Brownsville.)



BRGI also supports BNSF's request for permanent bi-directional overhead trackage rights on UP's Caldwell-Flatonia-Placedo line.

In this argument summary, BRGI wishes briefly to comment upon the circumstances warranting expeditious Board action to improve rail competition and efficient service in the vicinity of the Brownsville-Matamoros international gateway.

A product of BNSF's settlement negotiations with UP during the early phases of the original UP-SP merger proceeding was an agreement permitting BNSF trackage rights access to Brownsville, including direct access to the Port of Brownsville (via a connection with BRGI) and the Mexican railroad system (TFM) at Brownsville/Matamoros. BRGI and the shippers located within the Port of Brownsville expected direct service from BNSF, but this has not yet materialized. The Board is probably well aware that this is, to BRGI's knowledge, the only instance where BNSF has not instituted trackage rights operations where it has been permitted to do so under the UP-BNSF settlement agreements.<sup>1</sup>

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<sup>1</sup> BNSF has made clear throughout these proceedings that it regards trackage rights service to various "2-to-1" points, including Brownsville, as far preferable to haulage rights access. For UP to assert, in effect, that BNSF haulage access to the Brownsville area is "good enough" and that BNSF can be competitive on the basis of its haulage rights access alone misses the point. BNSF recognizes that its physical presence in this market area will ensure the most robust level of competition, and it had always contemplated converting its haulage rights access to trackage rights as soon as practicable to maximize competition. Indeed, BRGI has expected that BNSF would, at the very least, compete for bridge traffic between the Port of Brownsville and TFM at Matamoros, but in this regard BNSF has not yet had the opportunity to prove itself a competitor. UP's operating practices in the Brownsville area have thus far thwarted BNSF's goals, and have therefore frustrated BRGI's and the Port of Brownsville's expectations.



Earlier in this proceeding, Larry Cantu (BRGI's President and Chief Operating Officer) submitted verified statements on behalf of BRGI and the Port of Brownsville which made clear how BRGI and the Port of Brownsville have, post-merger, failed to secure the level of rail competition that BNSF's actual, physical presence in the area could ensure.

BNSF has, in Sub-No. 29, outlined an operating proposal for the Harlingen/Brownsville area that will ensure genuine rail competition. BRGI supports BNSF's proposal for a number of reasons, but primarily because it turns out that, in this case, the UP-BNSF settlement agreements have failed to live up to their billing and must be revisited and adjusted. Since BNSF and UP seem unable promptly to address and resolve this instance where the UP-BNSF settlement agreement has fallen short of its goal, it may be up to the Board to impose new conditions. BRGI's earlier testimony in this proceeding establishes why and how BNSF's proposal would improve operations generally through the Brownsville-Matamoros international gateway, and how it would ensure for BRGI and its shippers a competitive routing option for traffic to and from TFM at Matamoros. Indeed, BRGI operations are the centerpiece of BNSF's proposal for Brownsville/Harlingen. BRGI is ready, willing and able to do its part to implement the essential operations that BNSF contemplates in its request to the Board.

BNSF's proposal for Harlingen/Brownsville operations would not only ensure a meaningful, fully competitive BNSF presence in the lower Rio Grande Valley, but it would permit a truly local operation (BRGI) -- already well versed in the unique requirements of trans-border rail operations -- to assume responsibility for the handling of BNSF traffic to and from both Mexico and the Port of Brownsville. BNSF's proposal would aid efficient operations in the area, because it would enable BRGI to make expanded use of existing Port facilities to expedite and otherwise improve customs and USDA inspections and clearance for trans-border traffic. It would have the incidental but beneficial impacts of expanding the operations of a lower-cost short line operator, increasing the use of Port infrastructure (rather than necessitating otherwise avoidable capital expenditure by either BNSF, UP, or both), and reducing both the cost and transit times for traffic moving between the Port of Brownsville and TFM.<sup>2</sup>

UP has represented to the Board that it is willing to discuss with BNSF (and presumably also with BRGI) certain arrangements consistent with BNSF's operating proposal for the Harlingen/Brownsville area. However, UP has gone so far as to incorrectly claim that the counter-proposal it has issued to BNSF

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<sup>2</sup> BRGI notes that UP and BNSF, as large Class I carriers, are both oriented toward longer distance hauls. As a result, neither is the ideal choice to serve as an intermediate switching or "bridging" carrier between TFM and BRGI. On the other hand, BRGI brings to its operations the experience of a terminal short line carrier superbly situated for such short-haul service.



and BRGI "should moot... BNSF's condition proposal." UP/SP-356 at 12. While BRGI is pleased that UP is apparently willing to negotiate with BNSF and BRGI regarding Harlingen/Brownsville operations, BRGI regards UP's counter-proposal as an overture to further negotiations, which have not yet taken place.<sup>3</sup>

BNSF has already pointed out that UP misunderstood at least a part of BNSF's proposal, especially where UP incorrectly assumes that both BRGI and BNSF would operate separately south of Harlingen, TX, when, in fact, BRGI will handle all BNSF traffic as BNSF's agent. Further, UP incorrectly asserts that it provides "bridging" services between TFM and BRGI according to some agreed-upon "methodology," and it argues that BNSF should refrain from entering into any separate agreement with BRGI for any competing bridging service that BRGI might consider providing. See, UP/SP-358, Verified Statement of Gary Norman at 26 and supplemental attachment. To BRGI's knowledge, there is no such "bridging" charge methodology. There is only a switching charge, negotiated from time-to-time with UP, that is currently high enough to force significant amounts of traffic to trucks.

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<sup>3</sup> BRGI anticipates that, if the parties can negotiate an agreement, it will require greater specificity than that contained in Mr. John Holm's (UP) two-page letter of September 5, 1998, addressed to Larry Cantu (BRGI) and Rollin Bredenberg (BNSF). Thus, if there is still room for a negotiated settlement, and BRGI believes that there may be, the Board should not act to impose the general conditions set forth in UP's counter-proposal letter. In any event, BRGI cannot stress enough that it believes any settlement lacking the full compliment of proposed BRGI agency operations will unnecessarily perpetuate international gateway gridlock and UP's existing control over traffic between Mexico and the Port of Brownsville.

In addition, UP's efforts to persuade BNSF not to offer any competitive bridging service between TFM and BRGI is precisely the sort of anti-competitive behavior that BNSF's service in the area was supposed to address.

Finally, while UP's counter-proposal to BRGI and BNSF (as contained in Mr. Holm's September 5th letter), is clearly a constructive step in the right direction, BRGI objects (as we understand BNSF does) to UP's adamant refusal to permit BRGI to serve as BNSF's agent for all traffic south of Harlingen. UP claims that there is no legitimate basis for such an operating arrangement. UP, of course, is wrong. BRGI and BNSF have both made clear throughout this proceeding that BRGI's operations would aid immensely in promoting fluid operations at this gateway, and would hasten BNSF's efforts to establish a more competitive presence in the area. As evidence of the proposal's legitimacy, the record already reflects that BRGI, BNSF, TFM, the United States Department of Agriculture, the United States Department of Transportation, and numerous shippers located within the vicinity of the Port of Brownsville support this operating arrangement. Only UP opposes it.

UP seems to argue that BNSF should not be permitted to have BRGI serve as its agent, because UP is barred by its collective bargaining agreements from doing the same thing. While that may be true technically, UP could presumably transfer operations south of Harlingen to BRGI by means of a sale, lease, or trackage rights agreement. BNSF, on the other hand, without

its own lines or facilities in the Harlingen/Brownsville area, lacks the ability to undertake any of these options currently available to UP.

While UP's counter-proposal is a positive step, it is not the end of the road, nor is it the "extraordinarily generous" accommodation that UP would have the Board think it is. Instead, UP still seeks to establish operations in the Harlingen/Brownsville area on its own terms, and it clearly seeks to regulate BNSF's competitive access to the Port of Brownsville (and BRGI) by urging BNSF to -- (1) decline to provide for BRGI and its customers alternative bridging service between TFM and BRGI, and (2) accept a "phantom" switching service "methodology" for BRGI-to-TFM traffic which would be handled in exclusive UP service. In the end, UP would rather keep BRGI under its thumb and delay the initiation of BNSF trackage rights operations to the area than permit the efficiencies and enhanced competition that would flow from the full implementation of BNSF's proposal.

In his verified statement filed with the Board in this proceeding on October 16, 1998, Larry Cantu (on behalf of BRGI) stated his support for another component of BNSF's request for additional remedial conditions. Specifically, BRGI supports BNSF's request for permanent bi-directional overhead trackage rights on UP's Caldwell-Flatonia-Placedo line. As Mr. Cantu has already noted, such a condition would aid traffic flows to and from the Brownsville area.



BRGI is grateful to the Board for permitting BRGI the opportunity to present this written argument summary. We urge the Board to act expeditiously to implement those conditions, including those discussed in this argument summary, that not only foster the full measure of rail competition originally anticipated at the time the Board approved the UP-SP merger but also promote the most efficient transport of railroad traffic through international gateways.

Respectfully submitted,

Robert A. Wimbish  
Robert A. Wimbish

Counsel for the Brownsville & Rio Grande  
International Railroad

**CERTIFICATE OF SERVICE**

I hereby certify that I have, this 14th day of December, 1998, served a copy of the foregoing document upon all parties of record by means of first class mail, postage prepaid.

Robert A. Wimbish  
Robert A. Wimbish



STB FD 32760 (Sub 26) 12-14-98 D 192688

192688

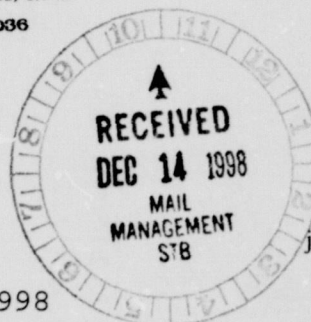
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December 14, 1998

BY HAND DELIVERY

The Hon. Vernon A. Williams  
Secretary  
Case Control Unit  
Attn: STB Finance Docket  
No. 32760 (Sub-Nos. 26 & 29)  
Surface Transportation Board  
Washington, D.C. 20423-0001

ENTERED  
Office of the Secretary

DEC 14 1998

Part of  
Public Record

Re: Finance Docket No. 32760 (Sub-Nos. 26 & ~~29~~)  
UP/SP Oversight -- Houston/Gulf Coast Area

Dear Mr. Secretary:

Enclosed for filing in the above-referenced proceeding please find an original and twenty-five (25) copies of the Summary of Texas Utilities Electric Company's Position in Support of BNSF's Remedial Condition No. 6 (TUE-25). A conforming computer disk is also enclosed.

Finally, we also have enclosed an additional copy of this filing to be date-stamped and returned to the bearer of this letter.

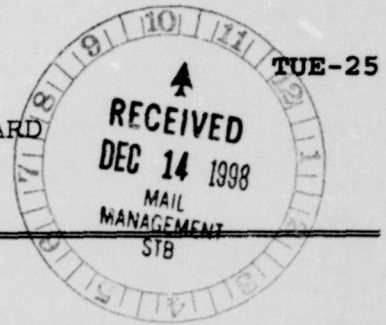
Thank you for your attention to this matter.

Sincerely,

John H. LeSeur

JHL:mfw  
Enclosures

BEFORE THE  
SURFACE TRANSPORTATION BOARD



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UNION PACIFIC CORPORATION,	)	
UNION PACIFIC RAILROAD COMPANY,	)	
and MISSOURI PACIFIC RAILROAD	)	Finance Docket No. 32760
COMPANY -- CONTROL AND MERGER --	)	(Sub Nos. 26 & 29)
SOUTHERN PACIFIC RAIL CORPORATION,	)	
SOUTHERN PACIFIC TRANSPORTATION	)	[Houston/Gulf Coast
COMPANY, ST. LOUIS SOUTHWESTERN	)	Oversight]
RAILWAY COMPANY, SPCSL CORP.,	)	
and THE DENVER AND RIO GRANDE	)	
WESTERN RAILROAD COMPANY	)	

---

**SUMMARY OF TEXAS UTILITIES ELECTRIC COMPANY'S  
POSITION IN SUPPORT OF BNSF'S REMEDIAL CONDITION NO. 6**

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Dated: December 14, 1998

Attorneys for Texas Utilities  
Electric Company

UNION PACIFIC CORPORATION,	)	
UNION PACIFIC RAILROAD COMPANY,	)	
and MISSOURI PACIFIC RAILROAD	)	Finance Docket No. 32760
COMPANY -- CONTROL AND MERGER --	)	(Sub Nos. 26 & <del>29</del> )
SOUTHERN PACIFIC RAIL CORPORATION,	)	
SOUTHERN PACIFIC TRANSPORTATION	)	[Houston/Gulf Coast
COMPANY, ST. LOUIS SOUTHWESTERN	)	Oversight]
RAILWAY COMPANY, SPCSL CORP.,	)	
and THE DENVER AND RIO GRANDE	)	
WESTERN RAILROAD COMPANY	)	

Pursuant to Oversight Decision No. 8, Texas Utilities Electric Company ("TU Electric") files this argument summary. TU Electric is a party of record in this Oversight Proceeding. We submitted a rebuttal statement ("TU Electric Rebuttal") to the Board on October 16, 1998 supporting Burlington Northern and Santa Fe Railway Company's ("BNSF") Remedial Condition Request No. 6. This request provides:

BNSF Application for Additional Remedial Conditions Regarding the Houston/Gulf Coast Area at 14 (dated July 8, 1998). We file this summary, which Decision No. 8 authorized, to emphasize to the Board the importance of this matter to TU Electric and its customers.



**SUMMARY**

TU Electric was an active party in the proceedings that led to the Board's approval of the merger between the Union Pacific Railroad Company ("UP") and the Southern Pacific Transportation Company ("SP"). See Decision No. 44 (served Aug. 12, 1996). In those proceedings, the Board granted, over UP/SP's objections, TU Electric's requested condition granting BNSF trackage rights over an SP line near TU Electric's Martin Lake Station. Id. at 186. The Board took this action to preserve TU Electric's pre-merger ability to obtain rail service from two competing sets of rail carriers at TU Electric's Martin Lake Station. The Board further ordered additional trackage rights in favor of BNSF to permit BNSF to provide service to and from the Martin Lake Station on a directional basis, consistent with UP/SP's announced directional running plans on lines near the Martin Lake Station. Id.

UP/SP's post-merger actions have necessitated TU Electric's participation in the instant oversight proceeding. These actions impact on BNSF's ability to provide competitive rail service to a second TU Electric plant -- the Big Brown Station situated near Fairfield, Texas. TU Electric plans on receiving Powder River Basin ("PRB") coal deliveries from BNSF at Big Brown. Deliveries are currently scheduled to start in the year 2000. BNSF's initially planned PRB-to-Big Brown route includes a segment between Fort Worth and Waxahachie, Texas where BNSF planned to move TU Electric coal trains over UP-granted

trackage rights (see Schematic 1 attached). However, after the UP/SP merger, UP/SP unilaterally announced its plans to operate the Fort Worth/Waxahachie line directionally, with traffic flows going in a northerly direction. Under this planned configuration, BNSF would have to move loaded TU Electric trains "against the flow." BNSF has informed TU Electric that such an operation is not feasible and, as a consequence, BNSF's only substitute routing option is to move loaded TU Electric coal trains over a Dallas Area Rapid Transit ("DART") line (see Schematic 2). DART is the high speed commuter rail carrier serving the greater Dallas-Fort Worth area. BNSF has further informed TU Electric -- and the Board<sup>1</sup> -- that running the coal trains over the DART line will create significant operating difficulties for BNSF.

TU Electric has conducted its own, independent investigation of UP's directional running plans in the Dallas-Fort Worth area. The results of this investigation are set forth in the expert testimony appended to TU Electric's rebuttal submission. The results of our investigation confirm the grim picture presented by BNSF. Any BNSF efforts to run TU Electric coal trains "against the flow" on the Fort Worth/Waxahachie line will create huge operational problems for BNSF. TU Electric Rebuttal at 4. BNSF's DART route option is also a terrible one for TU Electric (and other similarly situated shippers). Common sense teaches that running freight trains over a busy commuter rail line is not

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<sup>1</sup> See, e.g., BNSF Application for Additional Remedial Conditions, V.S. Hord at 19.

a sound transportation solution. TU Electric's expert testimony confirms this obvious conclusion. TU Electric Rebuttal at 3-4.

BNSF recognizes that it has no existing marketplace solutions to respond to UP/SP's new directional running plans. Accordingly, BNSF has asked the STB in its Request No. 6 to grant it trackage rights on UP's line between Dallas and Fort Worth. With these trackage rights, BNSF will be able to serve Big Brown on a "with the flow" movement and avoid the DART line (see Schematic 3).

TU Electric supports BNSF's trackage rights Request No. 6.<sup>2</sup> Granting that request will allow BNSF to provide a viable routing for TU Electric's Big Brown coal trains. Granting this relief is also consistent with the Board's prior ruling in Decision No. 44 involving TU Electric's Martin Lake Station. There, the Board carefully crafted an order that provided BNSF a "with the flow" route to TU Electric's Martin Lake Station. Conversely, failure to grant this request will significantly impede BNSF's ability to provide efficient service to TU Electric's Big Brown Station -- a result that is truly unfair to TU Electric, and unnecessary.

UP/SP does not dispute the operating problems that its directional running plans in Dallas-Fort Worth will cause to

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<sup>2</sup> Other coal shippers impacted by UP's directional running plans in the Dallas-Fort Worth area include Houston Lighting & Power Company, Texas Municipal Power Agency and Entergy Services, Inc. Each of these shippers has filed statements supporting BNSF's Request No. 6. See BNSF Rebuttal Evidence and Argument, Attachment 4 (dated Oct. 16, 1998).



BNSF, and shippers like TU Electric. UP/SP asserts, however, that it can run its railroad -- and deal with the Houston/Gulf Coast service issues -- in any way it sees fit. See TU Electric Rebuttal at 6-7. Such an approach is not in the public interest. The Board needs to insure that UP's implementation of the UP/SP merger -- as well as its response to the Houston/Gulf Coast crisis<sup>3</sup> - does not create a huge new set of operating problems. Granting BNSF's Request No. 6 will help achieve this objective.

Respectfully submitted,

By: John W. McReynolds  
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Dated: December 14, 1998

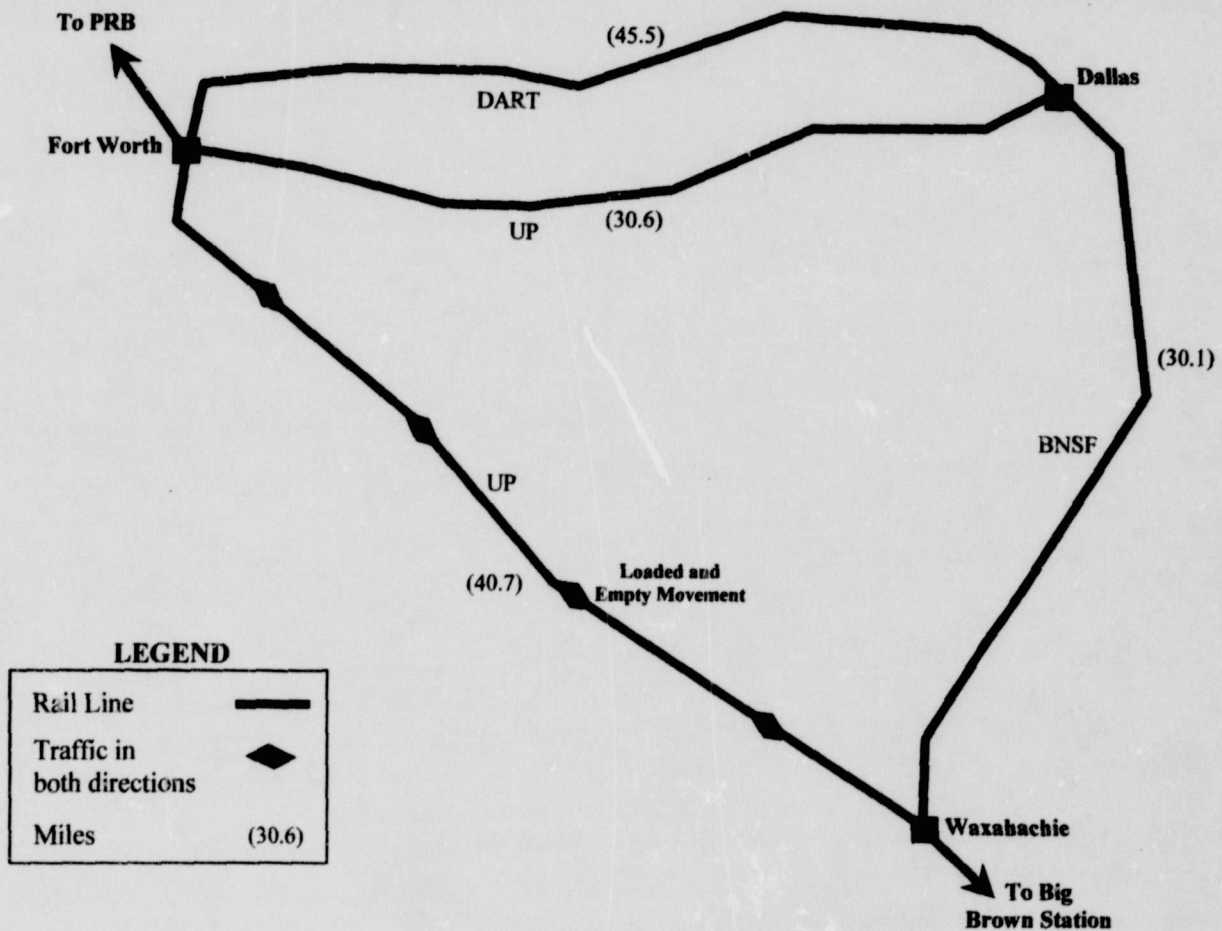
Attorneys for Texas Utilities  
Electric Company

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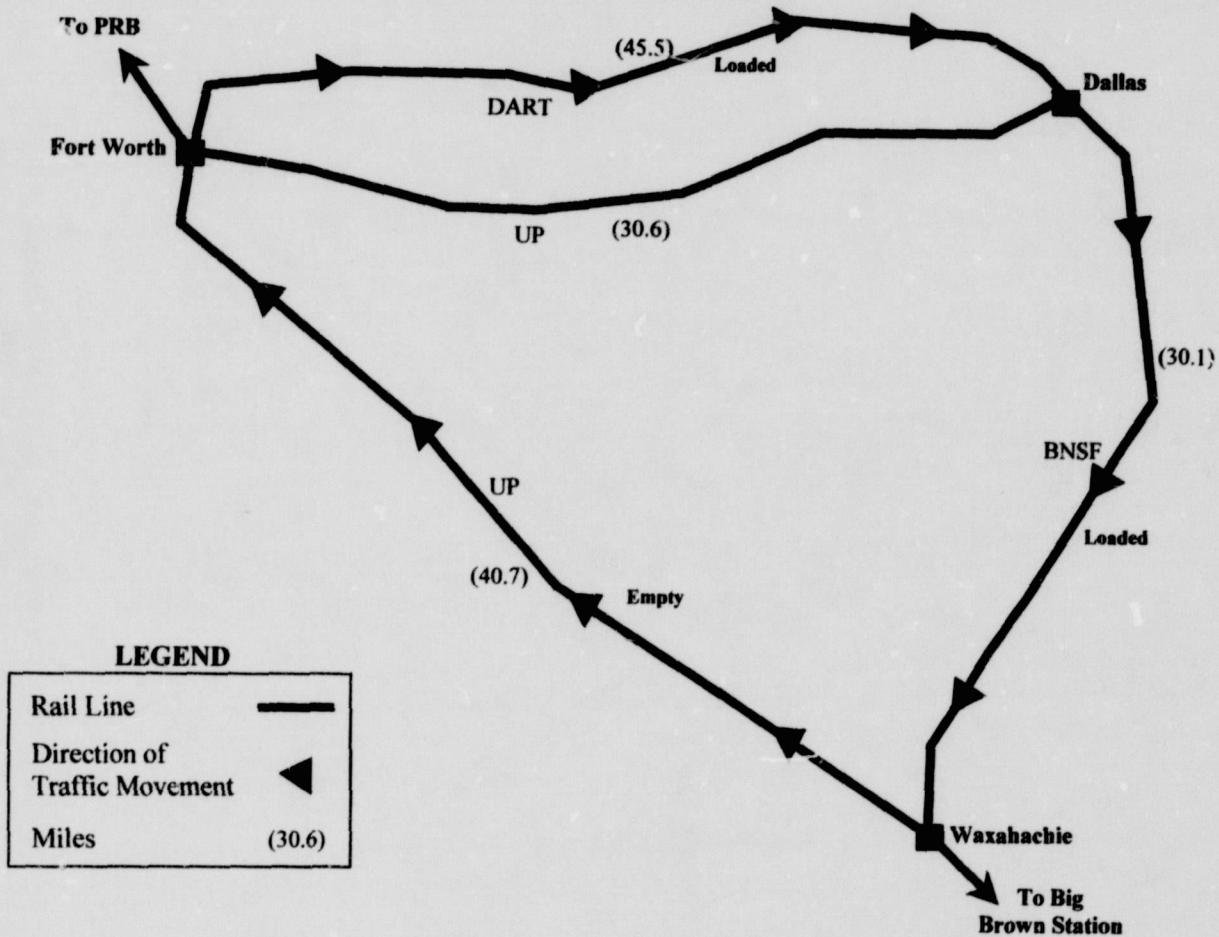
<sup>3</sup> TU Electric notes that UP/SP's institution of directional running schemes in the Dallas-Fort Worth-Houston rail corridor is a direct result of this merger, as well as UP/SP's efforts to ease congestion in the Houston/Gulf Coast area through restructuring of its Texas operations. See, e.g., UP/SP Railroad Merger Application, Vol. 3, V.S. King/Ongerth at 43, 126-28 (Nov. 30, 1995).



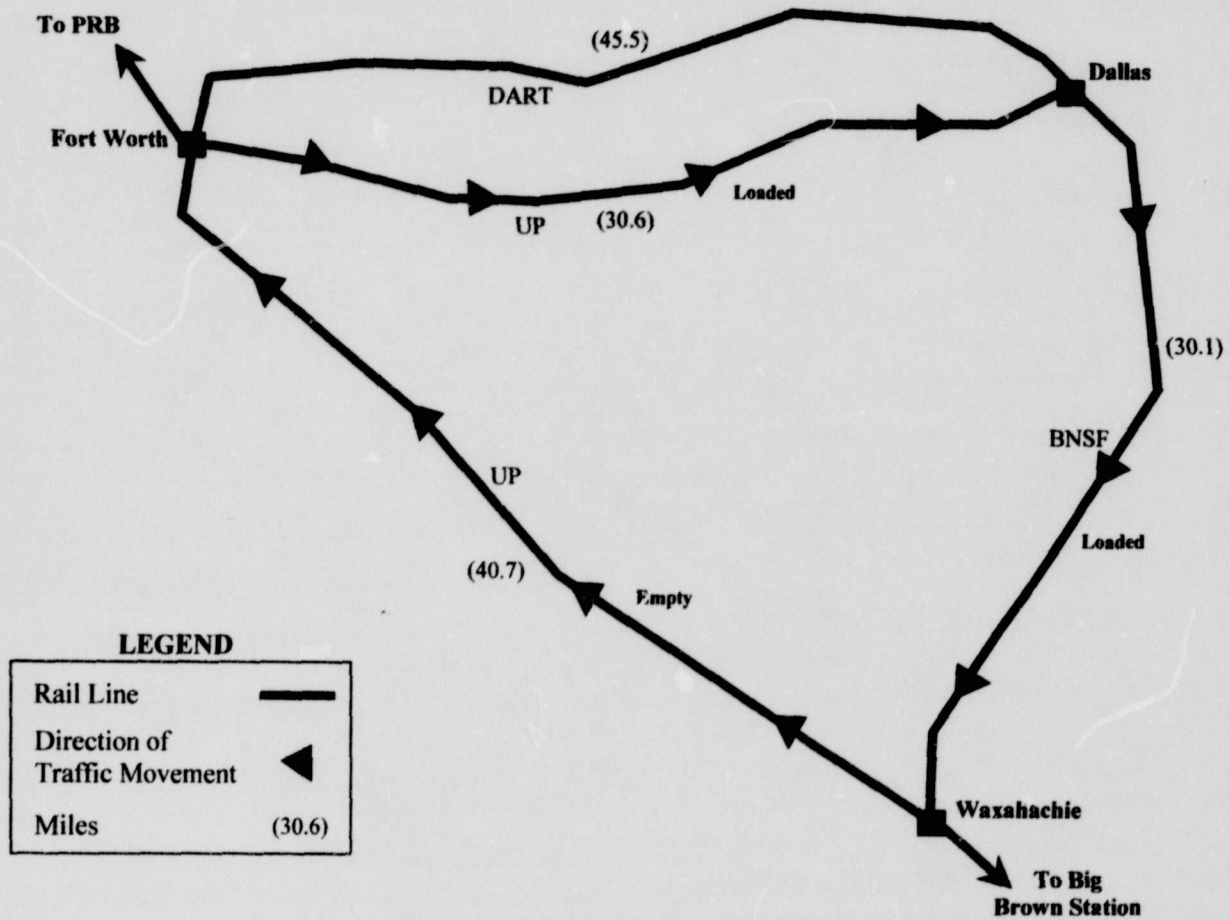
**Schematic of BNSF's Movement Between Fort Worth and Waxahachie  
Using Trackage Rights Over UP and Assuming UP's Bi-directional Operation**



**Schematic of BNSF's Required Detour Over DART  
Assuming UP's Directional Running From Waxahachie to Fort Worth**



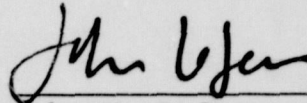
**Schematic of BNSF's Potential Movement Using  
Requested Trackage Rights Over UP Between Fort Worth and Dallas**





**CERTIFICATE OF SERVICE**

I hereby certify that this 14th day of December, 1998,  
I have caused a copy of the foregoing Summary of Texas Utilities  
Electric Company's Position in Support of BNSF's Remedial Condi-  
tion No. 6 to be served via first-class mail, postage-prepaid,  
upon all parties of record to this proceeding.

A handwritten signature in cursive script, appearing to read "John LeSeur", written over a horizontal line.

John H. LeSeur

STB FD 32760 (Sub 26) 12-14-98 D 192701



DONELAN CLEARY  
WOOD & MASER, P.C.

192701

ENTERED  
Office of the Secretary

DEC 15 1998

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Public Record

May 28, 1998



Via Hand Delivery

Vernon A. Williams, Secretary

Case Control Unit

ATTN: STB Finance Docket No. 32760 (Sub-No. 26)

Surface Transportation Board

1925 K Street, N.W.

Washington, DC 20423-0001

Re: STB Finance Docket No. 32760 (Sub-No. 26)  
*Union Pacific Corporation, et al.,--Control and Merger--*  
*Southern Pacific Rail Corporation, et al.*  
*Houston/Gulf Coast Oversight*

Dear Secretary Williams:

Earlier today this office filed a *Summary of Oral Argument in Support of Dow's Request for Additional Conditions* in the above-referenced proceeding. We inadvertently omitted the Certificate of Service from the copies that were submitted to the Board. However, copies of that filing (including the Certificate of Service) were served on all parties of record in the proceeding.

Enclosed are an original and twenty-five copies of the Certificate of Service which should have accompanied the filing. Please accept these and attach them to the Summary of Oral Argument described above.

We regret the oversight.

Sincerely yours,

Susan B. Urban  
Paralegal

Enclosures


cc: All parties of record

ATTORNEYS AND COUNSELORS AT LAW

1100 New York Avenue, Suite 750, N.W., Washington, D.C. 20005-3934, Tel: 202-371-9500, Fax: 202-371-0900

## CERTIFICATE OF SERVICE

I hereby certify that I have on this fourteenth day of December, 1998, served one copy of *SUMMARY OF ORAL ARGUMENT IN SUPPORT OF DOW'S REQUEST FOR ADDITIONAL CONDITIONS* by regular U.S. mail, postage prepaid, upon each of the parties of record, in accordance with the Board's rules of practice.

  
Susan B. Urban

STB FD 32760 (Sub 26) 12-14-98 D 192697



192697

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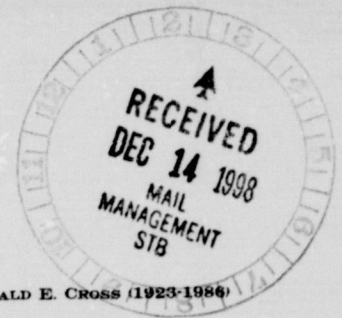
BRIAN L. TROLANO

ROBERT A. WIMBISH

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Office of the Secretary

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DONALD E. CROSS (1923-1986)

December 14, 1998

Hon. Vernon A. Williams  
Secretary  
Surface Transportation Board  
1925 "K" Street, N.W.  
Washington, D.C. 20423-0001

RE: STB Finance Docket No. 32760 (Sub-Nos. 26 ~~and 29~~),  
Union Pacific Corp., et al. -- Control and Merger --  
Southern Pacific Corp., et al.

[Houston/Gulf Coast Oversight]

Dear Secretary Williams:

In a filing submitted this morning in the above-captioned proceeding, the undersigned (counsel for the Brownsville & Rio Grande International Railroad -- "BRGI") inadvertently omitted his address and telephone number from the signature page of that document.

To address this omission, counsel for BRGI submits herewith an original and twenty five copies of the revised signature page, which includes the business address and phone number of BRGI's counsel.

Sincerely,

Robert A. Wimbish

Robert A. Wimbish

Counsel for Brownsville & Rio Grande  
International Railroad

Enclosure

cc: All parties of record

BRGI is grateful to the Board for permitting BRGI the opportunity to present this written argument summary. We urge the Board to act expeditiously to implement those conditions, including those discussed in this argument summary, that not only foster the full measure of rail competition originally anticipated at the time the Board approved the UP-SP merger but also promote the most efficient transport of railroad traffic through international gateways.

Respectfully submitted,

Robert A. Wimbish

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(202) 785-3700

Counsel for the Brownsville & Rio Grande  
International Railroad

**CERTIFICATE OF SERVICE**

I hereby certify that I have, this 14th day of December, 1998, served a copy of the foregoing document upon all parties of record by means of first class mail, postage prepaid.

Robert A. Wimbish

Robert A. Wimbish

STB FD 32760 (Sub 26) 12-21-98 D 192764

192764

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December 21, 1998

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**BY HAND**

ENTERED  
Office of the Secretary

DEC 21 1998

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Honorable Vernon A. Williams  
Secretary  
Surface Transportation Board  
Room 711  
1925 K Street, N.W.  
Washington, D.C. 20423-0001

Re: Finance Docket No. 32760 (Sub-No. 26)  
and Related Sub-Dockets

Dear Secretary Williams:

This responds to the letter of December 16 from Mr. Mullins, counsel for KCS, to the Chairman. Continuing a pattern of reckless, false assertions (e.g., his assertion in reply at Tuesday's oral argument that the record does not contain studies proving that UP rates have fallen since the merger, when the record is perfectly clear that such studies are contained in Exhibit E to our annual oversight filings), Mr. Mullins asserts in this letter that "UP's counsel seemed to know the scope and extent" of negotiations between BNSF and Tex Mex, "mentioning it [sic] several times." This is absolutely false. I first learned of such negotiations from Mr. Weicher's statement at the oral argument, and I responded with a categorical "No" to a specific question from the Chairman as to whether UP was involved in such negotiations. I, and UP, have no knowledge of such negotiations other than what Mr. Weicher said at the oral argument. Nor, secondarily, did I mention them "several times," as Mr. Mullins says; I mentioned them once, in explaining why, contrary to Mr. Weicher's suggestion, the existence of any such negotiations provided no basis for deferring decision on BNSF's Laredo trackage rights request.

Sincerely,

*Arvid E. Roach*  
Arvid E. Roach II

Attorney for Union Pacific  
Railroad Company

cc: Hon. Linda J. Morgan  
Hon. Gus A. Owen  
All Parties of Record



STB FD 32760 (Sub 26) 12-q-98 D 192459

152455  
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Office of the Secretary  
Case Control Unit  
ATTN: STB Finance Docket No. 32760 (Sub-No. 26)  
Surface Transportation Board  
1925 K Street, NW  
Washington, DC 20423-0001

December 1, 1998

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214 740 4000

43 BROOK ST  
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44 71 355 3330

Re: STB Finance Docket No. 32760 (Sub-No. 26), Union Pacific Corporation et al.--Control and Merger--Southern Pacific Corporation et al. [Houston/Gulf Coast Oversight]

Dear Mr. Secretary:

In accordance with Decision No. 7, served November 23, 1998 in this proceeding, Capital Metropolitan Transportation Authority ("CMTA") hereby notifies the Board that it intends to participate in the oral argument scheduled for December 15. CMTA understands that as a party having requested affirmative relief, it will be allotted 5 minutes of time for argument.

Copies of this document have been served upon all parties of record, and also on Administrative Law Judge Grossman.

Thank you for your attention to this matter.

Very truly yours,

Bracewell & Patterson, L.L.P.



Albert B. Krachman  
Attorney for Capital Metropolitan  
Transportation Authority

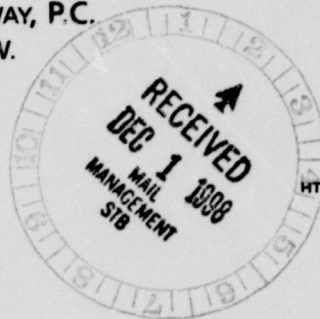


STB . FD 32769 (Sub 26) 12-1-98 D 192458

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December 1, 1998

Office of the Secretary  
Case Control Unit  
ATTN: STB Finance Docket No. 32760 (Sub-No. 26)  
Surface Transportation Board  
1925 K Street, NW  
Washington, DC 20423-0001

ORIGINAL

Re: STB Finance Docket No. 32760 (Sub-No. 26), Union Pacific Corporation et al.--Control and Merger--Southern Pacific Corporation et al. [Houston/Gulf Coast Oversight]

Dear Mr. Secretary:

In accordance with Decision No. 7, served November 23, 1998 in this proceeding, Formosa Plastics Corporation, U.S.A. (FPC) hereby notifies the Board that it intends to participate in the oral argument scheduled for December 15. FPC understands that as a party having requested affirmative relief, it will be allotted 5 minutes of time for argument, although FPC may, at argument, request the Board to permit FPC to reserve some of its allotted time for rebuttal argument.

Copies of this document have been served upon all parties of record, and also on Administrative Law Judge Grossman.

Thank you for your attention to this matter.

Sincerely,

Andrew P. Goldstein  
Attorney for Formosa Plastics  
Corporation, U.S.A.

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STB FD 32760 (Sub 26) 12-14-98 D 192692

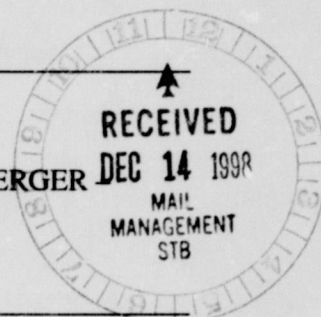
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BEFORE THE SURFACE TRANSPORTATION BOARD

FINANCE DOCKET NO. 32760 (SUB-NO. 26)

UNION PACIFIC CORPORATION, ET AL - CONTROL AND MERGER  
SOUTHERN PACIFIC RAIL CORPORATION, ET AL)

[HOUSTON/GULF COAST OVERSIGHT]



SUMMARY OF ORAL ARGUMENT

by

E. I. DUPONT DE NEMOURS AND COMPANY

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DEC 14 1998

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*[Handwritten signature]*

William A. McCurdy, Jr.  
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DuPont Legal  
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Frederic L. Wood  
Donelan, Cleary, Wood & Maser, P.C.  
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Due Date and Dated: December 14, 1998

BEFORE THE SURFACE TRANSPORTATION BOARD

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FINANCE DOCKET NO. 32760 (SUB-NO. 26)

UNION PACIFIC CORPORATION, ET AL – CONTROL AND MERGER –  
SOUTHERN PACIFIC RAIL CORPORATION, ET AL)

[HOUSTON/GULF COAST OVERSIGHT]

---

SUMMARY OF ORAL ARGUMENT  
by  
E. I. DUPONT DE NEMOURS AND COMPANY

---

December 15, 1998

---

INTRODUCTION

DuPont is a \$45 billion diversified chemical and energy corporation with over 200 manufacturing sites and almost 100,000 employees worldwide. Rail transportation is critical to DuPont's domestic and export business, and is for many of our chemical products the only safe and practical mode of transportation.

At DuPont, we believe that *safe, reliable, and efficient transportation at a competitive cost is essential to our business success*. Indeed, DuPont's principal core value is safety.

DuPont further believes that the best way to ensure this safe, reliable, and efficient transportation is through a fully *competitive, privately-owned and operated, market-based, and financially sound* transportation industry. Effective competition is a key driver to improved service and quality, as has been proven in countless other industries.

However, *where failure of the system occurs, some level of government intervention may be required* to restore the competitive balance. The railroad service crisis in the Houston/Gulf Coast area over the past year was such a situation.

DuPont has a major manufacturing facility at LaPorte, Texas. The facility ships over 3,000 rail cars each year, most of which contain hazardous materials which have no other



practical alternative means of transportation. This facility is located on the south side of the Houston Ship Channel. This plant is directly served only by the Union Pacific Railroad. While DuPont has always placed great value on its relationship with the UP, the events of the last year have highlighted for DuPont the importance of effective competition in ensuring the high-quality transportation service that DuPont and its customers must have.

### **HOW COMPETITION CAN BE MADE EFFECTIVE AT DUPONT LAPORTE**

There are two aspects of the situation at DuPont's LaPorte plant that need to be addressed in order to provide and restore the competition that previously existed. First, the exclusive access to the plant currently enjoyed by UP must be replaced with access by the Port Terminal Railroad Association and all of its connecting lines. Second, the existing unjustified limitations placed by UP on reciprocal switching needs to be removed.

The LaPorte plant is located at the former Southern Pacific (SP) rail station of Strang, Texas. Switching to and from the plant has been provided exclusively under terms of an October 31, 1961, multiple carrier operating agreement called the South Side Joint Track Agreement. As approved by the ICC, the agreement opened almost all of the surrounding area to access by the PTRRA and its member railroads, except for the DuPont plant, which is the only plant that is now excluded.

Much has changed in the nearly forty years since that agreement was approved. The effect of those changes has been to concentrate market power in the hands of the UP. The deleterious effects of that concentration were powerfully brought home to DuPont during the 1997-1998 service crisis. That concentration has made it extremely difficult for DuPont to avoid the adverse effects of such service disruptions.

The changes that have occurred since the approval of the 1961 agreement, taken together, have tipped the balance far in favor of the rail carrier, UP, with its exclusive right to directly serve DuPont's LaPorte plant. The Staggers Act has had the effect of limiting the ability of shippers to obtain meaningful and prompt regulatory relief. The number of line

haul carriers serving the greater Houston area has decreased from six to just two, with the merger of UP and Southern Pacific constituting the final step. In the course of approving that merger, the Board provided for limited access by the Texas Mexican Railroad to certain traffic in the Houston area, without clearly specifying which shippers would be served by the Tex Mex. In the course of implementing its acquisition of SP, UP has limited reciprocal switching access at the LaPorte plant to Burlington Northern Santa Fe. This violated the long-established provision of access to all line-haul carriers that was maintained by SP. When the service crisis burst upon the Houston area, UP was utterly unable to provide effective and efficient access even to the BNSF. DuPont's pleadings in the record provide the details of this inability, as well as the similar problems with DuPont's efforts to utilize the Tex Mex during the period when the service order was in effect.

The current situation is intolerable and future solutions must be found if DuPont is to remain competitive at LaPorte. Such a solution was recommended by DuPont in its prior submissions. The solution is in two parts. The first part is to authorize the PTRA to provide neutral switching service to DuPont's LaPorte plant in connection with all line-haul carriers serving Houston. The second part is to direct UP to provide reciprocal switching access at La Porte to all line-haul carriers that serve Houston, now or in the future. Thus, if Tex Mex, or any other carrier, obtains new or expanded access to the Houston area, DuPont's LaPorte plant will be able to realize the benefits of such service just like all the other shippers in Houston. These proposed solutions will not only protect DuPont's competitive position, but will serve important public and environmental interests by insuring that hazardous chemical products can always be moved quickly and safely through the Houston area.

## **DUPONT SEEKS A SPECIFIC AND APPROPRIATE REMEDY**

The remedy DuPont seeks is discrete, narrow, and limited. DuPont does not seek broader competitive access than already exists, nor does it wish to cause any economic harm to UP. DuPont seeks only the ability to control its own destiny through more effective use of rights and alternatives that already exist. DuPont respectfully seeks the following remedies:

1. Remove the restriction prohibiting PTR A from serving the DuPont LaPorte Plant;
2. Order Union Pacific and PTR A to work out a mutually acceptable service plan for the facility;
3. Order Union Pacific, if not done voluntarily, to restore DuPont's unrestricted reciprocal switching options;
4. Remove the obsolete restriction which prohibits reciprocal switching for intrastate transportation; and
5. Authorize the Tex Mex to permanently retain the right to access Houston customers served by HBT's successors, PTR A, and industries open to reciprocal switching on the UP.

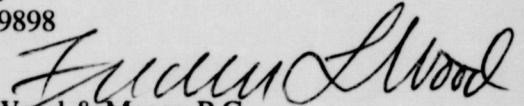
Should the Board, in its wisdom, choose not to order the foregoing remedies to allow the competitive market to address DuPont's safety and service issues, DuPont then requests the Board alternatively order Union Pacific to meet with BNSF, PTR A, and Tex Mex to develop and implement a plan to efficiently, effectively and directly interchange inbound and outbound rail cars for DuPont's LaPorte Plant where a carrier other than UP has the linehaul. The Board should also direct UP, if necessary, to restore unrestricted interstate reciprocal switching for DuPont. Such a ruling would at least allow DuPont to exercise its privilege of reciprocal switching options on interstate traffic.



Respectfully submitted,

William A. McCurdy, Jr.  
Logistics & Commerce Counsel  
DuPont Legal  
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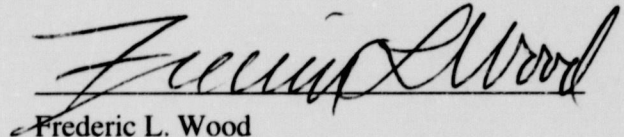
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Tel.: (202) 371-9500  
E-Mail: r.wood@dcwm.com



Due Date and Dated: December 14, 1998

CERTIFICATE OF SERVICE

I hereby certify that I have this 14th day of December, 1998, served a copy of the foregoing summary of oral argument on all known parties of record by first-class mail, in accordance with the Rules of Practice.



Frederic L. Wood

STB FD 32760 (Sub 26) 12-14-98 D 192693

192693

# MAYER, BROWN & PLATT

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December 14, 1998

## Hand Delivery

The Honorable Vernon A. Williams  
Secretary  
Surface Transportation Board  
1925 K Street NW  
Room 711  
Washington, DC 20423-0001



Re: Finance Docket No. 32760 (Sub-Nos. 26-~~32~~7)

Dear Secretary Williams:

As I advised your office, there was a last minute processing problem which arose as we were preparing BNSF's Summary of Oral Argument in Support of Requests for Additional Remedial Conditions in this proceeding. We have corrected that problem, and BNSF's filing is now complete. Accordingly, we request leave to file BNSF's Summary of Oral Argument and apologize for any inconvenience this delay may have caused.

Please contact me at (202) 778-0630 if you have any questions. Thank you for your assistance.

Sincerely yours,

Adrian L. Steel, Jr.



192693

# MAYER, BROWN & PLATT

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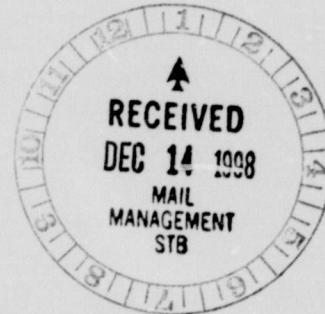
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December 14, 1998

## Hand Delivery

The Honorable Vernon A. Williams  
Secretary  
Surface Transportation Board  
1925 K Street NW  
Room 711  
Washington, DC 20423-0001



Re: Finance Docket No. 32760 (Sub-Nos. 26-32)

Dear Secretary Williams:

Enclosed for filing in the above-captioned proceeding are the original and twenty-five (25) copies of the Summary of BNSF Oral Argument in Support of Requests for Additional Remedial Conditions (BNSF-12). Also enclosed is a 3.5-inch disk of such filing in WordPerfect 6.1 format.

I would appreciate it if you would date-stamp the enclosed extra copy of this filing and return it to the messenger for our files.

Sincerely,

*Erika Z. Jones*  
Erika Z. Jones

Enclosures

cc: Parties of Record

CHICAGO BERLIN CHARLOTTE COLOGNE HOUSTON LONDON LOS ANGELES NEW YORK WASHINGTON  
INDEPENDENT MEXICO CITY CORRESPONDENT: JAUREGUI, NAVARRETE, NADER Y ROJAS  
INDEPENDENT PARIS CORRESPONDENT: LAMBERT ARMENIADES & LEE

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Office of the Secretary

BNSF-12

DEC 14 1998

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Public Record

BEFORE THE  
SURFACE TRANSPORTATION BOARD

---

Finance Docket No. 32760 (Sub-Nos. 26-~~32~~)

UNION PACIFIC CORPORATION, UNION PACIFIC RAILROAD COMPANY  
AND MISSOURI PACIFIC RAILROAD COMPANY

-- CONTROL AND MERGER --

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

[Houston/Gulf Coast Oversight]

---

**SUMMARY OF BNSF ORAL ARGUMENT IN SUPPORT  
OF REQUESTS FOR ADDITIONAL REMEDIAL CONDITIONS**

---

**INTRODUCTION**

In accordance with Decision No. 7 in this proceeding, The Burlington Northern and Santa Fe Railway Company ("BNSF") submits this summary of oral argument in support of its July 8, 1998 request that the Surface Transportation Board (the "Board") impose several additional remedial conditions of limited scope regarding the operations of BNSF on its trackage rights in the Houston/Gulf Coast area.

BNSF is requesting only that the Board fine-tune the rights it has already granted BNSF. Board action will enable BNSF to provide competitive, reliable service over the long term in the Houston/Gulf Coast area as a replacement for SP; preserve the efficacy of the rights granted BNSF, especially in the face of the adverse impact UP's service

crisis has had on BNSF over the past eighteen months; allow BNSF to adjust as UP continues to make far-reaching changes in its operational plans; and diminish the chance of a future service crisis in the Houston/Gulf Coast area. BNSF is not seeking new access to any shippers.

## **BACKGROUND**

Following the announcement of the UP/SP merger, BNSF and UP negotiated a settlement agreement which, as supplemented by the CMA Agreement and modified by the Board in Decision No. 44 (the "Settlement Agreement"), was intended to preserve competition for "2-to-1" and other shippers who otherwise would have lost competitive service as a result of the merger. The Settlement Agreement provided BNSF with a variety of trackage, haulage and other rights which, based on the reasonable expectations held by BNSF and others at that time, were thought to be sufficient to enable BNSF to be an effective post-merger competitor to UP for the business of such shippers. The Board identified the fact that "[s]hippers now served by SP, whose service is threatened by that carrier's decline, will now be assured of quality service by UP/SP or BNSF" as one of the "public benefits" resulting from the Board's approval of the conditioned merger. Decision No. 44 at 108 (emphasis added). As the Board has often recognized, the ability to provide quality service is a key component of a carrier's ability to compete.

Even absent the UP's service crisis, it would have been remarkable had the Settlement Agreement not required some fine-tuning given the complexity of rail operations in Houston and south Texas and the combination of UP and SP operations.



Indeed, the Board retained rights to oversee the implementation of the Settlement Agreement for precisely this reason. See Decision No. 44 at 146.

Of course, UP's service problems and its extensive operational responses to those problems have directly and negatively impacted the efficacy of BNSF's rights. These impacts have to some extent been obscured by the temporary operating rights granted BNSF and by the temporary migration to BNSF of traffic which UP simply could not serve during its crisis. UP had -- and retains -- an understandable incentive to adopt strategies and solutions which will solve its service-related problems, but many of those solutions will come at BNSF's expense unless the Board allows BNSF to synchronize its trackage and other rights with UP's revised operational plans. Therefore, the Board must take the long-view and act to preserve competition by approving the operational relief, modest in nature and surgical in scope, demonstrated by BNSF to be necessary to remedy the structural deficiencies in its current rights.

### **STANDARDS TO BE APPLIED**

In reviewing BNSF's request, the Board should recognize that changing circumstances and operations by UP require parallel changes in the operating rights BNSF received pursuant to the merger. BNSF should not have to be faced with the choice of paying UP for the right to adjust to UP's post-merger and post-service crisis operational decisions or of struggling endlessly to react to constantly changing operating conditions on the trackage rights lines in the future. However the issue is posed, Board action is necessary and critical to returning shippers to their pre-merger state of

competition by enabling BNSF to provide full and fair competition as a replacement for SP.

The first question for the Board to consider is the appropriate standard to apply to the various requests for additional remedial conditions. UP's proposed standard would effectively prevent the Board from making any modifications to the conditions adopted in Decision No. 44 as long as any level of post-merger competitive service is theoretically available to all "2-to-1" shippers. BNSF believes, to the contrary, that there are two distinct categories of requests pending before the Board and that a different standard should apply to each.

In the first category, some parties, like the Consensus Parties, request completely new competitive access. BNSF believes that the appropriate standard for those requests is the Board's traditional merger analysis. New competitive access should be granted only if: (1) the UP/SP merger is shown to have resulted in an actual loss of competitive options for shippers; (2) the conditions originally imposed in the merger decision have not effectively addressed the loss of pre-merger competitive options for identified shippers; and (3) the new conditions are narrowly tailored to address the identified competitive problem. To this end, BNSF agrees with UP that general arguments about "open access" do not belong in an oversight proceeding such as this -- and BNSF is, accordingly, not arguing that it should have new access to any shippers.

In a second, separate category are conditions, like those requested by BNSF, that would leave unaltered the basic competitive access structure, but which would modify specific limited operational rights in light of the lessons learned since implementation of



the UP/SP merger and unforeseen and unanticipated changes made by UP. The modifications sought by BNSF would:

- preserve certain of the temporary operating rights which BNSF has used to date in order to provide service that is competitive with UP's service and which have proven beneficial to both carriers (e.g., Caldwell-Flatonia-Placedo, Caldwell-Flatonia-San Antonio);
- limit the impact on BNSF's service capabilities of future changes in UP's operations (e.g., UP directional operations);
- respond to unanticipated and unilateral changes in UP's operating practices that have hampered BNSF's ability to provide consistent, reliable competitive service in place of the pre-merger SP (e.g., UP directional operations, neutral switching supervision, Taylor-Milano, access to clear routes through Houston Terminal);
- provide BNSF with the planning certainty necessary for it to enter into long-term contracts with shippers and to make the long-term investments necessary to serve those shippers (e.g., Caldwell-Flatonia-Placedo, Caldwell-Flatonia-San Antonio, Harlingen-Brownsville operations, Taylor-Milano); and
- forestall the need for the Board to micro-manage the steps which UP takes, today or in the future, to resolve service problems or to improve its services by adjusting BNSF's service rights to reflect UP's operations (e.g., UP directional operations).

As Professor Joseph Kalt explained in his Verified Statement submitted with BNSF's October 16, 1998 Rebuttal Evidence and Argument, the conditions BNSF requests should be imposed because they are reasonable and necessary to respond to: (1) operating circumstances unanticipated at the time of Decision No. 44; (2) identified deficiencies in the rights obtained by BNSF; (3) long-term incentives for UP to adopt operating policies which benefit it and, whether intentionally or not, harm BNSF's operations; and (4) the dependence of BNSF's competitive position on UP's changing and evolving operating decisions and practices. Indeed, Professor Kalt stated that any set of rights would, even absent a service emergency, likely have to be adjusted in light



of actual operating experience. The Department of Transportation ("DOT") also supports the pragmatic adjustment of existing rights, in light of current conditions, if "they would better enable competing railroads to offer the level of competition provided before the merger." DOT Comments at 2. Numerous shippers, shortlines and other entities have filed statements in this proceeding demonstrating their support of BNSF's requests for these same reasons.

BNSF's requested conditions would also serve to reduce the potential for a recurrence of the service problems experienced in Houston and south Texas. They are in the public interest and are supported by various parties which have a vital stake in preventing the recurrence of a rail service crisis.

BNSF's request for overhead trackage rights to Laredo should be imposed because such rights are reasonably necessary to respond to unanticipated service and related problems along the Alcoa route, unanticipated developments in the structure of the Mexican rail market, and the unwillingness or inability of Tex Mex, apparently due to KCS, to negotiate competitive long-term service arrangements with BNSF for Mexican traffic.

#### **UP OPPOSITION**

UP has opposed BNSF's requests on several grounds -- each of which is without merit.

First, UP's argument that BNSF is seeking open access to closed shippers is wrong as a matter of fact and should not sway the Board. None of BNSF's requested conditions would expand BNSF's access to shippers. Where shippers and shortlines

have themselves sought additional access to BNSF due to UP's inability to provide service, BNSF has simply fulfilled its duty to the Board by responding with information as to its ability to serve such applicants should the Board grant the shipper's request.

Second, the Board should reject UP's argument that BNSF's requests are unnecessary to preserve competition because BNSF has gained market share in some areas since the merger. Initially, as documented in BNSF's October 1, 1998 Quarterly Progress Report, BNSF continues to struggle to provide competitive service to customers along trackage rights lines and "2-to-1" service points where UP provides haulage or reciprocal switch services to originate or terminate BNSF trains. Moreover, it is impossible to parse BNSF's gains to determine which traffic gains are attributable to UP's service crisis, including traffic attracted because UP could not provide service, and which traffic gains are attributable to BNSF's long-term replacement of SP as a competitive alternative to UP. DOT makes this very point in its September 18 comments, expressing concern that the Board not mistake as evidence of competition the increased traffic levels on BNSF and Tex Mex which "may well have been influenced by the terms of the Board's Emergency Service Order No. 1518\* \* \*" or by UP service reaching "a point where shippers that were able to switch traffic from UP probably did so." DOT Comments at 5-6. Furthermore, UP will try to recapture and increase its market share, adopting operational procedures that will enhance its competitive position even if they adversely impact BNSF's position.

Third, UP's argument that BNSF is seeking Board intervention and assistance in the renegotiation of the rights previously bargained for in the Settlement Agreement is

without merit. BNSF fully believed at the time it negotiated its rights under the Settlement Agreement that those rights would be adequate to provide the desired level of service and expected competition following the merger, based upon BNSF's understanding of UP's operating plans for the combined properties. Even absent UP's service problems, it is likely that some adjustment of the negotiated rights would have been necessary. Moreover, no one anticipated the scope and duration of the service crisis which UP would face as it merged its operations with those of SP. Nor did anyone anticipate the massive structural changes UP would make in its combined operations in an effort to resolve the congestion and service problems at Houston and along the Gulf Coast, including the adoption of what UP itself has characterized as perhaps "the most extensive change in rail operations in American rail history" -- directional running over many key routes, including those shared by BNSF as a result of the Settlement Agreement. Further, when CMA and other parties raised concerns about directional operations in the Houston to Memphis corridor during the merger proceeding, changes were made to ensure that BNSF would be able to operate and compete efficiently in the corridor by allowing it to join UP's directional operations. Now that UP has commenced such directional operations elsewhere as a result of the merger and the service crisis, BNSF should be able to join those operations as well.

As UP makes changes to its operations along lines over which BNSF has trackage rights, it is imperative that the changes not have a discriminatory or adverse impact on the quality of service that BNSF, as a tenant, can provide as a competitor to the incumbent UP. BNSF already negotiated in good faith for adequate trackage rights



that would enable it to provide an effective level of competition to customers who would have otherwise lost access to competition at "2-to-1" and other points. BNSF should not be "estopped" from providing an adequate level of competition post-merger to rail shippers by its failure to predict various developments, like the service crisis, and UP's operational responses to those developments. More importantly, shippers should not be precluded from receiving effective two carrier competitive service by such developments and UP's responses.

Fourth, UP's argument that BNSF is seeking remedial conditions that will add to pre-merger competition, not preserve the pre-merger level of competition, is factually inaccurate. BNSF has not made this argument and is not seeking access to a single new shipper. As the map attached hereto shows, in those instances where BNSF is requesting additional permanent trackage rights in order to address operational concerns, the rights are over routes identical to those used by SP to provide competition to UP before the merger.

Fifth, UP's argument that granting BNSF's requests would subject UP to financial risk and undermine UP's efforts to recover from the service crisis is premised on the mistaken theory that it is entitled to some minimum share of Houston-area traffic and some guaranteed revenue level. While other parties' requested conditions might increase UP's financial risks significantly by creating a system of open access, BNSF's requested conditions would only enable BNSF to compete on the same basis that SP competed pre-merger for the business of "2-to-1" and other shippers whose business has

already been opened to BNSF. BNSF's proposal would do no more than preserve the competitive options of shippers, consistent with the goal of Decision No. 44.

Finally, the standard for review proposed by BNSF is consistent with the Board's views, expressed in its decision to retain oversight authority for five years after the merger. Economic theory also dictates that the Board respond to UP's evolving operational decisions to ensure that the remedial conditions similarly evolve in a manner that protects competitive opportunities for shippers.

Respectfully submitted,

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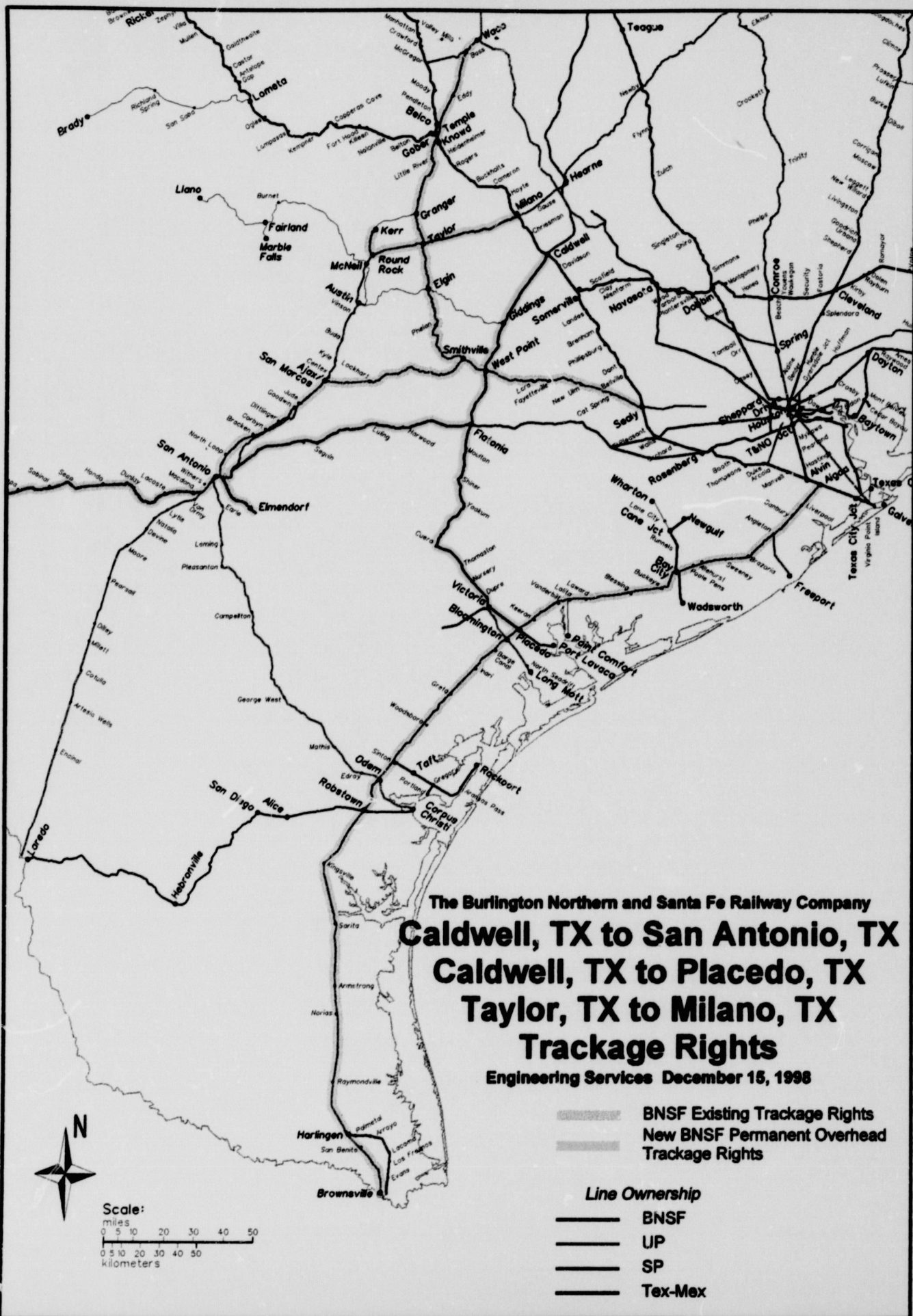
December 14, 1998

**CERTIFICATE OF SERVICE**

I do hereby certify that a copy of the foregoing Summary of BNSF Oral Argument In Support Of Requests For Additional Remedial Conditions (BNSF-12) is being served, by facsimile, on all participants in the oral argument listed in Appendix A to Decision No. 8 in this proceeding.

John J. A. A.





STB FD 32760 (Sub 26) 12-14-98 D 192689

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DOW-4

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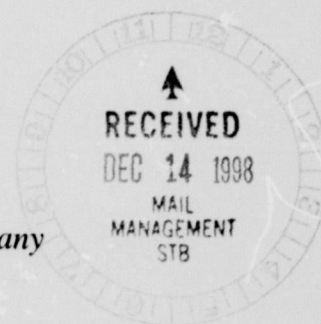
DEC 14 1998

Part of  
Public RecordBEFORE THE  
SURFACE TRANSPORTATION BOARD

Finance Docket No. 32760 (Sub-No. 26)

*Union Pacific Corporation, Union Pacific Railroad Company  
And Missouri Pacific Railroad Company**- Control And Merger -**Southern Pacific Rail Corporation,  
Southern Pacific Transportation Company, St. Louis  
Southwestern Railway Company, SPCSL Corp. And The  
Denver And Rio Grande Western Railroad Company**[Houston/Gulf Coast Oversight]***Summary of Oral Argument  
In Support of Dow's  
Request for Additional Conditions**

The Dow Chemical Company ("Dow") has requested two conditions in the Houston/Gulf Coast Oversight Proceeding. The first condition would grant The Burlington Northern and Santa Fe Railway Company ("BNSF") haulage rights from a new rail yard to be constructed by Dow and BNSF near Angleton, Texas to Dow's chemical and plastics production complex at Freeport, Texas. The second condition would permit Dow or BNSF to construct a build-in from a point on the Union Pacific ("UP") line between Angleton and Algoa, Texas to Freeport. This second condition cannot be granted without also imposing the first condition as an interim measure until the build-in can be constructed. The first condition, however, is feasible without granting the second condition. Both conditions would lead to the construction of additional





infrastructure in the Texas/Gulf Coast region that could help to alleviate the pressure upon the UP system that contributed heavily to the service crisis, which has lasted over a year at a cost of hundreds of millions of dollars to shippers.

The Board initiated this proceeding to determine whether there is any relationship between the market power gained by UP through its merger with the Southern Pacific Railroad ("SP") and the service crisis, and, if so, whether the situation should be addressed through additional remedial conditions. The merger has contributed significantly to the service crisis by consolidating much of the critical rail infrastructure needed to serve shippers in the Texas/Gulf Coast region, particularly chemicals and plastics shippers, in a single rail carrier, the UP. This left shippers with no rail infrastructure alternative – a "safety valve" – when UP's service deteriorated, thus prolonging and intensifying the effects of the crisis.

Prior to their merger, UP and SP were the major rail carriers in the Texas/Gulf Coast region. Although the Board attempted to preserve rail competition by granting BNSF access to UP's infrastructure to compete at "2-to-1" points, BNSF lacked an extensive infrastructure of its own. Instead, it was compelled to compete over UP's lines and was dependent upon much of UP's infrastructure. Thus, when the UP suffered its unprecedented breakdown in service, BNSF inevitably was affected too. This precluded BNSF from acting as a competitive "safety valve" even for "2-to-1" shippers who otherwise could shift their traffic off of the UP system. If enough shippers had had alternatives to the UP system, the service crisis would have been less severe in scope and duration.

In addition, by granting BNSF access primarily to "2-to-1" shippers, the Board did not give BNSF a traffic base that resembled the former SP's traffic base in any substantial way. Without a larger traffic base, BNSF has had relatively little incentive to invest in its own infrastructure in the Texas/Gulf coast region that would be independent of the UP's infrastructure.

In Decision No. 1 in this proceeding, the Board itself recognized that a lack of infrastructure played a significant role in the service crisis. It is incumbent upon the Board then to provide the rail industry with the ability and incentive to remedy this situation.

Part of the solution to this problem is to construct additional infrastructure in the Texas/Gulf Coast region and to have more of it under the control of BNSF. Dow's proposed conditions would do just that. Because Dow at Freeport is one of the largest volume shippers in the region, the Freeport rail traffic would go a long way towards enhancing BNSF's potential traffic base. That traffic alone would justify certain additions to the rail infrastructure in the region. Moreover, BNSF and Dow have agreed to construct a new rail yard near Angleton, Texas if Dow's first condition is granted and that could grow into a full scale build-in if the second condition also is granted. This new infrastructure could be used by BNSF to serve other shippers in the area and it would remove some of the pressure from the UP infrastructure. Furthermore, Dow's conditions would make minimal use of UP's existing infrastructure, thereby insulating it to a greater degree from future UP service problems.

Dow would contribute funds toward the construction of a portion of this infrastructure. This would increase the total pool of money available for the \$1.4 billion in infrastructure additions and enhancements that UP itself has said is necessary to remedy the current infrastructure deficiencies on its rail system. Moreover, to the extent BNSF has sufficient incentive to make these infrastructure investments, its service will be less susceptible to future disruptions on the UP system.

Throughout this proceeding, the UP has argued that its improving service levels render the purpose of this proceeding moot. The purpose of this proceeding, however, never has been to solve UP's service crisis. That was the purpose of Service Order No. 1518. The purpose of this proceeding is to address the underlying causes of the service crisis, to the extent they are connected to the merger, and to develop conditions that would alleviate those causes so that similar crises do not reoccur. The Board can do that by granting Dow's Request for Additional Conditions.



STB FD 32769 (Sub 26) 12-14-98 D 192690

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December 14, 1998

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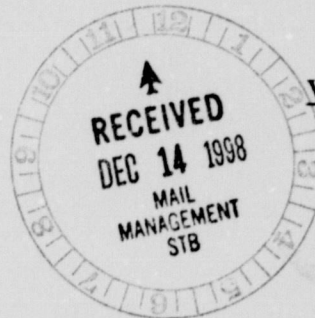
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The Honorable Vernon A. Williams  
Secretary  
Surface Transportation Board  
Case Control Unit  
1925 K Street, N.W.  
Washington, D.C. 20423-0001



Via Hand Delivery

Re: Finance Docket 32760 (Sub-No. 26), *Union Pacific Corp., et al.--*  
*Control and Merger -- Southern Pacific Rail Corp., et al.*

Dear Secretary Williams:

Enclosed for filing in the above-referenced proceeding are an original and twenty-five copies of Capital Metropolitan Transportation Authority's Summary of Argument in Support of Request for Limited Remedial Condition. Also enclosed is a 3.5 inch diskette that contains the text of this filing in WordPerfect 6.0 format.

I would appreciate your date-stamping the enclosed receipt copy of the filing and returning it with the messenger for our records.

Very truly yours,

Bracewell & Patterson, L.L.P.

*Albert B. Krachman*

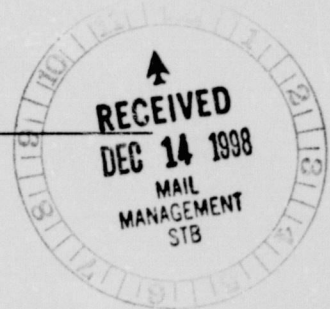
Albert B. Krachman

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**BEFORE THE  
SURFACE TRANSPORTATION BOARD**



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Union Pacific Corporation, Union Pacific	§
Railroad Company, and Missouri Pacific	§
Railroad Company -- Control and Merger	§
-- Southern Pacific Rail Corporation,	§
Southern Pacific Transportation Company,	§
St. Louis Southwestern Railway Company,	§
SPCSL Corp., and the Denver and Rio	§
Grande Western Railroad Company	§

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Finance Docket No. 32760  
(Sub-No. 26)

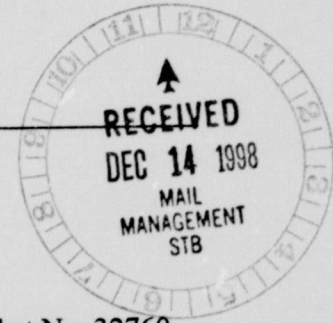
**CAPITAL METROPOLITAN TRANSPORTATION AUTHORITY'S  
SUMMARY OF ARGUMENT IN SUPPORT OF  
REQUEST FOR LIMITED REMEDIAL CONDITION**

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Transportation Authority



**BEFORE THE  
SURFACE TRANSPORTATION BOARD**



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Union Pacific Corporation, Union Pacific	§
Railroad Company, and Missouri Pacific	§
Railroad Company -- Control and Merger	§
-- Southern Pacific Rail Corporation,	§
Southern Pacific Transportation Company,	§
St. Louis Southwestern Railway Company,	§
SPCSL Corp., and the Denver and Rio	§
Grande Western Railroad Company	§

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Finance Docket No. 32760  
(Sub-No. 26)

**CAPITAL METROPOLITAN TRANSPORTATION AUTHORITY'S  
SUMMARY OF ARGUMENT IN SUPPORT OF  
REQUEST FOR LIMITED REMEDIAL CONDITION**

Pursuant to the Surface Transportation Board's ("the Board") Decision No. 8, Capital Metropolitan Transportation Authority ("CMTA" or "Capital Metro") hereby submits this Summary of Argument in Support of CMTA's Request for Limited Remedial Condition, CMTA-1, filed July 8, 1998 ("Request"). In that Request, Capital Metro asked the Board to grant the Burlington Northern Railroad Company and the Atchison, Topeka and Santa Fe Railway Company ("BNSF") an interchange with the Central of Tennessee Railway & Navigation Company, Incorporated d/b/a the Longhorn Railway Company ("Longhorn") at McNeil, Texas, and a 4.4 mile extension of BNSF's trackage rights from Round Rock to McNeil. As set forth in its Request and supporting documentation, the Limited Condition is necessary to save short line service in the Austin area, which is threatened by the market power UP obtained, and has abused, since the merger.

## **I. ARGUMENT**

### **A. SHORT-LINE SERVICE IN THE AUSTIN AREA WILL NOT SURVIVE WITHOUT THE LIMITED CONDITION**

Approximately one million people live in the Austin metropolitan area, which is one of the fastest-growing metropolitan areas in the country. Longhorn Railroad is the only short-line operator in the area.

The Board's decision on this limited condition is very simply a decision to eliminate or preserve short-line service in the Austin area, because Longhorn cannot survive without access to BNSF at McNeil. It is already operating at a substantial loss and has lost many of its customers due to the merger-related difficulties on the Giddings-Llano. In addition, Capital Metro has no resources or ability to find or subsidize a replacement carrier.

### **B. THE LIMITED CONDITION IS NECESSARY TO EFFECTUATE THE BOARD ORDERED COMPETITION**

In decision No. 44, considering the 2-1 merger effects and premised on the assumption that competition at Elgin would be adequate, the Board ruled that CMTA could choose between Elgin and Giddings as such relief would put CMTA in the same position that it had been in before the merger.

However, due to the Houston area melt-down and certain concerted strategies by UP, CMTA never realized Board-ordered relief. UP/SP congestion south of Austin prevents BNSF through-trains from picking-up Longhorn traffic at Elgin, despite the fact that available BNSF through-trains at Elgin were a pre-supposition of adequate competition for the Giddings/Llano traffic. As a result,

only branchline service is provided by BNSF a meager two(2) times a week.<sup>1</sup> There is therefore no effective interchange at Elgin.

The effective unavailability of BNSF at Elgin due to the congestion south of Austin, the limited number of cars capable of being interchanged at Elgin and UP/SP service problems effectively eliminate all of UP/SP's competition for traffic on the Giddings/Llano, and make Longhorn completely dependent on UP/SP.

**C. THE LIMITED CONDITION SATISFIES THE PUBLIC INTEREST TEST AS SET FORTH IN 49 U.S.C. § 11102**

The ultimate issue is whether public interest in maintaining short-line shipper services in Austin outweighs Union Pacific's desire to avoid scheduling BNSF traffic over four miles of track. The question is not difficult to answer.

In its opposition UP did not dispute that the public interest test was operative and did not dispute that the public interest provisions of the terminal facility statutes applied here. Under 49 U.S.C. 11102, the Board is to apply a public interest test in deciding whether to grant a condition allowing a rail carrier to use the terminal facilities and mainline track of another. The public interest test is satisfied if the Board finds that it is practicable and in the public interest to grant the condition without substantially impairing the ability of the rail carrier owning the facilities or entitled to use the facilities to handle its own business.

An interchange at McNeil is in the public interest because it is the only way to ensure the survival of freight rail service on the Giddings/Llano. Without it, shippers west of Austin will be

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<sup>1</sup> Such service is provided by BNSF only when the station at Elgin is in operation. The station has in fact not been in use by Longhorn in recent months due to flooding, a subsequent derailment and a lost bridge. UP/SP has been helpful to Longhorn in overcoming some of its flood-related service problems.



forced to use trucks. This will be a tremendous expense to the shippers, endangering their businesses. This will also cause increased rock traffic on public highways.

It is also noteworthy that UP did not controvert Capitol Metro's showing that extending these track rights would alleviate Houston area congestion, a major focus of this proceeding.

There is no serious question but that the public harm through loss of short-line service in Austin would be tremendous. Much has been written in the press recently about an apparent concerted strategy by UP to squeeze out short-line railroads because they pose administrative and limited financial burdens on UP. Austin should not be a victim of this policy.

UP asserts that there would be operational difficulties in coordinating the BNSF interchange. UP is already coordinating thousands of miles of BNSF trackage rights, and to suggest that to do so over a 4.4 mile segment in central Texas, which features side track sufficient to hold 90 Cars, is simply not credible. UP could do this without difficulty.

While denying the condition would be a great source of harm, granting the condition would have the salutary effects of (1) furnishing the originally contemplated level of competition, (2) mitigating Houston area congestion and (3) preserving short-line shipper service in this area.

Sen. Hutchison's September 10, 1998 letter to the Board underscored the sensitivity of this issue to the Austin area and urged very careful review of Capitol Metro's position. Senator Hutchison urged this Board to act so as to preserve the flow of rail traffic in the area, which will certainly be compromised if the condition is not granted.

The Board should not harm the Austin economy, extinguish short-line service, and forgo an opportunity to alleviate Houston congestion, just to avoid at worst a minuscule inconvenience for

UP over 4.4 miles of track. No calculus of the harms could possibly support a decision to deny the condition.

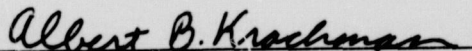
Finally, it is also clear that the Board would retain jurisdiction over this matter. Thus, if for any reason disruptions remotely similar to those protested by UP arose, the adequate remedy and mechanism to address lives.

## II. CONCLUSION

Granting this limited condition is essential to the public interest and to the survival of short-line freight train service in the Austin area. Reduced to its essentials, the nominal 4.4 miles of trackage rights CMTA seeks is the only condition standing between competitive line-haul rail service, and a monopoly for the merged UP/SP serving a metropolitan area with a million inhabitants. If this monopoly is allowed to continue, freight traffic on the Giddings/Llano line will not be able to continue due to economic impracticability.

For all these reasons, the Court should grant CMTA's Request for Limited Remedial Condition.

Respectfully submitted,



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Counsel for Capital Metropolitan  
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CERTIFICATE OF SERVICE

I certify that on this 14<sup>th</sup> day of December, 1998, a copy of the foregoing Summary of Argument in Support of Request for Limited Remedial Condition of Capital Metropolitan Transportation Authority was served by First Class Mail on the Parties designated on the list of participants attached to Decision No. 8.

Albert B. Krachman



STB FD 32760 • (Sub 26) 12-14-98 D 192691

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BY HAND

Honorable Vernon A. Williams  
Secretary  
Surface Transportation Board  
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Washington, D.C. 20423-0001

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Office of the Secretary

DEC 14 1998

Part of  
Public Record

Re: Finance Docket No. 32760 (Sub-No. 26)  
and Related Sub-Dockets

Dear Secretary Williams:

Enclosed is an original and 25 copies of a summary of points that may be made by Union Pacific at the oral argument, together with a disk containing this material in WordPerfect 7.0 format. The actual content of UP's argument will depend on the questions posed by the Board, the matters addressed by other parties, and available time.

Sincerely,

Arvid E. Roach II

Attorney for Union Pacific  
Railroad Company

cc: All Parties of Record

DEC 14 1998

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SUMMARY OF ORAL ARGUMENT OF  
UNION PACIFIC RAILROAD COMPANY

The question to be decided here is whether the UP/SP merger should be permanently conditioned to add new competition that did not exist before the merger. That is contrary to decades of settled railroad merger law, and it is in no way justified by the Union Pacific service crisis of the past year, serious as that crisis was.

Let me begin by stressing three preliminary points:

The Service Crisis Is Over

*First*, the UP service crisis is over. The Board found on July 31 that the Houston/Gulf Service emergency had ended, and since then there has been much additional improvement:

- Houston yards have been operating smoothly for months. In fact, the most vital Houston yard, Englewood, is operating much more efficiently than before the merger, thanks to the yard specialization and directional running that the merger made possible.
- Texas and Louisiana car inventory has been in a normal range for months, as have sidings blocked south of Kansas City.
- The Houston terminal, and the entire Houston/Gulf region, is operating smoothly, in large part because of the success of the Spring Dispatching Center.
- Transit times for chemical shippers to key Eastern and Midwestern markets have been back to normal for months. The one remaining problem area, transit times to California, was solved in September.
- Switching for Houston/Gulf customers is back to, or better than, pre-merger levels. The shippers that we had been calling every day since April to check on local service have said: "Don't call us, we'll call you."



- Traffic has been moving smoothly across the Mexican border for months.
- UP is now exceeding its targets for moving rock traffic from south Texas quarries to the Houston area and other end markets. With the opening last month of a second track at New Braunfels, this service will improve still further.

- Last week, UP set a record for moving coal trains to Texas utilities, delivering 31 trains in a single week.

- UP is no longer the fragile railroad of a year ago, which could not handle external stresses without severe service problems. UP has coped with several incidents of severe flooding and washouts in recent months, each time with little disruption of service. This is a resilient railroad again.

The recovery is not limited to the Houston/Gulf area, but extends to the entire UP system:

- We are delighted to be able to announce that systemwide average train speed, which has been steadily increasing for months, is now in the area of 17 miles per hour, which is within the normal range.

- Systemwide car inventory is in the 320,000 range, a normal figure, and systemwide trains held and sidings blocked are normal.

- UP handled this year's rush of import containers in southern California -- which was at very high levels because of the attractiveness of Asian imports -- without a glitch.

- The much-predicted autumn grain service crisis never happened. The volume of grain traffic to Gulf ports has been high, but UP has handled it without difficulty. UP has allocated 300 locomotives to grain service, and is offering general-distribution grain hopper cars to its customers.

- UP has invested hundreds of millions of dollars to upgrade its Central Corridor lines, adding second main track in Iowa and third main in Nebraska.
- UP will have a record year in moving Utah and Colorado coal.
- UP has improved equipment supply and transit times for Pacific Northwest lumber and paper producers, opening up new domestic markets for firms faced with the collapse of Asian Rim demand for their products.
- Safety, both in the Texas/Gulf area and across the UP system, is at record levels.
- UP has hired thousands of new employees, in Texas and Louisiana and throughout the West.
- UP's state-of-the-art TCS computer system has now been installed on the entire SP for five months, and the difficult process of training and breaking in thousands of employees on its use is behind us.
- Learning an important lesson from adversity, UP has decentralized most operating functions to three regions, so that the personnel who best understand the problems can make the decisions.

I could go on, but the bottom line is clear: While UP service is far from perfect, and work continues to improve operations and efficiency, the service crisis has been overcome. UP is on course to realize more and more of the benefits of the merger, and achieve continuing improvement for its customers.

#### The Board's Emergency Powers

*Second*, we are absolutely not here to deny that the service crisis was severe, or that the Board acted properly in imposing an emergency service order to address it. The

relevant point for this proceeding, however, is that permanent merger conditions are not the way to deal with service emergencies. The Interstate Commerce Act addresses service emergencies in Section 11123, and gives the Board very broad powers to direct service and take other necessary measures. The Board did that in the Houston/Gulf crisis, and it was right to do so. It is now in the process of adopting rules that codify the rights of shippers and railroads to emergency remedies where service has sharply deteriorated, and that establish expedited procedures to vindicate these rights. Those are the proper remedies if any railroad ever faces another service crisis -- not permanent merger conditions, ostensibly aimed at a crisis that no longer exists.

UP's Openness to Constructive  
Steps to Improve Service

*Third*, while UP opposes the conditions that are sought here because they fail the fundamental tests for merger conditions, this does not mean that UP is not open to constructive measures that will promote service improvement in the Houston/Gulf area and elsewhere. During the service crisis, UP released shippers from contracts, opened new junctions, and worked with other railroads to reroute traffic. We reached an agreement, at great commercial cost, to bring BNSF into the Spring Center. And we have voluntarily agreed to several of the steps that were proposed as conditions here, including selling the Wharton Branch to Tex Mex, admitting Tex Mex and the Port of Houston to membership in the Port Terminal Railroad Association, adding more lines to the Spring Center, splitting one overtaxed dispatching territory at the Center into two territories, and allowing BNSF to use an alternative route in the Brownsville area until a bypass track is constructed.

UP will continue to be open to any reasonable proposal that will improve service and treat those involved fairly. The Board does not need to use the inappropriate vehicle of



compulsory, permanent merger conditions to bring about ongoing creative private initiatives in this regard.

\* \* \*

Let me turn, then, to the core issues in this case. The proposed conditions should be denied because they fail the tests the Board set forth in initiating this proceeding, tests that are grounded in bedrock railroad merger law. First, the merger, as conditioned by this Board, did not cause any increase in market power in the Houston/Gulf area. Second, the service crisis was not caused by any such (non-existent) increase in market power. And third, the proposed conditions would improperly force competition, by government fiat, where none was lost by the merger, and cause problems rather than prevent them.

I. THE MERGER DID NOT CAUSE AN INCREASE IN MARKET POWER

Experience has shown that the Board was correct in concluding that the merger, as conditioned, would not diminish competition.

For "2-to-1" traffic, a huge record from two annual oversight proceedings proves that the BNSF conditions have been effective. Rates for "2-to-1" traffic are down. BNSF has won large and constantly increasing amounts of traffic, approaching 50% of the total market it estimated in the merger case. BNSF's trackage rights volumes are already many times what Mr. Crowley, the expert presented by many of these same condition applicants in the merger proceeding, testified it could ever secure. Hundreds of concrete examples show that both the "2-to-1" shippers that awarded BNSF their traffic and the "2-to-1" shippers that responded to lower UP rates by giving UP their traffic have reaped significant benefits -- which is, of course, exactly how competition is supposed to work. The so-called "studies" of "2-to-1" traffic that KCS/Tex Mex improperly tried to introduce here as rebuttal are full of errors, and ignore the

shipper-by-shipper record of strong competition, the sworn testimony of shippers like Exxon that post-merger competition for "2-to-1" traffic has been very effective, and the reductions in rates for this traffic for two straight years.

For "3-to-2" traffic, too, rates are down and competition stronger. For example, the major auto makers, who make up the largest single "3-to-2" traffic segment, have all secured much-improved contracts post-merger. KCS/Tex Mex, while seeking access to "3-to-2" traffic in Houston, admit that they cannot justify that condition on the basis of any competitive harm to "3-to-2" traffic.

Source competition for chemicals is even stronger than predicted in the merger case, as shown by the new study presented in Mr. Peterson's testimony. Rates for chemicals are down. So are rates for grain.

Eastern Mexico gateway traffic is enjoying stronger competition. Rates are down, and UP's post-merger share is below its pre-merger share. BNSF is handling more traffic with Tex Mex via Laredo than SP did before the merger; and Tex Mex is handling still more traffic over its trackage rights to Beaumont, where it connects with its partner KCS. Tex Mex's overall share of Laredo traffic has nearly doubled.

Finally, the vague claims of Tex Mex and BNSF that UP "discriminates" in dispatching have been definitively disproven by objective electronic sensor readings which show that these railroads' trains actually have been receiving better treatment than UP's own trains on the trackage rights segments. This has continued to be the case in the three months since we filed our opposition evidence. These "discrimination" claims were always totally lacking in credibility, since UP's dispatching center was open to Tex Mex and BNSF from "Day

One," and agreed-upon Dispatching Protocols gave Tex Mex and BNSF effective remedies for any dispatching issue, which they never used.

II. THE SERVICE CRISIS DID NOT RESULT  
FROM ANY EXERCISE OF MARKET POWER

It is absurd to suppose that the service crisis resulted from an exercise of any market power. As Professor Hausman testified, UP would have to have been the most incompetent monopolist in history to have used its supposed "market power" to destroy its own service, lose nearly 10% of its traffic to its arch-competitor BNSF, and suffer a billion dollars in additional costs and three straight quarters of negative earnings.

KCS/Tex Mex, recognizing that they cannot meet the Board's test of market power causation, argue that it should be sufficient, as a predicate for merger conditions, for there to have been any relationship at all between the merger and the service crisis. Their suggestion seems to be that if UP had "controlled" less Houston traffic, the crisis might have been alleviated, and that this somehow justifies the permanent access conditions they are demanding. Not only does this argument misstate the law -- which requires proof of merger-caused harm, and not just some vague "relationship" between a merger and a problem -- but it is simply mistaken. In fact, UP exclusively serves only a third of Houston-area traffic. Moreover, as the Board specifically found in the service proceeding, the service crisis was a Houston-wide capacity crisis. The railroads involved, with the Board's help, took all possible steps to make the best use of the available infrastructure and route traffic away from congestion. As the Board held, transferring lines to Tex Mex, as KCS and Tex Mex demanded, would only have worsened that crisis -- possibly benefitting some shippers, but only at the cost of harming others. In any event, the crisis has been solved, and KCS/Tex Mex's prediction that it would return this fall proved incorrect.



The truth is that the service crisis resulted from a weak SP Gulf Coast infrastructure being overwhelmed by external stresses, just as occurred in the "World War III" episode in 1979-82. The service crisis struck before UP and SP had merged in the Texas/Gulf area. The UP/SP merger, far from being the cause, was in the end the only real solution to this crisis. Thanks to the merger, UP recovered in half the time of the "World War III" episode, and without a recession to help clear congestion.

III. THE PROPOSED CONDITIONS IMPROPERLY SEEK TO  
ADD, RATHER THAN PRESERVE, COMPETITION, AND  
WOULD CREATE, RATHER THAN SOLVE, PROBLEMS

Finally, rather than being tailored to curing any merger-caused reduction in competition, the proposed conditions seek to create new competition; and many of them would create, rather than prevent, operating problems.

I cannot cover every proposed condition in these remarks, but a review of the principal ones illustrates these points.

KCS/Tex Mex's so-called "neutral switching" proposal for Houston is in fact a sweeping "open access" scheme. It would give KCS/Tex Mex, as well as BNSF, access to hundreds of shippers in the Houston-Galveston area that were exclusively-served before the merger and continue to be exclusively served today. These shippers were not competitively harmed by the merger; rather, they gained the benefit of a broader combined UP/SP rail network with expanded single-line service. There is no justification for injecting additional competitors at these points. "Open access" schemes ought to be considered, if at all, in Congress, and not imposed as merger conditions applicable to only a single railroad.

The KCS/Tex Mex access scheme would also be disastrous operationally. UP has submitted very detailed testimony demonstrating that this scheme, which would substitute PTRAs for UP and BNSF and force far more traffic through PTRAs yards than they could possibly handle, would lead to a Houston service "meltdown" that would dwarf anything experienced in the past year.

Other KCS/Tex Mex proposals, though they might appear innocuous, would cause similar harms. For example, undoing the rationalization of HBT and having PTRAs dispatch HBT lines would reintroduce numerous inefficient interchanges in the heart of the Houston terminal, and would destroy the Spring Center's effectiveness by creating a dispatching "black hole" in the heart of Houston.

BNSF's proposal for trackage rights over UP to Laredo is another prime example of creating new competition without justification, and worsening, rather than improving, operations. BNSF's proposal would inject a second single-line route to Laredo when only one existed prior to the merger, and would do so despite the fact that BNSF has more than substituted for SP as an interline partner for Tex Mex.<sup>1</sup> The result would be severe congestion at Laredo, on UP's San Antonio-Laredo line, and north of San Antonio. Moreover, Ferromex, the privatized Mexican railway that provides the only competitive alternative to TFM in Mexico via Eagle Pass, stresses that the BNSF condition would undermine competition for cross-border traffic by shifting more traffic to Laredo.

Indeed, all of the BNSF proposals seek added competitive advantages, beyond the rights that BNSF negotiated in the merger case and swore would fully preserve pre-merger

---

<sup>1</sup> Also, Tex Mex's claims of financial distress are belied by its recent announcement that it had an operating ratio of 94 -- lower than UP's -- in 1997. See [http://www.kcsi.com/tmr\\_t.html](http://www.kcsi.com/tmr_t.html).

competition. Any such additional BNSF rights should be obtained in arm's-length, "win-win" voluntary negotiations, not imposed as one-sided merger conditions.

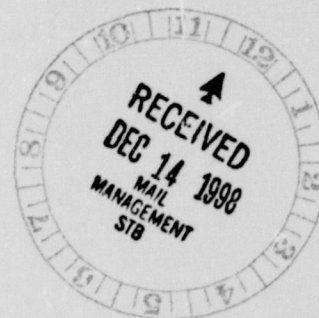
The various conditions that have been proposed would also be counterproductive because they would take traffic from UP just when it desperately needs to continue rebuilding its traffic base in order to be a fully effective competitor to the powerful BNSF system. UP lost almost 10% of its traffic to BNSF in the service crisis. In the three quarters of the crisis, UP lost \$230 million while BNSF was making \$759 million. While the traffic is slowly returning, UP volumes are still down more than 6% while BNSF's volumes are up 8%. The proposed conditions would put over three-quarters of a billion dollars in UP revenues at risk, and would undermine UP's ability to continue its ambitious investment plans in the Houston/Gulf area, which are so crucial to permanently solving the infrastructure problem in this area. Only UP has proposed, and is implementing, a comprehensive, billion-dollar-plus investment plan for the Houston/Gulf area. Saddling UP with additional conditions would threaten the balanced competition in the West that the Board sought to promote by approving the UP/SP merger. Such concerns explain why some 200 shippers, a score of railroads, nine Western Governors, 350 other public officials, and the United Transportation Union oppose the proposed conditions. In fact, if there is any "consensus" here, it is a consensus against these damaging and unjustified conditions.



STB FD 32760 (Sub 26) 12-14-98 D 192686

192686

Office of the Secretary  
Case Control Unit  
STB Finance Docket No. 32760 (Sub No. <sup>26</sup>31)  
Surface Transportation Board  
1925 K Street N. W.  
Washington, D.C. 20423-0001



Dear Mr. Secretary:

Enclosed with this letter you will find an original plus twenty-five copies of the Houston and Gulf Coast Railroad's Argument Summary.  
Copies of this document have also been sent to all parties of record.

Sincerely,

A handwritten signature in dark ink, appearing to read "K. Cotton".

Kenneth B. Cotton

HOUSTON AND GULF COAST RAILROAD

A large, simple handwritten letter "D" in dark ink.

ENTERED  
Office of the Secretary

DEC 14 1998

Part of  
Public Record

BEFORE THE SURFACE TRANSPORTATION BOARD

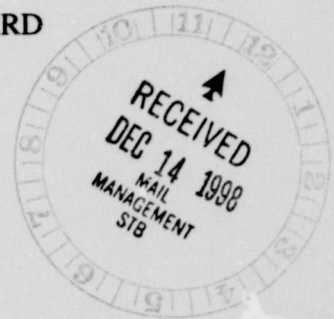
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STB Finance Docket No. 32760(Sub-No.31)

UNION PACIFIC CORPORATION, et. al.

--CONTROL AND MERGER--  
SOUTHERN PACIFIC RAIL CORPORATION, et. al

-----  
HOUSTON/GULF COAST OVERSIGHT

-----  
ARGUMENT SUMMARY OF HOUSTON AND GULF COAST RAILROAD





The Houston and Gulf Coast Railroad is the operator of 12 miles of track between Wharton and Bay City, Texas. Its mainline connection is with the BNSF near Bay City. BNSF reaches Bay City over Union Pacific's Brownsville Subdivision. The H&GC also connects with the intact but out-of-service former SP line which runs from Wharton to Rosenberg, Texas.

The H&GC is unique in that it is one of only two African-American operated railroads in the United States, and the only one west of the Mississippi River.

This railroad serves primarily agricultural customers on its line and was growing its traffic until the catastrophic service meltdown on the Union Pacific. Due to this service crisis, the BNSF was unable to service its customers south of Bay City, and could not timely serve the H&GC. Cars that were ordered had to be cancelled due to shippers needing more timely service, shipping their grain by more reliable, but more expensive truck to Houston, Galveston, and other markets.

This loss of traffic devastated H&GC's revenues and carloadings.

The H&GC, seeking to bolster its flagging revenues, contacted local UP operating management about storing and switching UP cars. Union Pacific was in fact, engaging short lines to switch and store plastic cars and manifest freight cars. Union Pacific was, and still is, short of space for SIT traffic; Union Pacific engaged every short line in the Houston/Gulf Coast area, and one as far away as Georgetown, Texas, 160 miles from the Gulf Coast area, to switch cars and store SIT traffic.

All attempts were blunted by upper UP management.

The H&GC is dying, mortally wounded by the service crisis and the apparent corporate racism of the Union Pacific.

In July, the STB asked for proposals to help prevent another service crisis and to promote competition in the Gulf Coast area.

To that end, the H&GC filed an application with the STB for trackage rights on Union Pacific between Bay City and Algoa, Texas; between Wharton and Rosenberg, Texas to interchange with the BNSF at Rosenberg; between Rosenberg and Harrisburg Junction (via West Junction); and compel the Union Pacific to sell its Galveston Subdivision (the former Galveston, Houston, and Henderson Railroad, known as the GH&H) from Congress Yard (MP 184.5) in Houston, Texas to MP 233.0 in Galveston, Texas, as well as the former Southern Pacific Galveston Line from MP 38.8 to MP 55.6 (see Exhibit B&C, H&GC application). H&GC also requested the rights to serve Imperial Holly at Sugarland, Texas and rights to reach the Texas City Terminal Railroad in Texas City, Texas, PTRC at Manchester Yard in Houston, Texas, and UP's Englewood and Settegast Yards, as well as BNSF's New South Yard.

Also requested were trackage rights on the Wharton-Victoria trackage if this line is rebuilt by Tex Mex. H&GC would serve all present and future customers on the Victoria-Rosenberg trackage, interchanging with all railroads serving Victoria.

Trackage rights between Bay City and Algoa would be for SIT traffic and overhead traffic to a connection with the UP and BNSF at Algoa.

The application also requests that all Galveston, Texas -bound grain trains are interchanged with the H&GC at either Rosenberg or Congress Yard in Houston. with these rights and line sales,the H&GC would provide two neutral SIT sites-one near Wharton,Texas to service plastic customers between Bay City and Algoa,ans one at Galveston,Texas to service customers in the Houston area,as well as provide neutral rail service to customers between Houston and Galveston.

Union Pacific controls 84% of all plastic storage in the Houston/Gulf Coast area,and this stranglehold keeps the plastic industry hostage.

In the Verified Statement of Larry L. Thomas,President of the Society Plastics Industry in Volume II of the Consensus Plan,he states," moreover,our members advise us that the UP has ignored requests over the past several years to increase the storage space available for hopper cars to be used in plastic resins service". In short,the UP was warned of the possible shortage,and did nothing to prevent this disaster.

The arrogance of Union Pacific can be further seen.In the July 8,1998 Dow Chemical request for new conditions,it states on page seven"Contrary to its proposal in the Infrastructure report,Up told Dow and other chemical and plastic shippers at a meeting on March 25,1998,that it would NOT construct a yard at Angleton.At the very least,this suggests that the Angleton project is n a priority among UP's laundry list of similar projects" This clearly shows the need for extra storage capacity in the Gulf Coast area,storage the H&GC would gladly provide.

Operations in Houston would be based at Congress Yard,an underutilized 200 car yard near downtown Houston.This line is ajacent to the West Belt and switching in this yard would not impede traffic on the West Belt. This yard would be used as an interchange point for the H&GC and a joint facility with the Union Pacific.It would also serve as the northern terminus of the Houston-Galveston trackage purchased from Union Pacific.

Should the relief sought by the H&GC be granted by the Board it would:

1. Give plastic producers neutral sites from which they could store and ship their products on the carrier of their choice;
2. Give rail customers on the Houston-Galveston line the option of choice among the Class One railroads serving the Houston/Gulf Coast area;
3. Serving as a conduit for agricultural shippers and offering less expensive access to world markets;
4. Promote competition among the Class One railroads in the Houston/Gulf Coast area;
5. Offer timely,responsive rail service to customers in the Houston/Gulf Coast area.
6. Provide short-haul rail service between the ports of Houston,Texas City,and Galveston.

The H&GC has offered \$7,000,000.00,payable over ten years,for the purchase of the Houston-Galveston trackage.The Board has the power to compel the sale of these lines if they meet the following conditions:



1. The rail carrier operating the line refuses within a reasonable time to make the necessary efforts to provide adequate service to shippers.

This is evidenced by the several Emergency Orders the Board has had to issue, lawsuits filed by shippers, and the continuing congestion of the railroad. For almost two years, shippers have lost hundreds of millions of dollars due to the collapse of the Union Pacific; many shippers have been forced to use Union Pacific because they had no other option. Plastic shippers have been hard hit because UP controls the bulk of SIT storage and are their only outlet. Other chemical shippers have had to shut down or ship by more expensive means, meaning truck, to make maritime schedules or to keep production lines open. The Union Pacific refuses to remedy the situation in a reasonable time frame.

Union Pacific has had long enough to mitigate their problems; they have behaved in an arrogant, uncaring manner and the Board has the power to remedy this emergency as soon as possible.

2. The sale of the line would not have an undue adverse effect on the carrier's operations.

The sale of the GH&H and the former SP Galveston Subdivision involve around 40,000 carloads per year. This total is only .376% of the total traffic that Union Pacific handles per year. Much of this traffic would still originate at UP points; however, outbound traffic from the area will have a choice in routing their cars over the Class One of their choice.

The sale of this line would free up locomotives, crews, and equipment that should receive better utilization, helping to keep Settegast and Englewood yards fluid.

Selling these line would also allow shippers to have closer contact with their shipments; with small-tiered management, shippers would have their questions answered much more quickly, fostering a good relationship between H&GC, its customers, and the railroads.

3. The sale would result in improved service over the line.

Service is the life blood of short line railroads. Without it, these railroads would die the deaths the Class Ones intended. Class Ones cannot deliver the service on a local basis the way a short line can. Innovation on short lines may take only a phone call to the railroad manager from the shipper; implementation may take place in hours. On Class Ones, innovation is more often stifled than encouraged. Implementation is difficult, and opportunities are missed by both shipper and railroad.

Short lines place their emphasis on providing excellent service instead of just running trains; as a result, they are becoming more important in the nation's transportation system, providing responsive, low-cost service that continue to grow in importance.

4. To provide competition.

The Union Pacific has enjoyed near-monopoly status in the Houston/Gulf Coast area. The result of this market dominance has been the near-total destruction of rail service in the area. Nine of the eleven rail routes into Houston belong to the Union Pacific.



If the Board approves H&GC's application, the H&GC, by owning its own route between Houston and Galveston, would serve as the neutral carrier with access to all Class Ones serving Houston and the Gulf Coast area, as well as giving the ports of Texas City, Galveston, and the Port of Houston the ability to tie together these facilities and operate in a responsive manner that only a short line can provide.

Shippers now will have an option as to who their line-haul carrier will be. With the option to interchange with everyone, the H&GC gives shippers freedom of choice, and, during periods of congestion or other problems hampering rail service, the shipper would be able to move his goods over the best available route for his product, keeping that company able to compete in his market.

The H&GC would be ready to purchase and operate these lines within ninety days of Board approval.

The Union Pacific seems to be engaging in a program to ration its service. A railroad, as a common carrier and in the public interest, should be able to handle all traffic tendered to it, with fair rates and dependable service. Union Pacific gives the impression that if you drive off the small shippers (and small railroads), they can focus on only handling intermodal and bulk commodity traffic.

When will this behavior stop? What sector of freight traffic will Union Pacific want to drive off next? How long will the Union Pacific continue to refuse to offer service, and continue to place a stranglehold on Houston rail traffic?


Should the Board approve H&GC's application, competition would be restored to an area that has recently had little. The service crisis clearly shows the destructive potential inherent when monopoly power clearly dominates a region, and there is no recourse for the shippers in that region.

The Houston and Gulf Coast Railroad would provide that recourse for shippers in the Houston/Gulf Coast area, as well as provide a vital link to farmers who need dependable, inexpensive rail transportation to access world markets, and to provide neutral rail service to all shippers it is permitted to serve.

The alternative is the destruction of the H&GC, the loss of rail service by its customers, and the continued stranglehold Union Pacific has on the Houston/Gulf Coast area.

Only the power granted to the Board and the grace of God can save the H&GC, and restore competition in the Houston/Gulf Coast area. Thank you for this opportunity and may God bless you.

Sincerely,



Kenneth B. Cotton

HOUSTON AND GULF COAST RAILROAD

STB FD 32760 (Sub 26) 10-16-98 D 191655V1 1/7

ORIGINAL

✕ CMA-4 ✕ SPI-4  
✕ RCT-3 ✕ TCC-4  
✕ TM-20 ✕ KCS-11

191655

BEFORE THE  
SURFACE TRANSPORTATION BOARD

FINANCE DOCKET NO. 32760 (Sub-No. 26)\*



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

HOUSTON/GULF COAST OVERSIGHT PROCEEDING

REBUTTAL EVIDENCE AND ARGUMENT IN SUPPORT  
OF THE CONSENSUS PLAN

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Office of the Secretary

OCT 19 1998

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VOLUME I

THE CHEMICAL MANUFACTURERS  
ASSOCIATION

THE SOCIETY OF THE PLASTICS INDUSTRY,  
INC.

THE RAILROAD COMMISSION OF TEXAS

THE TEXAS CHEMICAL COUNCIL

THE TEXAS MEXICAN RAILWAY COMPANY

THE KANSAS CITY SOUTHERN RAILWAY  
COMPANY

October 16, 1998

(\* and embraced sub-dockets)



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William A. Mullins

October 16, 1998

## **HAND DELIVERY**

Honorable Vernon A. Williams  
Case Control Unit  
Attn: STB FD 32760 (Sub-Nos. 26-32)  
Surface Transportation Board  
Room 700  
1925 K Street, N.W.  
Washington, D.C. 20006

ENTERED  
Office of the Secretary

OCT 19 1998

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RE: Finance Docket No. 32760 (Sub-Nos. 26 - 32),  
*Union Pacific Corp., et al. - Control & Merger - Southern Pacific Rail Corp.,  
et al. - Houston/Gulf Coast Oversight*

191655 191669 191670 191671 191672 191673 191674

Dear Secretary Williams:

Enclosed for filing in above captioned proceeding are an original and twenty-six copies of the Rebuttal Evidence And Argument In Support Of The Consensus Plan, Volumes 1 - 3 ("Consensus Rebuttal"), filed on behalf of The Chemical Manufacturers Association, The Society of Plastics Industry, Inc., The Railroad Commission of Texas, The Texas Chemical Council, The Texas Mexican Railway, and The Kansas City Southern Railway Company (collectively, the "Consensus Parties"). Please note that Volume 3 enclosed herewith contains material designated by the parties as Highly Confidential, and is being submitted under seal pursuant to the protective order issued by the Board in this proceeding. Also, included with this filing are a set of 3.5-inch diskettes containing the text of the pleading in WordPerfect format and containing tables in Microsoft Excel format.

Please date and time stamp one copy of the Consensus Rebuttal for return to our offices.

Sincerely,

William A. Mullins  
Attorney for The Kansas City  
Southern Railway Company

cc: Parties of Record  
Honorable Stephen J. Grossman

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### **VOLUME III**

**HIGHLY CONFIDENTIAL INSERTS**  
**(served only on parties who have signed the appropriate confidentiality undertakings)**



**BEFORE THE  
SURFACE TRANSPORTATION BOARD**

---

**FINANCE DOCKET NO. 32760 (Sub-No. 26)\***

---

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

---

**HOUSTON/GULF COAST OVERSIGHT PROCEEDING**

---

**REBUTTAL EVIDENCE AND ARGUMENT IN SUPPORT  
OF THE CONSENSUS PLAN**

---

**INTRODUCTION AND SUMMARY**

My administration has worked with the Greater Houston Partnership on this issue over the past nine months. The Partnership strongly supports the principles outlined in what is recognized as the Consensus Partners Plan. We concur and have also listened to shippers, the general public, local elected officials and the Port of Houston. Competitive rail is crucial to the Houston region's continued economic growth.

Lee P. Brown, Mayor, City of Houston, Texas  
Letter to The Honorable Linda Morgan,  
October 12, 1998.

**(\* and embraced sub-dockets)**

When the federal Surface Transportation Board approved the contentious marriage between Union Pacific and Southern Pacific Rail Corp. in 1996, it did so conditionally, reserving the right to change the merger's terms if competition was unacceptably thwarted. . . . Without hesitation, the Board should embrace an eight-point plan advocated by a coalition of shippers, government officials and rail competitors. . . . Understandably, the Board has been reluctant to intervene in this private business matter. Government interference always should be a last resort. But we're at the last resort. Government approved the deal, so now government — the Board — must make it work.

*Permanent Fix: Competition key to ending rail pain in Houston, Gulf Coast, Houston Chronicle, August 23, 1998, at Outlook, p.2.*

The Consensus Parties believe that Mayor Brown and the Houston Chronicle have it right. The Consensus Plan is not intended as a short-term, or temporary measure to solve Union Pacific Corporation's ("UP") Western U.S. service problems. The Consensus Plan is about a permanent fix to the competitive problems in the Texas Gulf Coast that resulted from the merger of UP and Southern Pacific Rail Corporation ("SP") which have been highlighted by UP's service meltdown.

UP has attempted to portray the Consensus Plan as "taking UP's property," an "open access plan," a plan that will have "substantial" financial impacts on UP and its investment ability, and a plan which is designed to provide Houston and Gulf Coast shippers with undeserved additional competition. Of course the Consensus Plan does none of those things. The Consensus Plan will add substantial new competitive infrastructure, restore competition, reinstitute operating arrangements that existed prior to the merger, and carry out the Board's desire that Tex Mex provide an effective alternative to UP at Laredo.



This Rebuttal Filing will address each and every one of these issues. The Consensus Parties will first briefly discuss each and every one of UP's "myths" against the Consensus Plan and then discuss the legal principles which should guide the Board's decision making process. Once this groundwork has been laid, the Rebuttal Filing will specifically address the competitive issues of this case and explain why the original conditions imposed by the Board to preserve competition in Houston and for NAFTA shippers, while well intentioned, have simply failed to preserve the pre-merger level of competition provided by SP.

In addition to these competitive issues, there are fundamental structural defects, such as the lack of neutral dispatching, switching and independent infrastructure, that severely impede the rights granted to Burlington Northern Santa Fe Railway ("BNSF") and The Texas Mexican Railway Company ("Tex Mex"). The Rebuttal Witnesses herein will clearly establish that these fundamental defects must be corrected in order to accomplish the Board's stated goal of preserving the pre-merger level of competition. Finally, it will be explained how the Consensus Plan will resolve both the competitive and structural problems that currently exist.

With the Consensus Plan, the shippers and the Texas economy no longer will be subject to the effective monopoly control and problems of UP. If the Consensus Plan is adopted, when UP has delayed trains, labor disruptions or any other service problems on its tracks, shippers will have alternatives. Shippers, as they did before the UP/SP merger, will have choices once again available to them — choices that were taken away from them as a result of a government-approved merger.



\* \* \*

Instead of focusing on these realities, UP, in an attempt to generate opposition to the Consensus Plan, publicly has been touting a series of "myths" about the purposes of the Consensus Plan and its effects. Of course the realities are quite different.

**UP MYTH # 1:**

The Consensus Plan is about "government regulation" and "open access" and expanding competition to shippers who did not have competition prior to the merger.

**REALITY:**

The Consensus Plan is about restoring the competitive and operating choices that were available to shippers prior to the UP and SP merger and countering the competitive effects of the merger. It is not about "taking something away" from UP that UP somehow earned in the free market.

Indeed, as recently as 1988, there were five separate Class I railroads serving Houston shippers, and two terminal railroads, the Houston Belt and Terminal Railway Company ("HBT") and the Port Terminal Railroad Association ("PTRA"). These two terminal railroads provided a significant number of Houston shippers with neutral dispatching and switching and allowed those shippers to be switched to any of the five railroads for the linehaul move, thus giving these shippers the service and rate options available from five railroads.

Just prior to the UP/SP merger in 1995, as a result of another UP merger (and another merger not involving UP) the number of Class I railroads serving Houston had dropped to three, but the HBT and PTRR remained in existence. After the UP/SP merger, the alternatives available to these Houston shippers were reduced to two; and the HBT, including the neutral switching and dispatching which it afforded, was eliminated.

The Consensus Plan will restore neutral switching and dispatching to all of the former HBT and PTRR shippers. The Consensus Plan will restore meaningful rail competition in Houston, an environment not preserved by the UP/SP-BNSF trackage rights agreement. To provide other service opportunities, the Consensus Plan restores the number of railroads serving Houston shippers to three. The Consensus Plan will allow shippers the choice of which one of the three railroads they will use.

Thus, the Consensus Plan is not about using "government regulation" to force UP to give up access to shippers which UP had somehow gained access to through competing in the free market. Instead, the Consensus Plan is about restoring competitive and operating choices that were taken away when the government allowed UP to merge with SP in the first instance.

**UP MYTH #2:**

In the Texas Gulf Coast, UP faces intense competition from BNSF and UP has lost a substantial amount of traffic to BNSF as a result of UP's service problems. There is no competitive problem in Texas.

**REALITY:**

UP's own data, submitted September 18, 1998, clearly shows that even in the midst of the emergency service crisis, when shippers were doing everything in their power to avoid using UP, UP maintained incredibly high market shares for Houston traffic destined to the Eastern and Southern gateways. For example, from July 1997 to June 1998, in the midst of the crisis, UP's carload market share for traffic originating in Houston ranged from 80% to 81% for traffic destined for the Northeast and from 78% to 84% for traffic destined to the Southeast. This gateway traffic should be fully competitive in that it does not entail closed destinations on the UP system. If Houston shippers truly had a choice between UP and BNSF, UP would not have maintained such high market shares. Obviously, despite the complete breakdown of UP service, shippers were still forced to use UP, including the fact that BNSF had to rely on UP's infrastructure, which rendered BNSF a non-competitive option.

It is true that BNSF has provided some competition to UP for the business of some shippers. However, the data clearly shows that BNSF is



competitive only for the traffic to the West, where BNSF has a large presence, independent infrastructure and itself controls a number of closed destinations.

Indeed, BNSF's July 8, 1998 comments recognize that it cannot effectively provide a competitive check to UP without some change in the structure of the Houston market. For instance, BNSF states that:

[T]he ability of BNSF to provide reliable, dependable and consistent service to shippers under the conditions imposed by the Board in the UP/SP merger to preserve competition is being thwarted by (i) structural deficiencies in certain of the rights which BNSF received as a result of the UP/SP merger on UP's lines in the Houston and Gulf Coast, and (ii) by UP's practice of favoring its trains over the trains of other carriers in situations where the continuing congestion and service problems on UP's lines preclude normal operations.

*BNSF Application for Additional Remedial Conditions Regarding the Houston/Gulf Coast Area*, Finance Docket No. 32760 (Sub-No. 26), filed July 8, 1998 ("BNSF Application") at 5.

The fact that BNSF has been able to provide some competitive alternative to UP for Western destinations for some traffic proves the precise point that the Consensus Parties (and BNSF itself) are making: where there is neutral switching and dispatching and where a railroad can control its own infrastructure (which BNSF does for shipments to the West), there is competition. The Consensus Plan ensures that all Houston shippers, not only PTRAs shippers, will benefit from these advantages.

**UP MYTH #3:**

UP plans on investing \$1.4 billion in the Texas/Louisiana Gulf Coast over the next five years and adoption of the Consensus Plan will mean that UP will not be able to spend these resources.

**REALITY:**

In reply to UP's Infrastructure Report, Mr. Tom O'Connor, a widely recognized expert on rail investments and strategies, calculated that: (i) UP had actually funded or begun investments in the Houston terminal area totaling \$29.3 million, a mere 2% of the planned total of \$1.4 billion; (ii) UP had actually funded or begun investments in other Gulf Coast areas totaling \$46.5 million, a further 3% of the planned total of \$1.4 billion; and (iii) 60% of all projects described in the Infrastructure Report were unspecified or unplanned. These calculations enabled Mr. O'Connor to conclude that the investments proposed in the Infrastructure Report would not occur in the near future and may not occur at all, depending on UP's subjective evaluation of future events. Furthermore, documents produced by UP in discovery clearly show that UP has actually spent, or authorized the spending of, a total of \$116.9 million in the Houston/Gulf Coast area. This amount represents 4.7% of the total of \$2.5 billion that UP plans to spend system wide in 1998 and 8.4% of the total investments planned for the Houston/Gulf Coast area over the next five years.

The inference to be drawn from UP's lack of investment in the Gulf Coast region is irresistible. UP does not face competition in the Gulf Coast region because it has a virtual monopoly in that region. Without competition, UP has no incentive to invest in the Gulf Coast region. Indeed, where UP does face intense competition from BNSF, in the Central Corridor and Northern California for example, UP is investing a significant amount of money — hundreds of millions of dollars — in 1998 alone. Thus, contrary to UP's claims, adoption of the Consensus Plan and its corresponding pro-competitive benefits, will actually provide incentives to UP to increase its investment in the Houston and Texas Gulf Coast area.

**UP MYTH # 4:**

This dispute is really a private dispute between rail carriers, intended merely to enrich Tex Mex and KCS, and is not intended to benefit shippers or the public interest.

**REALITY:**

The eight point Consensus Plan is intended to benefit the customers of the railroads and the public interest as a whole. It is not a "private dispute" between carriers, nor is the Consensus Plan a "KCS/Tex Mex" plan as UP continually calls it. The Consensus Plan is a good faith, consensus effort to do what is beneficial for the economy of Texas and for



the shippers. To call it a "KCS/Tex Mex" plan ignores the other supporters to the Consensus Plan.

The Consensus Plan has the widespread support of shippers and is endorsed by numerous other Texas public interest bodies. Joining the Houston Chronicle in endorsing and supporting the eight point Consensus Plan are some of the nation's largest shipper trade associations: The Chemical Manufacturers Association ("CMA"), The Society of the Plastics Industry, Inc. ("SPI"), and The Texas Chemical Council ("TCC"). Collectively, these three organizations represent over 2,000 individual shippers.

Another 70 plus shippers have submitted individual statements supporting all or part of the Consensus Plan. Unlike UP's shipper statements submitted on September 18, 1998, the vast majority of these 70 plus shippers have operations in the Houston/Gulf Coast area and represent the nation's largest shippers, such as Shell Chemical, Union Carbide, Mobil Oil Corporation, International Paper, E.I. DuPont de Nemours and Company, Phillips Petroleum Company, Citgo Petroleum Corporation, BASF, Rohm and Haas, and Huntsman Corporation. Indeed, the nation's largest shipper trade association, the National Industrial Transportation League, while not specifically endorsing the Consensus Plan, is today submitting comments endorsing every one of the items of

the Consensus Plan, except for expanded access for shippers located on the Bayport Loop.

Joining these shippers are numerous public interest bodies, who have either endorsed the Consensus Plan in total or the principles contained within the Consensus Plan. These bodies include the Railroad Commission of Texas, the Office of the Mayor of Houston, Port of Houston, Greater Houston Partnership (the equivalent of the Houston Chamber of Commerce), the Texas Farm Bureau, the Corpus Christi Chamber of Commerce, and the Texas Democratic Party.

**UP MYTH #5:**

The proposal is a massive government confiscation of UP's private property and will cause UP to lose significant revenues.

**REALITY:**

Not one piece of UP property will be confiscated by the government. While the Consensus Plan does request UP to sell some of its property to another carrier as a condition for approval of its merger with SP, such requests are standard conditions imposed in any merger. Indeed, at the July 1, 1996, oral argument, UP's own counsel invited the Board to require UP to sell certain lines and assets if the Board felt it was appropriate to do so after two years of the Board's oversight process.

If UP is requested to sell certain assets, UP will be fully compensated for any property that it sells; and if UP is unhappy with the

price, it has the right to request that the Board set a higher price.

Furthermore, for the property that UP does sell, the Consensus Plan calls for the purchaser to grant back to UP the right to use that property, along with the purchaser, in order to ensure that UP would not lose the use of that property.

The Consensus Plan also calls for UP to share some of its tracks with the PTR, BNSF and Tex Mex, but UP, as the owner of that track, will continue to have the right to operate over those tracks. Where PTR, Tex Mex or BNSF operate over these UP tracks, they will pay UP a usage fee equal to the fee that UP currently pays to BNSF when it operates over BNSF's tracks.

UP also claims that the Consensus Plan will cause UP to lose a significant amount of traffic revenue. This is simply not true. Of the approximate \$2.8 billion dollar Houston Business Economic Area ("BEA") rail market, UP controls (as stated by UP's own witness, Richard J. Barber) approximately \$1.9 billion (69%) of that market. Of course, UP did not gain control over this revenue through competing for it in the free market, but by buying SP's share through a government approved merger. Nonetheless, of UP's \$1.9 billion share, the Consensus Plan projects about \$155 million (or approximately 8% of UP's revenues from Houston) will be diverted from UP to other carriers, including BNSF, Tex Mex and KCS.



Of course, this is just a projection and is based upon the premise that the Houston market is a "fixed pie" (which premise is faulty, as the competition brought about by the Consensus Plan is likely to increase the overall size of the "pie"). But even if this diversion does occur, such diversions will occur precisely because those other carriers' services are more efficient than the UP routes and provide a better alternative to Houston shippers than the existing UP routes. These diversions will not occur because the government ordered UP to "give" this traffic to the other carriers.

Finally, in 1997, even with its service-related loss of traffic, UP had gross operating revenues of approximately \$11 billion. Even if the pie remains fixed and all projected diversions occur, the notion that a loss of less than 1.5% of UP's revenues will somehow cripple UP is preposterous. Indeed, UP itself claims that it can't even handle all of its traffic today and needs to "ration its service." Allen R. Myerson, *Union Pacific to Limit Traffic on its Tracks*, N.Y. TIMES, September 1, 1998, at C10. In fact, UP is beginning to study what sorts of traffic might be "dispensable." *Id.*

**UP MYTH #6:**

The Consensus Plan is unworkable and would create serious operational problems if it were adopted.

## REALITY:

The Consensus Plan contains a full explanation of how the rail operations would work following the Consensus Plan's adoption. The three railroad operating witnesses supporting the Consensus Plan have 91 years of railroad operating experience among them. One witness is the former President of the HBT, and another spent 11 years operating railroads into and out of the Houston area.

These and other UP myths will be fully rebutted in this filing. One would think that UP, which claims it is willing to "work with our customers, and with other railroads" and find "cooperative and creative ways of improving service," *UP's Opposition to Condition Applications*, Vol. 1, Finance Docket No. 32760 (Sub-Nos. 26-32) filed September 18, 1998 ("UP/SP-356") at 11, would find something to support and be positive about with respect the numerous proposals made to improve service (instead of attempting to denigrate such proposals by spreading these insubstantial myths). Yet, when the Consensus Parties proposed an eight point Consensus Plan to improve service in Texas; when BNSF proposed a 9 point plan; and when Dow, Formosa, DuPont, and Central Power & Light proposed solutions to improve service to their plants, UP responded by stating: "UP opposes all of these conditions." UP/SP-356 at 11. For a railroad which has caused billions of dollars in damages to the Texas economy alone, such intransigence is remarkable.

Numerous witnesses will explain in great detail why UP's allegations and arguments against adoption of the Consensus Plan are simply wrong. The Consensus

Plan will add substantial new competitive infrastructure, restore the competitive and operating arrangements that existed before the UP/SP merger, allow Tex Mex to be an effective competitive alternative to UP for U.S./Mexican traffic, and ensure that UP's problems will never again cause such pervasive and unmitigated problems for the Texas economy. The Consensus Plan should be adopted.

## **ARGUMENT**

### **I. THE PROPER LEGAL STANDARD**

#### **A. The Board's Conditioning Authority**

UP acts as if the Board's Decision No. 44 somehow found that there was no competitive problem from the UP/SP merger for Houston and NAFTA traffic. This mischaracterizes the Board's finding. The Board noted that the Applicants to the UP/SP merger "presented their plans for addressing competitive harms at the outset [of the merger proceeding.]" Decision No. 44 at 117 (STB served August 12, 1996). Observing that a "condition will not be imposed unless the merger [will] produce effects harmful to the public interest," the Board found that "subject to [the BNSF] agreement and certain conditions that [the Board] impos[ed] . . . the merger as conditioned [was] unlikely to lead to any significant competitive harms." *Id.* at 116, 144 (emphasis added). Moreover, the Board held that "for many shippers throughout the West, the various rights provided for in the BNSF agreement will ameliorate the competitive harms that would be generated by an unconditioned merger." *Id.* at 145 (emphasis added).

For NAFTA traffic, the Board found that "Tex Mex and its supporters have raised legitimate concerns that absent a grant of Tex Mex's responsive application, the merger



could result in a reduction of competition at Laredo, the most important U.S.—Mexican gateway.” *Id.* at 147 (emphasis added). Thus, the “partial grant of Tex Mex’s responsive application [was] required to ensure the continuation of an effective competitive alternative to UP’s routing into the border crossing at Laredo.” *Id.*

As noted, to resolve the competitive problems in Texas and for NAFTA traffic, the Board relied upon a series of trackage and other rights granted to BNSF and Tex Mex. The Board granted these conditions to ensure that shippers would not lose their competitive alternatives as a result of the merger. Decision No. 44 at 103 (“In essence, the BNSF agreement will permit BNSF to replace, to a large extent, the competitive service that is lost when SP is absorbed into UP.”).

In imposing these conditions, the Board recognized the possible need for further, future modification of these conditions due to unforeseen future circumstances and thus specifically retained oversight jurisdiction “for 5 years to examine whether the conditions we have imposed have effectively addressed the competitive issues they were intended to remedy.” Decision No. 44 at 146. In formulating that “oversight” condition, the Board specifically retained the jurisdictional power “to impose additional remedial conditions if, and to the extent, we determine that the conditions already imposed have not effectively addressed the competitive harms caused by the merger.” *Id.*<sup>1</sup> In addition, Ordering ¶ 6 of

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<sup>1</sup> The Board has reiterated its oversight jurisdiction in nearly every decision issued thus far in the Oversight Proceeding, Finance Docket No. 32760 (Sub-No. 21). In decisions numbered 1 and 10, the Board specifically stated that it had retained jurisdiction to impose “additional remedial conditions.” Decision No. 1 (STB served May 7, 1997) and Decision No. 10 (STB served Oct. 27, 1997).

Decision No. 44 states that further conditions, including divestiture, may be ordered under the oversight provision. *Id.* at 231.

Indeed, each of the Board members' separate comments in Decision No. 44 elaborated on the need for further oversight. For example, Chairman Morgan stated that "[i]f competitive harm becomes a problem, we can and will act. The divestiture option will remain available during the entire oversight period." *Id.* at 240. On the same topic, Vice Chairman Owen declared that "[d]uring this oversight period we have authority to impose additional conditions and we will be an alert and aggressive policeman." *Id.* at 250. Even UP's own counsel, Arvid E. Roach II, during oral argument on the merger, specifically declared that under the oversight jurisdiction, the Board "will have unrestricted power to impose additional conditions if appropriate . . . includ[ing] divestiture. . . . There's no reason that in a year or two or three, if [the Board] conclude[s] that [divestiture] is appropriate, you can't require it." UP/SP Merger, Finance Docket No. 32760, Oral Argument Transcript, July 1, 1996 at 59. Mr. Roach gave no hint that UP, later faced with the reality of such divestiture, would decry it as an improper expropriation by the Board of UP's rightful property. Thus, to the extent that the Board's original conditions have not proved adequate to effectively address the harms from UP's control of SP, the Board has retained jurisdiction to impose additional remedial conditions. Indeed, the Board has a legal obligation to "ensure" that the



conditions imposed to alleviate the anticompetitive effects of the UP/SP merger are working.<sup>2</sup>

Notwithstanding the existence of the Board's oversight jurisdiction, the Board also has adequate independent authority to modify the conditions granted to KCS/Tex Mex. 49 U.S.C. § 11327 provides that "[w]hen cause exists, the Board may make appropriate orders supplemental to an order made in a proceeding under sections 11322 through 11326 of this title." In fact, the United States Supreme Court precedent strongly supports the Board's independent basis under § 11327 (through its statutory predecessors) to consider and grant supplemental relief in consolidation and merger proceedings. See Penn-Central Merger and N & W Inclusion Cases, 389 U.S. 486, 522 (1967).<sup>3</sup> Whether

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<sup>2</sup> Section 11324(c) of Title 49 of the United States Code states in pertinent part that:

The Board may impose conditions governing the transaction, including the divestiture of parallel tracks or requiring the granting of trackage rights and access to other facilities. Any trackage rights and related conditions imposed to alleviate anti-competitive effects of the transaction shall provide for operating terms and compensation levels to ensure that such effects are alleviated.

<sup>3</sup> Other precedent also exists for the Board to utilize its jurisdiction, even where the Board has not expressly retained jurisdiction, to add to or otherwise modify conditions contained in previous orders and decisions. The Board's predecessor has specifically declared that "it is common for the Commission or a reviewing court to revisit and modify conditions." *Union Pacific Corp. et al. - Control - Chicago and North Western Transportation Co.*, Finance Docket No. 32133 (ICC served April 6, 1995). See also, *Rio Grande Industries, Inc. et al. - Purchase and Related Trackage Rights - Soo Line Railroad Company*, Finance Docket No. 31505 (ICC served Nov. 13, 1989) (The Board also has authority to issue supplemental orders in the absence of an express reservation of jurisdiction.); *GLI Acquisition Co. - Purchase - Trailways Lines, Inc. et al.*, No. MC-F-18505 (ICC served Dec. 10, 1990) ("Apart from our reservation of jurisdiction, we also have specific statutory authority under 49 U.S.C. § 11351 [now § 11327] to make necessary supplemental decisions, "when cause exists", in §§ 11343-11344 [now §§ 11323-11324] proceedings."); *People of State of Ill v. ICC*, 713 F.2d 305 (7<sup>th</sup> Cir. 1983) (The same test for determining whether additional conditions should be imposed is



the Board invokes its jurisdiction under its oversight proceeding, other statutory authority, or both, it is clear that the Board has the legal duty to impose additional remedial conditions if the original conditions have failed.

**B. The Houston/Gulf Coast Oversight Condition**

Recognizing the extraordinary and unprecedented nature of the service crisis and the continuing complaints from shippers and others about UP's market power and service ability, the Board invoked its oversight authority to determine whether the original conditions imposed in the UP/SP merger for the Houston/Gulf Coast were truly effective in replacing the service and competitive options that would have otherwise been lost in an unconditioned UP/SP merger.<sup>4</sup> According to UP, the Board's order establishing this proceeding requires the Consensus Parties to answer three questions: First, did the UP/SP merger give UP enhanced market power in the Houston/Gulf Coast? Second, if it did, did that increased market power cause the service problems? Third, if the answer to both of the foregoing questions is "yes," then should any proposed conditions be imposed? UP/SP-356 at 5 (emphasis added). UP claims this is the test that the Board established in Decision Nos. 1 & 6 in this proceeding.

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used in supplemental order proceedings and continuing jurisdiction proceedings, either way the petitions are not unusual.) (*citing Greyhound Corp. v. ICC*, 668 F.2d 1354 (D.C. Cir. 1981).

<sup>4</sup> The Board correctly has shown concern with both competition and service; they are interrelated and both are elements of the public interest that the Board must use its merger-conditioning power to protect. 49 U.S.C. § 11324(b)(1) and (b)(5).

However, if one carefully examines the language contained within those decisions, one easily can see that UP suggests a false test. UP has performed one of the oldest tricks in the book—it has set up the “straw man” and then knocked that “straw man” down.

What the Board’s language really said was that the Board would examine “whether there is any relationship between any market power gained by UP/SP through the merger and the failure of service that occurred in the region, and, if so, whether additional remedial conditions would be appropriate.” Decision No. 6 at 6 (STB served Aug. 4, 1998); Decision No. 1 at 5 (STB served May 19, 1998). Nowhere in this language is there a requirement to prove that the UP/SP merger gave UP “enhanced” market power. Nowhere is there a requirement to prove that the “enhanced” market power “caused” the service crisis.

The Board clearly wants to examine whether there is any “relationship” between the market power gained and the service crisis, but this is a “relational” test, not a “causal” test. As Dr. Curtis M. Grimm and Mr. Joseph J. Plaistow show in their attached joint rebuttal verified statement (“R.V.S. Grimm/Plaistow”), there is a significant relationship between the market power UP gained by its purchase of the SP and the service crisis. UP’s market power did not directly cause the service crisis, and no one claims that it did; but the service crisis did clearly show the extent to which UP gained market power as a result of the merger.

If UP had no enhanced market power, and if UP were unwilling or unable to give its customers good service because of mismanagement, merger implementation

difficulties, or for any other reason, the presence of an effective competitor would have enabled a significant portion of the customers to obtain that service from others. In the Houston/Gulf Coast region, however, UP's customers have not had that option. As evidenced by the large market share UP maintained throughout the crisis, UP's complete control of the Houston/Gulf Coast infrastructure, dispatching and switching clearly showed the extent to which UP has market power and showed that the conditions imposed in the original merger decision to ensure adequate levels of competition and service for Houston shippers have not been sufficiently effective and need to be enhanced. R.V.S. Grimm/Plastow at 4.

No monopolist would intentionally use its market power to cause a service crisis that would cost that monopolist millions of dollars in lost revenue; and it would be unnecessary for any party to try to prove, as UP suggests they should, that the service crisis was caused by a monopolist's exercise of its market power. Indeed, the Board was correct when it stated that "UP/SP did not manufacture the crisis to exploit some sort of dominant position in the market, or to obtain some sort of competitive advantage." Decision served February 17, 1998, Ex Parte No. 573, Service Order No. 1518 at 12 ("ESO-1"). The service crisis was caused by myriad factors, including missteps in integrating UP and SP; however, the critical factor in this proceeding is that the effects of the service crisis on the shippers and the economy as a whole were much worse as a result of the market power that UP gained through the merger. R.V.S. Grimm/Plastow at 13.



## **II. THE CONDITIONS IMPOSED TO PRESERVE COMPETITION IN THE HOUSTON/GULF COAST HAVE BEEN INEFFECTIVE**

### **A. BNSF Has Been Ineffective In Replacing SP For Houston Originated Traffic**

The Board fully intended BNSF to replicate the pre-merger level of competition that SP provided to UP in the Houston market. Decision No. 62 at 6-7 (STB served November 27, 1996) ("The merger should actually strengthen competition in Houston by replacing SP with a stronger BNSF."); *Id.* at 8 ("We are confident that BNSF will emerge as a strong and effective replacement in Houston for the competition lost through the merger.").<sup>5</sup> Indeed, the entire focus of this oversight proceeding is to determine whether the conditions imposed by the Board in Decision No. 44 to alleviate the service and competitive problems of an unconditioned UP/SP merger in the Houston/Gulf Coast market are working. If they are not, the Board has a legal obligation to change those conditions to "ensure" that the service and competitive problems in the Houston/Gulf Coast are in fact alleviated.

#### **1. Aggregated Houston Market Shares**

The service crisis has shown that the conditions initially imposed by the Board on the UP/SP merger to preserve competition in Houston have been inadequate to preserve pre-merger levels of rail competition and rail service. Before the merger, SP provided a

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<sup>5</sup> See also Decision No. 57 at 3 (STB served November 20, 1996) ("In Decision No. 44 we imposed 'a number of broad-based conditions that augment the BNSF agreement to help ensure that the BNSF trackage rights will allow BNSF to replicate the competition that would otherwise be lost when SP is absorbed into UP.'" (citations omitted).

much larger competitive presence in the Houston market vis-a-vis UP than BNSF has achieved under the conditions. R.V.S. Grimm/Plastow at 6. Before the merger, when there was a service failure on either the UP or SP, shippers had alternatives. As a result, a service failure did not cause substantial damage to the shippers or the economy. Without question, BNSF has simply not emerged as "a strong and effective replacement at Houston for the competition lost through the merger." The Consensus Plan will restore those service and competitive options so that UP's problems do not become everyone's problems and so that shippers will once again enjoy the same level of competition in Houston that they enjoyed before the merger.

UP criticizes the original Grimm/Plastow market study for using data from the first half of 1997 and states that a more "meaningful" period is from January 1998 to June 1998. UP/SP-356 at 47. The reason why the later period was not used in the original Grimm/Plastow study was due to the fact that UP did not make its 100% traffic tapes available until July 15, 1998, a week after the July 8th filing deadline. Accordingly, Grimm/Plastow have used the later period in their latest analysis. They have also examined both Houston originations and terminations and adapted Mr. Barber's methodology with regard to geographic destinations in order to eliminate UP's accusations of "gerrymandering." UP/SP-356 at 46. The rebuttal study thus uses the exact data and data points as UP witnesses Barber and Peterson. Even after making these adjustments, the overall conclusion is the same: BNSF has not been an effective replacement for SP for Houston originated traffic to certain geographic destinations.



An examination of Houston market share numbers for July through December 1997 and January through June 1998 show that UP retained a highly dominant market share despite the crisis, particularly to the Northeast and South. Mr. Barber's Appendix Tables 1 and 6, UP/SP-357, actually support this finding. On a carload basis, UP has 80% of Houston originating traffic and 89% of Houston terminating traffic to/from the Northeast in Jan.-June, 1998. With regard to traffic to and from the South, UP had 78% of originating traffic and 87% of terminating traffic in the first half of 1998. *Id.*

The large market share UP maintained throughout the crisis and UP's complete control of the Houston/Gulf Coast infrastructure, dispatching and switching clearly show the extent to which UP has market power and showed that the conditions imposed in the original merger decision to ensure adequate levels of competition and service for Houston shippers have not been sufficiently effective and need to be enhanced.

UP attacks the use of the Houston BEA as an improper market definition, UP/SP-357, V.S. Barber at 5, but while arguing against the value of such a market definition as overly broad, UP then proceeds to provide page after page of evidence using Houston as a market definition and then proceeds to provide additional pages with an even broader market definition, that of Texas and the entire Gulf Coast. *Id.* at 21-39. By using the Houston BEA as the market definition, the point UP is trying to make is that BNSF's modest post-merger gain in market share during the service crisis indicates an absence of competitive effects from the merger, but the point is fundamentally flawed as a matter of basic economics and antitrust principles. The fatal flaw is that UP Witness Barber offers as a basis of evaluating the impacts of the merger a comparison of the combined UP/SP



market shares in 1994 with current UP market shares. A proper analysis of the impacts of the UP/SP merger on market structure should use the pre-merger market shares of each individual carrier, BNSF, UP, and SP, as the baseline numbers and not the pre-merger combined UP and SP market shares, as Barber has done.

By way of testing UP's logic, suppose we have a market with three competitors, two with market shares of 49% each and the third with a share of 2%. If the two largest competitors merge, they would then have a combined market share of 98%. Subsequently, number three gains 1% of that combined share so that the market is now structured with the top firm having a 97% share and the second with 3%. By UP's logic, simply because the second firm in the post-merger environment was able to acquire 1% in market share shows that the merger has resulted in a more competitive market structure, even though one firm now dominates the market. This logic is contrary to any standard analysis of the effects on competition of a merger. Indeed, as noted, the Board, when it approved the UP/SP merger, clearly understood that the relevant comparison in a post-merger environment is whether or not BNSF was going to sufficiently replace SP's market share, not whether or not a combined UP and SP would lose some market share to BNSF.

The key is to compare the post merger market shares with the pre-merger shares. Using 1994 as a base year (as UP did), and disaggregating Barber's "UP" (which is really the combined UP/SP) into its components, UP and SP, this data reveals that the merger has clearly resulted in UP dominance. For example, based on carloads of Houston outbound traffic, UP's market share has increased from 61 to 80% in the Northeast, from

49% to 78% in the South-Southeast and from 37 to 69% overall. R.V.S. Grimm/Plaistow at 5. When using the proper pre-merger market shares as a comparison, the same result holds whether using originations or terminations, or carloads or tons — the merger has clearly resulted in much greater market dominance by UP in Houston.

Although BNSF has gained some market share since the merger vis-à-vis the combined UP/SP market share, this gain has not in any way countered the increase in UP's market dominance from its acquisition of SP. SP clearly provided a much larger competitive presence in the Houston market than BNSF has achieved under the conditions. See R.V.S. Grimm/Plaistow, Figures 4, 5, 6 & 7.

The fact that UP's Houston market share fell modestly merely indicates that BNSF exerted some competitive pressure during the crisis to some geographic locations, but UP's own analysis shows that BNSF has not been effective to the Northeastern, South/Southeastern, or Midwest gateways. For example, from July 1997 to June 1998, in the midst of the crisis, UP's carload market share for traffic originating in Houston ranged from 80% to 81% for traffic destined for the Northeast, from 78% to 84% for traffic destined to the Southeast, and from 72% to 77% for traffic destined to the Midwest. UP/SP-357, V.S. Barber at Exhibit 1. This gateway traffic should have been fully competitive and does not entail closed destinations on the UP system, but BNSF was able to only achieve, at most, a 6% increase in its market share, even at the height of the crisis. R.V.S. Grimm/Plaistow at 6. Certainly one cannot challenge a finding that UP dominates the market for rail traffic to the Northeast, where BNSF picked up only a 1% increase. Regardless, the issue for this oversight proceeding is not whether BNSF exerted



some competitive pressure, but whether or not BNSF has replicated SP's pre-merger market share and whether or not UP lost market share to and from certain locations, specifically the Northeast, Southeast, and Midwest.

UP points to the traffic gains of BNSF and Tex Mex during the service crisis as evidence that UP has not exercised any market power. Simply stating the volume of BNSF traffic growth over the trackage rights lines does nothing to account for reroutes of existing BNSF traffic (non trackage rights traffic) over those lines nor does it account for general economic growth and changes in commodity flows. R.V.S. Grimm/Plaistow at 3, n.1. Furthermore, without also providing corresponding volume gains on the UP, simply pointing to BNSF's traffic gains does not provide a meaningful comparison of the effectiveness of BNSF vis-a-vis UP, which is the real issue. To the extent these gains did occur, however, they were only for certain traffic and only to and from certain geographic destinations, and some of those gains are directly attributable to the existence of the ESO, which, in some ways, implemented parts of the Consensus Plan.<sup>6</sup>

Of course, UP is trying to have it both ways. UP cannot point to these traffic gains as evidence of competition in the Houston BEA, but at the same time ignore the fact those gains occurred during the period of the ESO. The fact that there were gains to BNSF and Tex Mex attributable to the ESO proves precisely why the Consensus Plan is

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<sup>6</sup> UP itself admits that a "portion of Tex Mex's gains may have occurred due to UP's service problems and [the] partial embargo in March of this year of traffic destined for the Laredo gateway." UP/SP-356 at 136, n. 30.



necessary. Absent the ESO and absent the Consensus Plan, BNSF and Tex Mex will not achieve these so-called traffic gains.

## **2. Disaggregated Houston Shippers**

UP continues to maintain that BNSF has been a competitive success in the exercise of its merger conditions. UP/SP-356 at 33. UP claims that BNSF's traffic volumes have steadily and dramatically increased and are approaching half of the total of Houston traffic. UP/SP 356 at 32. BNSF, on the other hand, is adamant about the fact that it has been severely limited in its ability to compete with UP. BNSF proclaims that "in a number of situations, including in particular, where BNSF has to rely on UP haulage and/or switching to serve "2-to-1" customers — the customers most significantly affected by the UP/SP merger, BNSF has often been unable to compete effectively with UP. From lack of cooperation and neglect to outright discrimination and manipulation of existing agreements, UP has forced BNSF into an inferior competitive position which fails to provide "2-to-1" shippers the clearly competitive service choice they had prior to the merger when UP and SP competed." *Comments of The Burlington Northern and Santa Fe Railway*, Finance Docket No. 32760 (Sub-No. 21), filed August 14, 1998 ("BNSF-7") at 3-4 (emphasis added).<sup>7</sup>

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<sup>7</sup> In a letter to the Board dated October 7, 1998, UP's counsel, Arvid Roach, again claimed that "BNSF is unquestionably providing highly effective competition using the rights it obtained as conditions to the UP/SP merger — and in many cases, further rights that UP has unilaterally provided to it." Mr. Roach went on to state that "Attachments 13 and 19 to BNSF's October 1 [1998] report show that traffic growth at these points has been dramatic indeed." A review of Attachments 13 and 19 reveals that these assertions are not valid with respect to the Houston/Gulf Coast area. First, Attachment 13 covers

Despite BNSF's own statements, UP continues to claim BNSF has had tremendous success in competing for 2-to-1 traffic, pointing to its annual oversight reports and increased BNSF volumes over the trackage rights lines. UP/SP-356 at 31-34. However, UP's reports with respect to the 2-to-1 traffic are not specific to the Houston/Gulf Coast market and do not account for Houston originations and terminations to and from the specific geographic destinations.<sup>8</sup>

To evaluate UP's statements, Dr. Curtis Grimm and Mr. Joseph Plaistow conducted a market share analysis of the 2-to-1 shippers located in the Houston BEA, which BNSF gained access to as part of Decision No. 44. *See* R.V.S. Grimm/Plaistow at 7-8. The analysis was conducted by drawing on the shippers identified by UP and BNSF as 2-to-1 shippers in the Houston area, then matching these shippers in the 1998 traffic tapes of UP and BNSF. The results are contained in Table 3 and show that even for this 2-to-1 traffic, to which BNSF received direct access as a result of the merger, UP

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switch/haulage loads delivered by UP for BNSF at 2-to-1 points in Texas. Attachment 13 therefore does not isolate the Houston/Gulf Coast area. It is largely undisputed that once BNSF's traffic moves off the UP system in Houston, BNSF has fewer service problems. This is borne out by BNSF's statement that it is trying to find ways to reroute traffic so as to bypass Houston on less congested routes in Texas e.g. through Temple. BNSF-PR-8 at 11. Second, Attachment 19 covers switch/haulage loads delivered by UP for BNSF at 2-to-1 points system wide. These statistics are also not a reliable indicator of BNSF's ability to serve 2-to-1 customers in the Houston/Gulf Coast area.

<sup>8</sup> For those specific examples in the Houston area, UP points to rock from Georgetown Railroad and sugar from Sugarland, Texas. UP/SP-356 at 32. UP also says there are numerous other Houston area 2-to-1 examples in its Confidential Appendices. *Id.* But none of these examples refute Dr. Grimm's essential point. Dr. Grimm would not dispute that BNSF has been effective for some 2-to-1 traffic to and from certain origins and destinations, but BNSF has not been effective in replacing SP for Houston BEA traffic to and from the Northeast, Midwest, and Southeast.



continued to maintain a 91% carload market share of this traffic during the service crisis. This analysis confirms BNSF's statements that it has not been able to effectively compete for 2-to-1 traffic.

**B.     The Merger Caused SP And UP Exclusively Served Shippers To Suffer Competitive And Service Harm**

The adverse impact of the UP/SP merger on so-called "1-to-1" shippers in the Houston/Gulf Coast region, warrants the expansion of the neutral switching district as proposed in the Consensus Plan. These Houston/Gulf Coast shippers have not only suffered most acutely during the 1997-1998 UP rail service crisis — a situation which could occur again — but also continue to face long-term competitive disadvantages vis-à-vis other producers (foreign and domestic) within their own industry sectors.

Several 1-to-1 shippers would benefit from increased competition in the Houston area by means of neutral switching, which is contained in two items of the Consensus Plan's request that the Board:

- "restore neutral switching in Houston that was lost when the UP and BNSF dissolved the HBT" (Item 2 of the Consensus Plan); and
- "expand the neutral switching area to include all customers currently located on the former SP Galveston Subdivision between Harrisburg Jct. and Galveston . . ." (Item 3 of the Consensus Plan).

Of course, Item 2 builds on the sound foundation of the established Houston neutral switching zones that have been successfully operated by PTRC and, prior to its dissolution, the HBT. Item 3 of the Consensus Plan, however, includes expanding neutral



switching to reach some 1-to-1 shippers, who would for the first time obtain access to competitive linehaul service. On its face, Item 3 appears to go beyond the pre-merger status quo in the Houston/Gulf Coast region. For that reason, it is necessary to examine the unique circumstances relating to rail competition in that region.

Providing neutral switching for these 1-to-1 shippers would alleviate the competitive problems created as a result of the merger, while also providing service alternatives that could assist such shippers in the event of future UP operational difficulties. It is simply not true that these shippers suffered no competitive harm as a result of the merger. While there are many other captive rail shippers (and receivers) located at points throughout the United States, the Board is well aware of the unique circumstances of the Houston/Gulf Coast rail market. The historical development of the chemical and plastics industries in that region has resulted in the existence of a number of exclusively served shippers on both UP (former Missouri Pacific) and SP lines. In some cases, the same manufacturing company built or purchased separate plants that were each captive on one of those two competing rail systems.

A shipper with plants that are captive to two different railroads still has some economic leverage to bargain for better rates and services. R.V.S. Grimm/Plaistow at 11. For example, if the shipper has excess production capacity or intends to install additional capacity, it can offer traffic to the two railroads in order to obtain competitive benefits. But when those same two rail carriers merge, as happened in the UP/SP transaction, the shipper's leverage is completely eliminated. Even where plants producing the same commodity belong to different manufacturing companies, the merger reduced

competition because there were no longer an independent UP and an independent SP with concerns about keeping "their" captive shippers competitive in the marketplace. R.V.S. Grimm/Plaistow at 11. So while separate shipper facilities were treated as 1-to-1 points and accorded no protection in Decision No. 44, there was in fact a reduction in rail-to-rail competition in the Houston/Gulf Coast region among those shippers. R.V.S. Grimm/Plaistow at 9-13.

Perhaps the best real-world illustration of this aspect of the UP/SP merger is the plastics industry, which produces about 90 billion pounds of resins each year — 80% of which is manufactured in the Gulf Coast region. Most plastics resins are stored in hopper cars and ultimately shipped by rail. No other mode provides the storage and transportation service that plastics shippers and their customers require. Many plants are 1-to-1 points. Yet given the plastics industry's concentration in Texas and Louisiana, where most 1-to-1 points were served by either UP or SP, that merger sharply reduced competition. This effect was foreseen by the Society of the Plastics Industry, Inc. (SPI) in its evidentiary submissions to the Board. *See Comments of the Society of The Plastics Industry, Inc., Finance Docket No. 32760, filed March 29, 1996 ("SPI-11")* at 19-28. The last two years have shown that the UP/SP merger did reduce the leverage available to plastics shippers, who also bore the brunt of UP's service failures. *Rebuttal Verified Statement of Larry L. Thomas ("R.V.S. Thomas")* at 3-5.

The expansion of the geographic limits of the proposed neutral switching area would enhance the public interest by providing 1-to-1 shippers with competitive service packages, as well as effective access to alternative linehaul carriers in the event of another

major service failure. UP states that the mere fact that it did not turn over all of its exclusively served business to competitors during the service crisis is not an exercise of merger-related market power because those shippers would have been exclusively served with or without the merger. UP/SP-356 at 70. UP thus claims these exclusively served shippers suffered no merger related harm. This is simply wrong. While those shippers may have been exclusively served prior to the merger, they were not all exclusively served by UP. Some were SP exclusively served shippers.

These SP shippers did suffer merger-related harm during the service crisis due to UP's market power because prior to the merger, if UP had a service crisis, these exclusively served SP shippers were not subject to UP's switching, dispatching, or operating practices and thus would not have been impacted by a service crisis on the UP. (Similarly, UP exclusively served shippers would not have been impacted by SP's 1978 meltdown). All of these SP and UP exclusively served shippers are now subject to UP's operating, switching, and dispatching practices, which means that the effects of a service crisis are now much worse on exclusively served shippers than they were before the merger.

UP attacks the expansion of the neutral switching limits by arguing that the premise that every exclusively served shipper on a merging railroad should be opened to permanent competition so that there will be alternative service in the event of an emergency is "absurd." As the Board has established a separate rulemaking proceeding to determine under what circumstances exclusively served shippers should have access to



alternative carriers in the event of a service emergency,<sup>9</sup> the suggestion is not absurd, but generally in line with the Board's thinking.

Nonetheless, the Consensus Parties do not argue that "every" exclusively served shipper on a merging railroad be opened to permanent competition — only those Houston/Gulf Coast shippers who have suffered some service or competitive harm due to the merger. There must be some relationship between the merger and the loss of a service option. For Houston, this is only a small number of former exclusively served UP or SP shippers, essentially the Bayport Loop shippers. These 1-to-1 shippers did suffer both a competitive and service harm as result of the merger. Nonetheless, for the vast majority of other Houston shippers, especially former HBT and PTRR shippers, the Consensus Plan does not "open up" new competition, but merely restores a service and competitive option that was lost due to the merger.

**C. There Are Fundamental Deficiencies In The Structure Of The Houston/Gulf Coast Market Which Prevent BNSF From Providing Effective Competition**

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Even if the Board disagrees with particular aspects of the Grimm/Plaintiff market study, there is more than sufficient evidence in the record to make a finding that additional remedial conditions are necessary. BNSF itself has admitted it suffers from certain fundamental structural problems with its existing trackage rights. BNSF's difficulties in acting as a competitive check to UP are not surprising. The United States Department of Transportation ("DOT") explains the problem as follows: "where, as here,

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<sup>9</sup> See 63 Fed. Reg. 27253 (May 18, 1998).

a tenant railroad must compete over thousands of miles of the landlord carrier's system, the former is necessarily vulnerable to the problems of the latter — even without considering the inherent possibility of discriminatory treatment.” *Comments of the United States Department of Transportation*, Finance Docket No. 32760 (Sub-Nos. 26-32), filed September 18, 1998 (“DOT Comments”) at 6. BNSF's vulnerability to the vagaries of the landlord-tenant relationship is particularly pronounced in the Houston/Gulf Coast area where UP's controls nine out of the eleven tracks that run through Houston, 70% of the switching and, until recently, controlled virtually all the dispatching in the Houston terminal area.

BNSF has sought to reduce its vulnerability to this landlord-tenant relationship in various ways.<sup>10</sup> However, BNSF has realized that complete independence from UP, while desirable, is not possible. Therefore, in areas such as the Houston terminal where the joint operation over common lines is unavoidable, BNSF has attempted to secure a level of joint control to assure impartiality in the way operations are structured and carried out. To some degree, BNSF believes it has been successful in achieving such joint control.<sup>11</sup> However, BNSF has been severely limited in its ability to fulfill its role as an effective competitive check — a fact clearly evident from BNSF's continuing

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<sup>10</sup> For example, BNSF continues to look for ways to reroute BNSF traffic so as to bypass Houston. BNSF Application at 7.

<sup>11</sup> BNSF continues to rely on the Term Sheet Agreement, which provides for joint dispatching by BNSF and UP of a large part of the Houston/Gulf Coast area, as a success.

complaints<sup>12</sup> regarding its inability to fulfill the competitive role envisioned for it by the Board and BNSF's request for additional remedial conditions.

**1. Dispatching Discrimination Compounds BNSF's Inferiority**

In Decision No. 44, the Board expressly acknowledged that "the landlord's power to control dispatching is an important one," and that the Board might have been reluctant to rely on trackage rights to solve a competitive problem over such a large area without assurances that dispatching would be conducted without discrimination against the tenant carrier. However, since Applicants and BNSF had agreed upon a detailed written dispatching protocol, the Board felt that this would ensure that dispatching discrimination would not occur. Decision No. 44 at 132.

In its Second Annual Report on Merger and Condition Implementation,<sup>13</sup> UP stated that the BNSF-UP dispatching protocol had worked well. UP claimed that both parties had exercised their rights to monitor the dispatching of their trains by the other and that any issues that had arisen were quickly and cooperatively resolved. *Applicants' Second Annual Report on Merger and Condition Implementation* Finance Docket 32760 (Sub-No. 21) filed on July 1, 1998 ("UP/SP-344") at 59.

According to BNSF, the reality is very different. It appears that UP's account of the success of the dispatching protocol and the Board's belief that dispatching

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<sup>12</sup> As will be described in more detail below, BNSF has complained to the Board about the inequalities of the landlord-tenant relationship in every quarterly progress report that it has filed since October 1, 1997.

<sup>13</sup> See UP/SP-344.



discrimination would not occur were overly optimistic. In spite of continuing complaints, BNSF was continually subject to dispatching discrimination at the hands of UP until only recently. It was only when the Joint Dispatching Center was started on March 13, 1998 that BNSF's complaints about dispatching discrimination in the Houston/Gulf Coast area subsided. BNSF, however, continues to complain about dispatching discrimination in other locations where it has trackage rights.<sup>14</sup>

In its Quarterly Progress Report filed October 1, 1997,<sup>15</sup> BNSF complained that UP's dispatching of the former SP routes between Houston and Memphis and between Houston and Iowa Junction was resulting in UP trains with lower priority receiving preference over BNSF trains with higher priority which was in violation of the dispatching protocol. To remedy this problem, BNSF recommended that a Houston-area dispatch center be established to enable supervision by BNSF dispatchers of these routes, a concept surprising similar to that proposed by the Consensus Parties. BNSF-PR-5 at 6-7.

BNSF also complained that UP's dispatching of HBT lines was causing trains to be tied up which was adversely affecting the operations of PTRR and BNSF. To remedy this problem, BNSF recommended (again, consistent with the Consensus Plan) that PTRR take over on a temporary basis the dispatching of various routes through

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<sup>14</sup> See BNSF-7 at 10. BNSF's complaints are discussed in more detail below.

<sup>15</sup> *The Burlington Northern and Santa Fe Railway Company's Quarterly Progress Report*, Finance Docket No. 32760 (Sub-No. 21) filed October 1, 1997 ("BNSF-PR-5").

Houston.<sup>16</sup> Owing to its institutional knowledge of the area, trackage, facilities and customers, BNSF suggested that PTRAs would be the best organization to direct emergency operations to relieve congestion through the Houston area. BNSF-PR-5 at 6.<sup>17</sup>

Even though BNSF's operations continue to be hampered by dispatching discrimination in areas where it is subject to UP control, BNSF nevertheless opposes the proposal for neutral dispatching put forward by the Consensus Parties,<sup>18</sup> notwithstanding that: (i) BNSF was powerless to prevent dispatching discrimination in Houston prior to the implementation of the joint dispatching center;<sup>19</sup> (ii) it remains powerless to prevent dispatching discrimination in areas where it does not have a joint dispatching arrangement with UP;<sup>20</sup> and (iii) in those areas where it does not have a joint dispatching

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<sup>16</sup> See BNSF-PR-5 at 5-6. The routes included (i) the HBT lines; (ii) the SP route between Bridge 5A, Manchester Junction, Sinco Junction and Deer Park Junction; and (iii) the SP route between West Junction and Harrisburg Junction.

<sup>17</sup> BNSF subsequently dropped its request for neutral dispatching by the PTRAs because it was able to secure for itself a joint dispatching arrangement to the exclusion of Tex Mex. See *Request for Adoption of a Consensus Plan in Order to Resolve Service and Competitive Problems in the Houston/Gulf Coast Area*, Finance Docket No. 32760 (Sub-No. 26) filed July 8, 1998 ("Consensus Plan") at 47-48.

<sup>18</sup> *BNSF Comments, Evidence and Arguments on Requests for New Remedial Conditions In Additional Oversight Proceeding*, Finance Docket No. 32760 (Sub-Nos. 26, 30 and 32) filed September 18, 1998 ("BNSF-9") at 14.

<sup>19</sup> See BNSF-PR-5, Verified Statement of Ernest L. Hord ("V.S. Hord") at 6-8.

<sup>20</sup> See BNSF-7 at 10. BNSF states that despite UP's assertion that the dispatching protocol has "worked well," the reality is that there are far too many occasions on which UP has dispatched one of its trains over one of the trackage rights lines when the crew for that train did not have sufficient time to allow it to complete the movement. These occurrences have led to the lines being blocked while a replacement crew has been called in, and BNSF's service has been adversely affected.



arrangement, BNSF continues to call for neutral dispatching<sup>21</sup> or extended joint dispatching.<sup>22</sup>

Obviously, BNSF is no longer concerned about neutral dispatching in the Houston/Gulf Coast area, not because there has been a fundamental structural change so that the possibility for discrimination has been eliminated for all carriers operating in Houston, but only because it has been able to secure joint control with UP of dispatching in and around the Houston terminal area. Hence, its statement that neutral dispatching "would be at odds with the operations and mission of the recently-established joint dispatching center at Spring, TX," BNSF Application at 14, is understandable as self-serving to exclude KCS/Tex Mex from the Houston area. Of course, the solution for all of the parties is to establish a truly neutral dispatching center, or, at a very minimum, to allow Tex Mex to also participate in the management of the Spring dispatching center and give Tex Mex an equal role in selecting the neutral dispatcher that would oversee the entire Houston operations.

## **2. Switching Problems Severely Impede BNSF's Operations**

In Decision No. 44, the Board explained that at plants where no third carrier was present, UP/SP had granted BNSF access either directly through trackage rights or

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<sup>21</sup> See BNSF-7 at 11. BNSF states that it expects to follow up with UP to ensure that BNSF trains are dispatched in accordance with the dispatching protocol.

<sup>22</sup> In the BNSF Application, BNSF requested that the jurisdiction of the joint dispatching center be extended to UP directional routes between Houston and Longview, TX and between Houston and Shreveport, LA. BNSF claimed that this would assist BNSF and UP in scheduling and coordinating movements over these lines into and out of Houston. BNSF Application at 14.



through reciprocal switching. The Board predicted that the trackage rights BNSF had been awarded and the switching arrangement would enable BNSF to function effectively as a replacement carrier for SP. Decision No. 44 at 121.

In its Opposition to Condition Applications filed on September 18, 1998, UP claims that the switching of individual Gulf Coast customers remains consistent and as timely as before the crisis. UP further claims that since the first week in June, the large group of customers that UP monitors has requested and received switches more than 96% of the time, and UP has been switching within the required period of time at the same level of consistency. UP/SP-356 at 76.

According to BNSF, the reality is very different. UP's erratic and discriminatory switching practices have proved to be one of the most intractable elements of the UP-BNSF landlord-tenant relationship. BNSF has stated that "UP's [switching] service for BNSF has proven erratic and unworkable when provided pursuant to the Settlement Agreement — a remarkable occurrence because reciprocal switching has been a standard railroad service which works everywhere else, and has for most of the past century, between many carriers in many venues." BNSF-7 at 5.

In its Quarterly Progress Report filed October 1, 1997, BNSF first complained that UP's switching practices were causing shipments from the Baytown Branch to move in error via UP to Englewood instead of via BNSF from Dayton in spite of customers' routing instructions. To remedy this problem, BNSF recommended that neutral switching, another concept called for in the Consensus Plan, be established on the former

SP's Baytown Branch under the direction of the PTRAs to assure expeditious handling of traffic for interchange to both UP and BNSF destinations.<sup>23</sup>

In its Quarterly Progress Report filed July 1, 1998 ("BNSF-PR-8"), BNSF asserted that the Spring Consolidated Dispatching Center had significantly helped the situation, but that various operational problems in Houston and the Gulf Coast area still were adversely affecting BNSF's ability to compete with UP. BNSF-PR-8 at 8-9. This included (i) discrimination by UP in favor of its own trains over the trains of other carriers<sup>24</sup> and (ii) erratic and unpredictable service provided by UP via reciprocal switch and haulage.<sup>25</sup> BNSF referred to various proposals that its representatives had made to UP to overcome the operational handicaps<sup>26</sup> but that UP had refused to accept any of BNSF's proposals. As a result, BNSF stated that it was intending to file a request for additional remedial conditions in the present proceeding. BNSF-PR-8 at 11.

In the BNSF Application, BNSF described various problems with switching that it had experienced with (i) customers in the Houston terminal seeking to use BNSF service from points BNSF gained access to as a result of the UP/SP merger and (ii) customers

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<sup>23</sup> See BNSF-PR-5, V.S. Hord at 8.

<sup>24</sup> For example, BNSF described how Baytown Branch shipments moving via haulage on the UP have often been delayed because UP gives preference to its trains over BNSF trains, otherwise fails to switch BNSF trains in a timely manner, or does not deliver outbound cars to BNSF at the Dayton, TX interchange. See BNSF-PR-8 at 10.

<sup>25</sup> For example, BNSF described how it was experiencing alternating cycles of several days of sporadic improvement in UP service followed by a number of days when service would return to near crisis levels. See BNSF-PR-8 at 10.

<sup>26</sup> These proposals relate to the rerouting of BNSF traffic to less congested UP routes and BNSF joining UP directional operations in additional corridors.

accessed by BNSF in the Houston area via reciprocal switch service from UP. These customers were continuing to find that their traffic was being delivered unreliably and late. This was partly because UP had failed to adequately perform its switching or haulage functions for BNSF and its customers. BNSF-PR-8 at 11.

On the Baytown and Cedar Bayou Branches, switching options provided by the BNSF Settlement Agreement were insufficient to provide customers with access to competitive BNSF service. BNSF suggested that these switching problems could be resolved if operations on the Baytown and Cedar Bayou Branches were to be directed on a neutral basis by a third party using UP and BNSF personnel already in place to conduct the switching operations. BNSF-PR-8 at 25.

On the Clinton Branch, UP's inefficient coordination of the Clinton Branch and its discriminatory policies were leading to backups and delays. BNSF recommended that the Clinton Branch be operated by the PTRC which would be in a better position than UP to monitor and manage on a neutral basis inbound grain flows to the Houston Public Elevator.<sup>27</sup>

In spite of its own request for the introduction of neutral switching by the PTRC, in its Comments on Requests for New Remedial Conditions filed September 18, 1998, BNSF opposed the proposal by the Consensus Parties for the expansion of the Houston

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<sup>27</sup> See Verified Statement of Peter J. Rickershauser ("V.S. Rickershauser") in support of the BNSF Application at 27. BNSF's concerns may relate more to the geographic size of the proposed neutral switching district than the concept of neutral switching itself. The Consensus Parties have reason to believe that BNSF would support the Consensus



neutral switching area. BNSF claimed without giving reasons that "this request would not improve operations in the Houston/Gulf coast area or preserve pre-merger competition, but instead would result in significant additional rail carrier access to shippers." BNSF-9 at 13.

**3. Insufficient Access to Yards in Houston Previously Impeded BNSF**

In Decision No. 44, the Board referred to the fact the CMA settlement agreement, which augmented the BNSF Agreement, provided for BNSF access to a number of yards, including Dayton Yard, which would supply some of the needed additional storage capacity. That agreement indicated that BNSF would have equal access to Dayton Yard and that UP/SP would work with BNSF to locate additional facilities on the trackage rights lines as necessary. Decision No. 44 at 152.

Notwithstanding these contractual undertakings by UP/SP, BNSF's yard access was limited and BNSF was hindered by not having its own yard in Houston. This situation changed on November 1, 1997, when BNSF and UP decided to restructure the operations of the HBT by dividing the operation of HBT between UP and BNSF. In a verified statement in support of the restructuring plan, HBT's General Manager, J.B.

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Parties' plan to provide neutral switching of the HBT and PTRS but that BNSF would not support that concept for those shippers located in the Bayport Loop.

Mathis, explained that the restructuring plan would enable BNSF to gain control over its own classification yard in Houston for the first time.<sup>28</sup>

In its Comments on Requests for New Remedial Conditions filed September 18, 1998, BNSF stated its support for the proposal of the Consensus Parties that Tex Mex needs its own yard in the Houston area to accomplish interchanges, setouts and pickups and general switching activity. BNSF recognized that the lack of adequate yard space for Tex Mex has caused and continues to cause problems in the Houston terminal. BNSF-9 at 18 (BNSF described how it has suffered interference with its operations as Tex Mex has blocked main lines in the terminal area and has added to the overall congestion in the Houston Terminal).

**4. Like Tex Mex, BNSF Is Prevented From Operating Over The Most Efficient Routes Through the Houston Terminal**

Presently, BNSF operations through Houston are restricted to the former HBT East and West Belt routes.<sup>29</sup> In the BNSF Application, BNSF complained that when

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<sup>28</sup> See Verified Statement of J.B. Mathis ("V.S. Mathis") at 2-3 in support of *UP/SP's Opposition to the KCS/Tex Mex Petition for Emergency Cease and Desist Order and Complaint* in *Texas Mexican Railway Company v. Houston Belt & Terminal Railway Company*, Finance Docket No. 33507 filed Oct. 31, 1997 ("UP/SP Opposition to HBT Complaint"). According to the restructuring plan developed by BNSF and UP, BNSF would (i) manage Old and New South Yards; (ii) serve the shippers located on HBT lines south of the GH&H railroad line connecting Congress Yard and Tower 85; and (iii) serve customers west of Belt Junction on the Old Rock Island. UP would (i) operate the Columbia Tap and (ii) operate HBT's industrial support yards and serve all industries on the remainder of HBT. The KCS/Tex Mex Petition For Consolidation, To Declare Exemptions Void Ab Initio, and to Revoke Exemptions, filed February 3, 1998, which argues that the proposed transaction was really a lease and not an exchange of trackage rights, is still pending.

<sup>29</sup> See V.S. Hord in support of the BNSF Application at 20.

these routes are congested, even though alternative routes are available, UP will not permit BNSF to use these lines unless prior trackage rights agreements are in place. In the same manner as the Consensus Parties, BNSF requested additional trackage rights, to be administered through the Spring Center, permitting it to operate over any clear through UP route available in Houston to improve velocity and ease congestion.<sup>30</sup>

In its Comments on Requests for New Remedial Conditions filed September 18, BNSF expressed its support for the proposal by the Consensus Parties that carriers operating through the Houston terminal should be granted trackage rights to use the best available routes through Houston, and not just the lines that they currently have trackage rights over. BNSF-9 at 8.

**D. There Are Fundamental Structural Deficiencies Which Prevent Tex Mex From Being An Effective Alternative To UP At Laredo**

UP argues that the Consensus Plan is not needed to make Tex Mex an effective competitor for traffic through Laredo. UP/SP-356 at 132-148. UP's arguments, however, ignore the serious obstacles which, as Tex Mex's experience since the merger has shown, have prevented Tex Mex from performing the competitive role that the Board intended in Decision No. 44.

In Decision No. 44, the Board granted Tex Mex's application for trackage rights between Robstown and Beaumont in order to preserve the second route for U.S.-Mexican rail traffic through Laredo that would compete with the UP's route through Laredo via

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<sup>30</sup> See V.S. Rickershauser in support of the BNSF Application at 28.



San Antonio as effectively after the UP/SP merger as it had before the merger, when SP was Tex Mex's principal interline connection for that traffic. Although UP proposed to give BNSF trackage rights over UP lines to Robstown, where it could interchange with Tex Mex, the Board was persuaded by Tex Mex's submission that BNSF would not be a full competitive replacement for SP for that traffic on that route. Decision No. 44 at 148-149. The Board found that BNSF would not have access to much of the traffic that SP had interchanged with Tex Mex and that BNSF would not be able to retain all of the SP traffic to which it did get access. The Board also noted that BNSF would receive trackage rights from UP to the Eagle Pass gateway to Mexico, and thus would likely divert traffic to that gateway that it would otherwise interchange with Tex Mex and route through Laredo. Accordingly, the Board concluded that Tex Mex needed a connection to another Class I railroad, the KCS at Beaumont, in order to preserve over its route the same level of competition with UP over the Laredo gateway as existed before the merger.

*Id.*

The Board, however, imposed a significant restriction on Tex Mex's trackage rights, prohibiting Tex Mex from using its trackage rights to carry any traffic that did not have a prior or subsequent movement over Tex Mex's own line between Laredo and Corpus Christi. Believing that this restriction would seriously hamstring its ability to be the effective competitor to UP that the Board intended, Tex Mex petitioned for reconsideration asking the Board to remove it. The Board declined to do so. That was before subsequent events revealed problems stemming from the merger that were not

only unprecedented in their impact on shippers but also were completely unanticipated by the Board, which received no warning of them from UP.

Experience since the merger has borne out Tex Mex's concerns and provides the Board more than enough reason to take actions and make adjustments that may not have seemed necessary two years ago. There are three fundamental structural problems that have combined to prevent Tex Mex from being as effective a competitive alternative to UP for U.S.-Mexican traffic through Laredo as the Board intended in Decision No. 44. First, without the Consensus Plan, Tex Mex simply does not have access to a sufficient amount of traffic and revenue to make it financially capable of making it an effective competitive alternative to UP. Second, Tex Mex remains subject to UP's dispatching control and is prevented from operating over the most efficient routes through Houston. Tex Mex's route requires Tex Mex trains to travel 422 miles between Laredo and Houston, 289 of them over UP tracks subject to UP dispatching control, compared to UP's 348-mile route over its own tracks via San Antonio. Third, Tex Mex lacks a yard in Houston, without which Tex Mex cannot operate effectively. See Consensus Plan, Vol. 1 at 69-77.

Three items of the Consensus Plan in particular would largely remedy these problems and greatly reduce Tex Mex's dependence on and vulnerability to UP:

- (i) eliminating the restriction on Tex Mex's trackage rights; (ii) requiring UP to sell and permitting Tex Mex to restore the out-of service line between Victoria and Rosenberg; and (iii) requiring UP to sell or lease one of its yards in Houston to Tex Mex at a

reasonable rate.<sup>31</sup> UP must see some benefit to Tex Mex's proposal to spend an estimated \$65 million to acquire and restore the 88-mile out-of-service line between Victoria and Rosenberg, otherwise UP would not enter into negotiations for the sale of the Wharton Branch. See UP/SP-356 at 213-17. This restoration would add much needed infrastructure to the Texas Gulf Coast region, would reduce the length of Tex Mex's route between Laredo and Houston by 70 miles, and would take Tex Mex off of 157 miles of UP trackage, including the heavily congested Glidden Subdivision now used by UP, BNSF, Tex Mex and Amtrak.

These three items of the Consensus Plan, however, are interdependent. Tex Mex needs the Victoria-Rosenberg line in order to be a fully effective competitor to UP for traffic through Laredo. However, Tex Mex could not generate sufficient revenues to economically justify the very substantial investment that would be required to acquire and restore the Victoria-Rosenberg line, and would not make that investment, unless the restriction on Tex Mex's trackage rights were eliminated. At the same time, and as discussed more fully below, Tex Mex clearly needs a yard in Houston in order to adequately and efficiently handle traffic to, from and through Houston.

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<sup>31</sup> Our reference here to these three items is not to suggest that the other items of the Consensus Plan are less important, but rather to indicate that these items are particularly relevant to remedying the obstacles that have prevented Tex Mex from being a fully effective competitor to UP for traffic through Laredo. The other items of the Consensus Plan are more relevant to remedying other competitive harms to the Houston/Gulf Coast region caused by the UP/SP merger.



**1. Without The Consensus Plan, Tex Mex Is Not Financially Capable Of Providing A Significant Competitive Alternative To UP**

UP's basic argument is that Tex Mex does not need any of the Consensus Plan items to be an effective competitor to UP for traffic through Laredo because it already is an effective competitor for that traffic. UP cites the projections made by Joseph Plaistow of what Tex Mex's traffic and revenues should have been after the merger if UP's service crisis had not occurred, and then asserts that "Tex Mex's actual experience has, in all significant respects, outstripped even these very positive projections of Mr. Plaistow's." UP/SP-356 at 135. This assertion, however, relates only to gross car counts and gross revenues; not to the critical bottom line. While the number of cars handled and gross revenues received by Tex Mex since the merger has grown beyond what the model predicted, Tex Mex's costs have grown even more. In terms of what is relevant to a carrier's long term ability to provide adequate and competitive service, Tex Mex's "actual experience" is that it lost \$1,193,000 in 1997. Consensus Plan, Vol. 1, V.S. Plaistow at 9.

There is thus no truth to UP's assertion that "[t]he UP/SP merger as conditioned by the Board has turned out to be far more beneficial to Tex Mex than Tex Mex predicted would be the case even if the Board had granted it the full unrestricted trackage rights it sought in the merger proceeding." UP/SP-356 at 137. Operating at an annual net revenue loss of almost \$1.2 million is hardly "beneficial" by any accounting standard.<sup>32</sup>

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<sup>32</sup> In contrast, in the merger proceeding, Tex Mex's expert witness, Patrick Krick, projected that Tex Mex would have a net income in 1997 of \$269,000 if it were granted

Clearly, Tex Mex could not long operate in that fashion and continue to function as "an effective competitive alternative to UP's routing into the border crossing at Laredo," which the Board intended to preserve in Decision No. 44. Decision No. 44 at 149.

UP, however, argues that this actual experience is irrelevant to the question of Tex Mex's competitive effectiveness. UP's arguments on this point do not withstand scrutiny. First, UP claims that Tex Mex's loss in 1997 resulted from congestion caused by UP's service failures, and that "[t]his phenomenon, however, affected all carriers serving Texas and is purely transitory." UP/SP-356 at 139. While UP's service failures undoubtedly contributed to Tex Mex's operating loss, all of the other impediments to Tex Mex's trackage rights were important contributing factors.

Furthermore, whatever effect UP's service failures may have had on UP or other carriers is quite beside the point. The question is whether, with the trackage rights the Board granted it, Tex Mex has been able to function as an effective competitive alternative to UP for traffic through Laredo, as the Board intended in Decision No. 44. Evidence of its experience since the merger was consummated indicates compellingly that it has not. The \$1.2 million dollar loss in 1997 is just a number, but the actual experiences it represents are innumerable instances over the past two years of Tex Mex trains standing for days, sometimes through as many as six 12-hour crew shifts, waiting for clearances from UP dispatchers; of UP dispatchers routing Tex Mex trains many

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unrestricted trackage rights. TM-23, Verified Statement of Patrick Krick ("V.S. Krick") at 192; TM-34, V.S. Krick at 3.

unnecessary miles when much shorter routings were available; and of many other experiences all of which made it utterly impossible for Tex Mex to provide viable competitive service to its customers.<sup>33</sup>

The truth of that conclusion is in no way undermined or refuted by the fact that UP's service failures also affected UP and other carriers serving Texas. In Decision No. 44, the Board imposed conditions to ensure that the merger that UP and SP wanted to effect did not result in anticompetitive consequences. If the merger, or other actions for which UP bears responsibility, have prevented the conditions from having their intended effect, UP cannot legitimately object to an adjustment of those conditions on the ground that it has also been hurt by those actions.

UP's claim that the conditions that required Tex Mex to operate at a substantial loss in 1997 are "purely transitory" likewise provides no basis for not adjusting the conditions that were imposed to ensure that Tex Mex will be the effective competitor the Board intended. UP's claim that the problems of the past two years are over and will not recur is simply UP's prediction of the future. If the evidence shows that what has actually happened since the merger has prevented Tex Mex from being the effective competitor that the Board intended, UP's hope for the future is not a rational basis for declining to make appropriate adjustments to the conditions imposed. UP certainly did

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<sup>33</sup> These instances are set forth in greater detail in the verified statements of Patrick Watts, Tex Mex's Vice President-Transportation in TM-7/KCS-7 at 156-166 and in the Consensus Plan, Vol. 1 at 384-385.



not predict its post-merger service failures in its case to the Board supporting the merger. UP cannot trump actuality with speculation.<sup>34</sup>

The fact that BNSF in the merger obtained its own direct routes to Eagle Pass and Brownsville to which it can divert traffic that might otherwise go through Laredo in interchange with Tex Mex makes it a serious possibility that even if Houston/Gulf Coast operations return to "normal" and UP eliminates its discriminatory dispatching practices, the Tex Mex is at risk of losing significant revenues. As shown in Tex Mex's response and objections to BNSF's request for trackage rights between San Antonio and Laredo, BNSF has in fact diverted large amounts of traffic to Eagle Pass and away from a Tex Mex-Laredo routing between March and July 1988 and has so far refused to enter into a long-term divisions agreement with Tex Mex. TM-17, V.S. Skinner at 7-8.

Finally, UP argues that Tex Mex's ability to operate profitably over its lines is irrelevant to its effectiveness as a competitor to UP because it has strategic value as a link between two other railroads, TFM and KCS, which are owned by Tex Mex's owners, TMM and KCSI. Because of this strategic value, UP argues, KCSI and TMM would keep Tex Mex alive and operating over its line and trackage rights whether or not it could do so profitably. UP/SP-356 at 142-148.

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<sup>34</sup> Furthermore, although UP's service over the past several months has certainly improved, it remains far below pre-merger levels, and UP may have benefited from below-normal grain shipments this Fall. In any event, the experience over the last few months should not be regarded as more indicative of post-merger normality than the disastrous situation that persisted for well over a year (despite UP's repeated promises of imminent recovery) and for most of the period since the merger was effected.

This argument is baseless. Whether Tex Mex can function as an effective competitive alternative to UP for traffic through Laredo, as the Board intended in Decision No. 44, depends entirely on the costs, impediments and other circumstances affecting Tex Mex's operations over its own lines and trackage rights, not on its relationship to other railroads. The higher the costs and other impediments (trackage rights restrictions, route circuitry, lack of yard space, restrictions, etc.) of Tex Mex's operations, the less competitive its service will be to UP's service, and if Tex Mex's costs exceed the revenues it can earn from its service, it will not be able to continue that service in the long run regardless of its relationship to other entities.<sup>35</sup>

## **2. Tex Mex's Trains Are Subject To UP's Discriminatory Dispatching Practices**

UP follows its regular approach to concerns raised by Tex Mex. First, it denies that there is a dispatching discrimination problem at all: "UP does not discriminate against trackage rights tenants." UP/SP-356 at 59. Second, it claims that it cannot admit or deny whether there is a problem: "It is virtually impossible for landlord railroads to disprove discrimination." UP/SP-356 at 52. Third, it begrudgingly admits that discrimination takes place: "If anything, they [Spring Center dispatchers] favor Tex Mex trains because they know that their treatment of those trains is under a microscope." UP/SP 356 at 204. Fourth, it diverts attention away from itself by claiming that Tex Mex

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<sup>35</sup> Even if TMM and KCSI were willing to indefinitely subsidize Tex Mex's operating losses — a dubious proposition — the amount of those subsidies would simply be a measure of the degree to which UP was shielded from effective competition for rail service through Laredo.

is the cause of the problem: "Tex Mex officials have never raised questions about the dispatching of their trains." UP/SP 356 at 204. Fifth, it sets out to destroy the dispatching discrimination claims that KCS/Tex Mex and the Consensus Parties put forward without even visiting the merits of most claims. UP/SP-356 at 205-8.

As will be seen, this is typical of the way in which UP deals with complaints of dispatching discrimination by KCS/Tex Mex and is the very reason why neutral dispatching is the only solution that will prevent this type of gamesmanship from continuing. The time has come for the Board to accept that UP has not honored its assurances to the Board in the UP/SP merger proceeding that dispatching would be conducted without discrimination.<sup>36</sup> UP has shown that the landlord's power to control dispatching has been abused and that the Board needs to act immediately to bring about the neutral and equal treatment of trains that it endeavored to in Decision No. 44.

a. UP Denies That a Discrimination Problem Exists

At various points, UP flatly denies that a dispatching discrimination problem exists. First, UP states that BNSF's unsubstantiated assertions of UP "favoritism" and "discrimination" are false. UP/SP-356 at 34. UP again states that Spring Center dispatchers are instructed to treat Tex Mex trains fairly and do not discriminate. UP/SP-356 at 60. UP later states again that "Spring Center dispatchers are told to treat all trains equally and that they do not discriminate." UP/SP-356 at 204.

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<sup>36</sup> In Decision No. 44, the Board stated that it was relying on assurances by UP/SP that dispatching would be conducted without discrimination. See Decision No. 44 at 132.



As a preliminary matter, to understand why UP so vigorously denies any claim of dispatching discrimination, it is necessary to refer to the Trackage Rights Agreements between UP and BNSF and UP and Tex Mex which were entered into as a result of the UP/SP merger proceeding. These agreements provide that "in the management, operation (including dispatching) and maintenance of the Joint Trackage, Owner and User shall be treated equally."<sup>37</sup> UP does not want to breach these agreements and this accounts for its denials of any and all claims of discrimination by Tex Mex and BNSF.

Even if one accepts that UP dispatchers are instructed never to discriminate against other rail carriers,<sup>38</sup> the idea that dispatching discrimination never occurs is totally implausible. To illustrate this point, Patrick Watts explains that UP dispatchers are instructed to obey railroad operating rules. However, sometimes they do not follow these rules. The issuance of rules by management does not automatically ensure that they are followed without a commitment by management to the enforcement of such rules. Similarly, the issuance of rules, such as the dispatching protocols and memoranda requiring fair dispatching does not guarantee that discrimination will not take place.

Rebuttal Verified Statement of Patrick L. Watts ("R.V.S. Watts") at 3. Troy Slinkard

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<sup>37</sup> See Section 2.4 of Exhibit B of Terms for Texas Mexican Railway Company Trackage Rights attached as Attachment A to the *Joint Submission of Primary Applicants and Tex Mex respecting terms for Trackage Rights Granted to Tex Mex in Sub-No. 13*, Finance Docket No. 32760 (Sub-No. 13) filed August 22, 1996.

<sup>38</sup> See Memo from Steve Barkley to All Train Management Personnel on November 6, 1997, where Mr. Barkley instructs that all trains are to be dispatched equally without discrimination "as we face continued review by the Surface Transportation Board." (UP/SP Bates No. N021-0001).

concedes that dispatchers in the Spring Center are overworked and under immense pressure.<sup>39</sup> Under these circumstances, dispatching discrimination (whether intentional or unintentional) can happen at any time. R.V.S. Watts at 4. UP's attempt to deny that this ever happens is disingenuous.

UP points to quantifiable data prepared by Jerry Wilmoth purporting to show that Tex Mex and BNSF trains receive equal and sometimes better treatment than UP's trains ("Wilmoth Study"). However, as Mr. Watts explains, the Wilmoth Study is fundamentally flawed for a number of reasons. First, the Wilmoth Study represents a very recent snapshot of train performance over a very limited period — August 11, 1998 through September 10, 1998. UP has been facing claims of discrimination by KCS/Tex Mex in this proceeding as early as October 1997, and by BNSF even before that. If UP were sincere about analyzing transit times to avoid discrimination it would have performed this study much earlier and on an ongoing basis. Thus, it would appear that the Wilmoth Study was prepared solely for the purpose of UP's Opposition and not out of a sincere desire to explore the discrimination claims that KCS/Tex Mex and BNSF have repeatedly made.

Second, the Wilmoth Study was prepared during a time when the treatment of Tex Mex trains by UP's Spring dispatchers was under a microscope. As a result, the Spring dispatchers were actually favoring Tex Mex trains and the claim by UP that Tex Mex and BNSF trains performed somewhat better than UP trains of the same class is therefore not

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<sup>39</sup> See UP/SP-358, V.S. Troy Slinkard at 2-3.



surprising. This is a point that UP readily acknowledges. UP/SP-356 at 204. In fact, discrimination in favor of tenant railroads is exactly what one might expect of a dispatcher being watched under a microscope.

Third, the Wilmoth Study fails to measure two critical areas where the bulk of the discrimination incidents arise — the Houston terminal area and the line between Flatonia and Placedo, TX. Even if one acknowledges the difficulties in assembling the requisite data for those segments, this fact does not cure the fundamental flaw in the Wilmoth Study, which is that it does not accurately represent the locations where the discrimination occurs.

Fourth, even if the Board decides to accept the Wilmoth Study with its flaws, there is absolutely no indication that the discrimination problems will cease after this proceeding is over. In view of UP's repeated denials that dispatching discrimination occurs and its failure to establish a neutral dispatching system which would eliminate the incentives for discriminatory dispatching, there is every reason to believe that UP will simply go back to business as usual after this proceeding is over. R.V.S. Watts at 3.

UP refers to a letter written by Mr. Watts to his former SP supervisors where Mr. Watts states that he doubts that any UP dispatcher intentionally mishandles SP trains. While Mr. Watts did in fact make that statement over six years ago, UP omits to mention that Mr. Watts went on to explain that "UP's upper management has been responsible for assigning our "hot" [high priority] trains a low priority in their Computer Aided



Dispatching ("CAD") system."<sup>40</sup> The problem that Mr. Watts is describing exists in the Spring Center to this day: most dispatching discrimination is not malicious but takes the subtle form of assigning lower priorities to Tex Mex trains. This problem is clearly evident in the dispatching discrimination incidents that Mr. Nichols and Mr. Watts describe in their verified statements in support of the Consensus Parties' Request.

b. UP Admits that It Cannot Disprove Discrimination Claims

After repeatedly stating that dispatching discrimination does not occur, UP then states that "it is virtually impossible for landlord railroads to disprove discrimination claims." UP/SP-356 at 52. Troy Slinkard offers support for this assertion in his verified statement by acknowledging that he cannot recall particular dispatching incidents unless he makes a note of them, UP/SP-358, V.S. Troy Slinkard at 7, and that the likelihood of one of his dispatchers remembering a particular incident is even more remote owing to the fact that they perform thousands of dispatching actions in a 24-hour period.<sup>41</sup>

On the other hand, the possibility that Tex Mex's accounts of dispatching discrimination are inaccurate is negligible. Mr. Nichols is required to document all instances of discrimination that he observes in his capacity as a neutral observer as they

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<sup>40</sup> See letter from Patrick Watts to Mr. C. T. Shurstad on June 28, 1992 in Appendix A of UP/SP-356.

<sup>41</sup> UP/SP-358, V.S. Troy Slinkard at 3. The Consensus Parties applaud UP's recognition that a number of dispatchers in the Spring Center are overburdened and UP's resulting decision to subdivide the STO-2 territory in Houston. Mr. Watts proposed this subdivision in his verified statement on July 2, 1998 in support of the Consensus Plan and it appears that part of his proposal has been accepted by UP. See UP/SP-356 at 53, n.14. However, the Consensus Parties continue to maintain that the dispatchers of STO-2 and the new STO-3 territories should be neutral.

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take place and Mr. Watts based his discrimination claims on objectively verifiable evidence provided by UP's Digicon tapes. If UP was so confident that Mr. Watts' discrimination incidents were incorrect, then it would have gone back to the Digicon tapes and refuted Mr. Watts' testimony on the basis of those tapes. Instead, UP relies on the memory of Troy Slinkard, which Troy Slinkard himself admits is unreliable when he does not take notes. UP/SP-358, V.S. Troy Slinkard at 5 and 7. Therefore, if anyone is to be believed, it is Mr. Nichols, who took contemporaneous notice of the incidents and Mr. Watts, who studied the Digicon tapes.

c. UP Admits that Dispatching Discrimination Occurs

After denying that dispatching discrimination occurs and then admitting that it cannot disprove or prove discrimination, UP then admits that dispatching discrimination does occur. First, UP states that "UP trains were in fact delayed to give a Tex Mex train preferential handling." UP/SP-356 at 52. Second, UP states that "if anything, [Spring Center dispatchers] favor Tex Mex trains because they know that their treatment of those trains is under a microscope." UP/SP-356 at 204. Third, UP states that the Wilmoth Study shows that "Tex Mex trains enjoy better transit times than comparable UP trains on all segments." UP/SP-356 at 201.

These allegations by UP are troubling because they confirm that dispatchers do in fact discriminate in favor of one rail carrier over another. This discrimination is the very reason that the Consensus Parties have called for neutral dispatching. Mr. Watts explains that he does not want UP dispatchers to have the ability to discriminate for or against a



tenant railroad. R.V.S. Watts at 5. Neutral dispatching is therefore necessary to ensure that all trains are treated fairly by the Spring Center dispatchers.

d. UP Claims That Tex Mex is the Problem

UP attempts to divert attention away from itself by claiming that Tex Mex is the cause of the problem. First, UP claims that "Tex Mex officials almost never raise questions about the dispatching of their trains." UP/SP-356 at 204. Second, UP claims that when Tex Mex officials raise questions, they tend to do so long after the event rather than at the time when UP officials can look into the situation. UP/SP-356 at 204. Third, UP claims that Tex Mex failed to substantiate its claims of discrimination after being afforded two weeks to describe and document alleged instances of discrimination. UP/SP-356 at 202-3. Fourth, UP claims that KCS/Tex Mex are refusing to participate in joint dispatching at the Spring Center because they believe they still have a chance of wresting commercial conditions from the Board. UP/SP-356 at 209. Before dealing with each of these allegations separately, the Consensus Parties wish the Board to note that UP's determination to blame Tex Mex for each and every one of its dispatching problems demonstrates why neutral dispatching is required and why the dispatching protocols do not work.

It is simply untrue that Tex Mex officials almost never raise questions about the dispatching of their trains. Mr. Nichols points out in his verified statement in support of the Consensus Plan that whenever he observes discrimination or unfair treatment against Tex Mex trains, he attempts to intervene immediately by offering suggestions and advice to the Spring Center dispatchers on how to resolve the problem. Although Mr. Nichols

has a vast knowledge of the Houston terminal area and surrounding territories, his suggestions are ignored because he is a Tex Mex employee. Mr. Nichols' only remaining recourse is to report the incident to the joint corridor manager and by that time it is already too late to prevent the incident from occurring. Consensus Plan, Vol. 1, V.S. Nichols at 3. Even when claims of discrimination are presented to it, UP purports to investigate them and then denies them in the same manner as it does now.

UP claims that Tex Mex failed to substantiate its claims of discrimination after being afforded two weeks to describe and document alleged instances of discrimination. UP/SP-356 at 202. This is a distortion of the ruling of the ALJ in a discovery conference held on August 27, 1998, where ALJ Grossman held that KCS/Tex Mex was required to support any further allegations of discriminatory treatment with underlying documentation.<sup>42</sup> Since Mr. Watts was not afforded a further opportunity to review the Digicon tapes for the two week period in question subsequent to the discovery conference, it is not surprising that KCS/Tex Mex did not come up with any new allegations of discrimination.

UP's emphasis on the failure by KCS/Tex Mex to produce further instances of discrimination is misplaced and represents a failure by UP to understand the true nature of the problem. The problem is not in the ability of KCS/Tex Mex to come up with more and more examples of discrimination for UP to deny. If the Board wanted to be sure that

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<sup>42</sup> See *Transcript of Discovery Conference*, Finance Docket No. 32760 (Sub-No. 26), August 27, 1998, at 34 (emphasis added).



at least some of the apples in a particular barrel were rotten, it would not require the claimant to pull every apple from the barrel to demonstrate this point. Similarly, the Board would not require KCS/Tex Mex to document every possible instance of dispatching discrimination in order to be satisfied that a pattern of dispatching discrimination exists. KCS/Tex Mex have provided the Board with over thirty examples of dispatching discrimination dating back to October 1997.<sup>43</sup> If the Board accepts the validity of these examples, which the Consensus Parties urge it to do, then a number of additional examples would not take the matter any further.

The examples provided by KCS/Tex Mex clearly show discrimination and UP's attempted "explanations" for this discrimination simply do not hold up to scrutiny.<sup>44</sup>

e. KCS/Tex Mex Are Not Simply Making Excuses

UP claims that KCS/Tex Mex merely offer a number of "excuses" for not participating in the Spring Center when the real reason is that they believe they still have

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<sup>43</sup> Indeed, Mr. Watts explains in his verified statement that a pattern of dispatching discrimination by UP has existed since 1992. The discrimination has historically abated at times of heightened ICC (and now Board) scrutiny. Thus, when SP complained to the ICC in 1994 about UP dispatching discrimination, the discrimination abated. After that proceeding was resolved privately between the parties, the UP recommenced its pattern of dispatching discrimination. Now the UP is again "under the microscope" and dispatching discrimination has abated. But the usual pattern will recommence unless the Board takes decisive action this time by requiring neutral dispatching as requested by the Consensus Parties. R.V.S. Watts at 3.

<sup>44</sup> See R.V.S. Watts at 8-12. In his Rebuttal Verified Statement, Mr. Watts responds in detail to UP's characterizations of the incidents of dispatching discrimination described in the Consensus Plan and KCS-7. Mr. Watts also explains how UP's refusal to allow Tex Mex trains to run along the most efficient routes in the Houston terminal is an unnecessarily obstructive act designed to increase congestion rather than reduce it. R.V.S. Watts at 7.



a chance of wresting commercially valuable conditions from the Board. UP/SP-356 at 209. Before responding to these "excuses," the Consensus Parties wish to reiterate their position that the discrimination allegations are not about wresting commercially valuable conditions from the Board, but stem from a deeply held belief that the joint dispatching center is not neutral, does not treat all rail carriers equally despite the Dispatching Protocols, and that the Board's powers must be invoked to bring about what the Board has referred to as the need for "equal treatment of all trains without regard to ownership." Decision No. 44 at 132.

Excuse No. 1. UP alleges that it does not want Tex Mex to be an observer only showing up infrequently at the Spring Center. UP wants KCS/Tex Mex to participate in the management of the Spring Center but according to UP, KCS/Tex Mex refuse to even discuss the matter. UP/SP-356 at 210. Mr. Watts responds by saying that KCS/Tex Mex have never refused to discuss any matter regarding the Spring Center. Instead KCS/Tex Mex have been very clear about what they would like to see in terms of the structure of the Spring Center. R.V.S. Watts at 12. In fact, a document produced by UP in discovery, under the "confidential" designation, contradicts UP's statement that KCS/Tex Mex have refused to discuss the Spring Center. See R.V.S. Watts, Exhibit 1.

While UP continues to encourage KCS/Tex Mex to participate in the Spring Center, it always stops short of saying that KCS/Tex Mex can have an equal say in the center. R.V.S. Watts at 6. UP invites KCS/Tex Mex to negotiate an agreement along the same lines that BNSF was able to negotiate with UP. However, UP fails to mention that BNSF had to threaten to reopen the merger proceeding before UP was prepared to

negotiate the joint dispatching arrangement which now exists at the Spring Center.<sup>45</sup>

Negotiating an agreement for neutrality is clearly not as easy as UP suggests. If it were that easy, such an agreement would be in place by now.

Excuse No. 2. UP argues that KCS/Tex Mex should make use of the Dispatching Protocols which guarantee neutral dispatching and which are the same protocols BNSF and UP use. It should by now be apparent to the Board that the Dispatching Protocols are not enough to guarantee fair dispatching treatment. As discussed elsewhere in this filing,<sup>46</sup> BNSF's quarterly progress reports are filled with complaints about violations of UP of the Dispatching Protocols. Even to this day, BNSF complains about violations of the Dispatching Protocols in areas where it does not have joint control with UP over dispatching. Tex Mex has no way to stop these violations from occurring and UP simply denies that they occurred at all. UP has been able to resist the requests of KCS/Tex Mex for neutral dispatching because KCS/Tex Mex do not wield the same amount of clout as BNSF does. However, the Consensus Parties urge the Board to recognize that KCS/Tex Mex's request for equal and fair dispatching treatment is no less meritorious than that of BNSF.

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<sup>45</sup> See letter from Robert Krebs to Richard Davidson dated February 6, 1998 ("If we cannot reach an agreement that closely parallels our proposal [for joint dispatching], we will most likely ask the Board to reopen your merger case and to order divestiture of the eastern portion of the SP system."). This letter is included in the evidentiary supplement of the Consensus Parties' Request.

<sup>46</sup> See page 37 of this Rebuttal.

Excuse No. 3. UP argues that Mr. Watts and Mr. Nichols should "speak up" promptly if they have any questions or complaints. UP/SP-356 at 211. UP has already made this argument earlier when it suggested that Tex Mex officials almost never raise questions about the dispatching of their trains. The Board is referred to the discussion above which responds in detail to that unsupported assertion.

UP justifies its failure to invite Mr. Nichols to the joint meeting at the Spring Center on June 18, 1998, with the excuse that Troy Slinkard believed that Mr. Nichols was not a Tex Mex employee. UP/SP-356 at 211. However, UP does not explain why it failed to invite another Tex Mex employee if it was uncertain of Mr. Nichols' status with Tex Mex. Even though Troy Slinkard opted not to invite Mr. Nichols to the meeting, another employee of Tex Mex should have been invited. This is further evidence of the subordinate status of Tex Mex at the Spring Center.

### **3. Tex Mex Needs Yard Space**

Despite UP's protests, Tex Mex's need for yard space in Houston remains clear, not only with respect to northbound traffic but also with respect to southbound traffic moving to Corpus Christi, Laredo and Mexico. Tex Mex needs access to a yard in Houston in order to perform switching service and to assemble trains for movement, as well as for interchange with other rail carriers. While UP resists this aspect of the Consensus Plan on the grounds that it, UP, allegedly needs Booth Yard, UP overlooks the fact that the new neutral switching operations to be performed by PTRC would obviate UP's need for Booth Yard. UP's suggested alternatives to Tex Mex's proposed use of



Booth Yard either are not available to Tex Mex or are too remote to be usable as a switching and classification yard for Houston traffic.

UP's challenge to Tex Mex's stated need for use of Booth Yard is flawed because it proceeds from several dubious premises, including that Tex Mex suffers inefficient "double reverse handling" of cars only if they are destined to points north of Houston; that PTR, UP and BNSF adequately block cars for Tex Mex; and that the Consensus Plan's proposals to lift the northbound restriction on Tex Mex's trackage rights and for neutral switching of the Greater Houston Terminal Area will not take effect. All of these premises of UP's argument are wrong.

The Consensus Plan has demonstrated Tex Mex's genuine need of yard space in Houston, preferably Booth Yard. *See* Consensus Plan, Vol. 1 at 71-80 and 410-434. Contrary to its statement to the Board in 1996 that Tex Mex should establish a yard operation in Houston, *see Applicants' Submission Respecting Terms For Trackage Rights Granted To Tex Mex* (UP/SP-272), Finance Docket No. 32760 (Sub-No. 13 & 14), filed August 23, 1996, V.S. R. Bradley King at 9, a concept with which BNSF agreed in a June 17, 1998, letter, *see* Consensus Plan, Vol. 2 at 295, UP now contests Tex Mex's need for such operations. In large part, UP's challenge is based on its premise that Tex Mex will not need to haul cars interchanged to it in Houston to either Beaumont or Corpus Christi for classification and blocking prior to moving them back through toward their destination because (a) that sort of "double reverse handling," as UP calls it, occurs only on northbound traffic, and (b) BNSF, PTR and UP all block cars for Tex Mex. Both of these are faulty premises. UP cites Tex Mex documents produced by Tex Mex in

discovery as Nos. TM-8-HC-002082 - 002095 for the proposition that only northbound traffic suffers "double reverse handling." However, as shown in the attached Rebuttal Verified Statement of Paul L. Broussard ("R.V.S. Broussard") at 3, those documents show that over fifteen percent of the cars that suffered such double reverse handling were loads southbound from Houston. These inefficient moves all together cost Tex Mex over \$6,000 in trackage rights fees alone, to say nothing of added fuel costs, costs resulting from delay in movement of the freight, and other costs. R.V.S. Broussard at 3. Thus, UP is wrong in asserting that double reverse handling does not involve southbound loads. For this reason, Tex Mex needs yard space in Houston, to classify and block its own cars.

Moreover, Mr. Handley's indications that UP and BNSF, as well as PTR A, make up blocks for Tex Mex is wrong. Only PTR A, not UP or BNSF, blocks cars for Tex Mex. R.V.S. Broussard at 4. Thus, for freight received in interchange from BNSF or UP, this critical function is not performed for Tex Mex, again necessitating Tex Mex having access to its own yard space in Houston. For these and other reasons previously specified — e.g., the need to allow Tex Mex to interchange cars without blocking the East Belt, as it now must do on interchanging with PTR A especially, *see* Consensus Plan, Vol. 1 at 420-422 — Tex Mex continues to need yard space in Houston.

Booth Yard continues to be by far the preferable location for Tex Mex to use, for reasons previously specified by Mr. Broussard. Booth Yard's proximity to PTR A's North and Manchester Yards, in particular, make it ideal for fostering interchange with PTR A, with whom Tex Mex does the vast majority of its interchanges in Houston. Booth Yard also fits in well with Tex Mex's proposed reconstruction of the Rosenberg-Victoria



line, a line which UP admits will add useful south Texas infrastructure if rebuilt.<sup>47</sup> Booth Yard is the yard most efficiently located in the Houston area for a switching and classification yard that needs to handle interchanges with PTR A and to assemble and receive trains moving on the Rosenberg-Victoria line. R.V.S. Broussard at 11.

UP's response to Tex Mex's demonstrated need for Booth Yard is essentially the allegation that UP needs the yard more than does Tex Mex. This argument is specious for two reasons. First, before KCS and Tex Mex began pursuing obtaining Booth Yard in this proceeding, UP's CEO Dick Davidson responded as follows to a KCS/Tex Mex proposal for acquiring Booth Yard through purchase or lease:

**"Booth Yard**

As you know, we are using every available track in the Houston area. Booth Yard provides us with badly-needed SIT and overflow capacity. . . . In addition, your plan to use Booth Yard as a switching facility in Houston would be disruptive."<sup>[48]</sup>

Subsequently, however, UP has developed an ever-shifting series of "uses" for Booth Yard which it has insisted make it essential for UP to retain Booth Yard. Even assuming

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<sup>47</sup> Indeed, UP's Michael Ongerth calls SP's cessation of operations on the Rosenberg-Victoria line "SP's worst major capacity error" in the Houston area. UP/SP-358, V.S. Ongerth, Tab 11 at 12.

<sup>48</sup> Contrast this with UP's revisionist version of history in its September 18 filing where it states, "When UP assumed control of Booth Yard from HBT in the fall of 1997 . . . UP moved quickly to make more effective use of this well-located facility." UP/SP-356 at 223. Apparently to UP taking more than 4 months — from the October 31 dissolution of HBT to sometime after the February 27 date of Mr. Davidson's letter — is acting "quickly." Moreover, to the best of Tex Mex's knowledge, UP has yet to commit to any schedule for rehabilitating Booth Yard. See *1998 Authorization for Expenditure on Texas Projects* dated as of April 15, 1998.



that UP does use Booth Yard as it says and does not merely use it for car storage, as its CEO said, the presence of PTRAs as neutral switchers of the Greater Houston Terminal Area would alleviate UP of that responsibility, enabling PTRAs to handle those operations at whichever yard was most appropriate and relieving UP of the need for Booth Yard. R.V.S. Broussard at 7. Thus, UP's stated "need" for Booth Yard is overstated, particularly when neutral switching operations in Houston are commenced.

UP's proffered alternatives to Tex Mex's planned use of Booth Yard each have significant drawbacks from an operational point of view. First, of course, UP suggests that Tex Mex should look to BNSF, which has a mere 4 yards in the Houston terminal, rather than to one of the 21 yards controlled by UP, in seeking to satisfy Tex Mex's need for yard space. Obviously, this is merely an attempt by UP to use Tex Mex to limit BNSF's operations in Houston, and should not be considered even momentarily by the Board. UP's assertion that even BNSF's currently limited Houston yard space is underutilized indicates that BNSF is indeed a weak competitor in the Houston market.<sup>49</sup>

UP's suggestion that Tex Mex substitute use of North or Manchester Yards for Booth Yard is unworkable because Tex Mex does not have rights to use those facilities for switching and classification.<sup>50</sup> As for the suggestion that Tex Mex should use Glidden

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<sup>49</sup> When Tex Mex once proposed that the Board allow Tex Mex to use a portion of Old South Yard, BNSF objected vigorously. *Report of BNSF Pursuant to Supplemental Order No. 1 to STB Service Order No 1518*, filed Dec. 12, 1997, at 2.

<sup>50</sup> Also, Tex Mex is constrained by a lack of trackage rights needed for efficient access to Manchester Yard. On occasion, this has resulted in UP dispatchers routing Beaumont-bound Tex Mex trains out of Manchester Yard through Harrisburg Junction and as far as 25 miles west to Sugarland, TX, where the Tex Mex train was directed onto a siding so

or Chaney Yards, UP's Michael Ongerth's statement, UP/SP-358, V.S. Ongerth at 12, shows that those yards have been mostly or completely dismantled, and are therefore of little or no immediate use to Tex Mex. UP's suggestion that Tex Mex construct a switching and classification yard on the Rosenberg-Victoria line is simply impractical as the distance involved between that point and, for example, PTR's North Yard, a distance of approximately 40 rail miles, would require such extended switching movements that delay and unnecessary costs would doubtless result. By contrast, a yard on the Wharton Branch would be ideal for car storage because it would remove the cars from the working yards of the crowded terminal area but would allow reasonable access to them when they were occasionally needed, much as UP uses its Lloyd Yard north of Houston to hold cars for shippers in the Bloomington and Freeport areas. R.V.S. Broussard at 6-7.

Tex Mex needs Booth Yard for switching its traffic destined both northbound and southbound from Houston. UP's operational concerns expressed in opposition to Tex Mex's use of Booth Yard would be alleviated by the implementation of the Consensus Plan, and UP's proposed alternative yards would not suit the needs of Tex Mex and Houston shippers nearly as well as would Tex Mex's use of Booth Yard. Accordingly, the Board should grant Item 7 of the Consensus Plan. Whatever UP's shifting description

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its locomotives could run around the train and begin the journey eastward toward their intended destination of Beaumont.



of its use of Booth Yard may be at the moment, that function could also be accomplished by the Consensus Plan's neutral switching carrier.

**III. UP IS USING ITS MARKET POWER TO REDUCE SERVICE AND INVESTMENT IN THE HOUSTON/GULF COAST MARKET**

**A. UP Continues To Provide Poor Service**

**1. UP's Poor Service Is An Indication That BNSF Is Not An Effective Replacement For SP**

It is axiomatic that harm from a merger may occur from either a reduction in competition or from a competing carrier's inability to provide adequate service. *See CSX Corporation and CSX Transportation, Inc., Norfolk Southern Corporation and Norfolk Southern Railway Company -- Control and Operating Leases/Agreements -- Conrail Inc. and Consolidated Rail Corporation*, Finance Docket No. 33388, Decision No. 89 at 48 (STB served July 23, 1998). Indeed, as the U.S. Department of Transportation stated:

Service levels as well as rates may also be an important element in competitive markets. If a railroad cannot provide reliable service matched to shipper needs — for whatever reason — it will not be able to capture traffic and will not be able to serve as a competitive check.

DOT Comments at 5. Thus, the level of service provided either by the merged company or its competitor are crucial elements in whether or not a merger has harmed the public interest.

Despite UP's claim that "service has been restored in the Houston/Gulf Coast area," UP/SP-356 at 16, neither UP nor BNSF is providing the shippers with a high degree of service. While service has improved since the height of the crisis, it is nowhere near the pre-merger SP levels nor is it even close to the levels UP predicted in its merger



application. Indeed, UP's own press release responding to termination of the Emergency Service Order quoted UP's Chairman Dick Davidson as stating, "Our job of restoring Union Pacific Railroad service to its traditionally high levels is far from finished." *Union Pacific Reaction to STB's Ruling*, UP press release issued July 31, 1998.

Despite admitting that it needs to continually improve service, UP has gone to great efforts to portray the rail service problems as having ended; however, this is not the case. UP's claim is based upon fallacious and irrelevant comparisons to service at the height of the service crisis, February/March of 1998, UP/SP-358, V.S. Duffy at 2-3, and by comparison to 1997. *Id.* at 4-8.

As demonstrated in Exhibits A and E to the Verified Statement of Larry L. Thomas, President of SPI, service is barely back to transit times experienced in the latter part of 1997. That, however, is not the benchmark. In the UP/SP merger, UP promised to improve transit times, and to improve upon what it characterized as the grossly deficient SP system and service. As illustrated by Mr. Thomas' Verified Statement, including Exhibit E, transit time experience, developed according to a methodology for service measurement adopted by a joint SPI-UP task force, substantially degraded from that prior to the merger.

A number of individual shippers commenting in this proceeding also provided testimony concerning UP's degraded level of service. These include:

Champion International Company ("Champion"), which described its experience with UP's service, as follows: "... because service deterioration began almost immediately after the merger ... our definition of 'normal' can only be equated to the consistent service afforded our operations by SP prior to the merger. We have not experienced that

service level on a consistent basis." *Verified Statement of Champion International Corporation on Behalf of Itself and Its Short Line Railroad Subsidiary Operation: Moscow, Camden and San Augustine Railroad*, Finance Docket No. 32760 (Sub-No. 26) filed September 15, 1998 ("CIC-2") at 7.

Dow Chemical addressed service performance, in part, through a Verified Statement of Ernest L. Hord, Vice President, Operations of the Burlington Northern and Santa Fe Railway Company, who explains that "Dow's request is based on the delay, congestion, and other problems it has been having and continues to experience with UP's service at its Freeport Complex. Dow's filing details UP's deterioration in service at its Freeport Complex including the increase in its cycle times for railcars, the erratic nature of railcar availability, less regular service and the plummeting of on-time service." *Request for Additional Conditions of the Dow Chemical Company*, Finance Docket No. 32760 (Sub-No. 26), filed July 8, 1998 ("DOW-1"), Verified Statement of Ernest L. Hord ("V.S. Hord") at 1.

DuPont states that it "... found it necessary to take the extraordinary step of exercising competitive routing alternatives in order to maintain the integrity of our supply chain and serve internal and external customer requirements. A prolonged downward UP service spiral left DuPont with limited rail shipping options." *Request for New Remedial Conditions by E.I. DuPont de Nemours and Company*, Finance Docket No. 32760 (Sub-No. 26) filed July 9, 1998 ("DUPX-1") at 4.

Formosa Plastics Corporation ("FPC"), captive to the UP south of Houston, states that "... the underlying problems have not been resolved, and are likely to plague FPC and its customers for the foreseeable future. ... Without improved rail service, FPC will soon lose customer base. We have several competitors served by railroads other than UP, and those competitors are in a position to provide more reliable deliveries of product over routes only partially involving UP to customers that FPC can reach only via UP exclusively. Moreover, some of our competitors have the distinct and significant cost advantage of efficient rail service, which holds their private car and other transportation costs to a minimum, in comparison with our private car costs, which have been bloated by UP's inefficient operations. If FPC continues to receive unreliable, inefficient, and costly rail service from UP, we cannot continue to compete effectively with those who can deliver the same products predictably and at efficient prices to the same customer base as FPC seeks to serve." *Comments and Request for Remedial Conditions of Formosa Plastics Corporation*,



U.S.A., Finance Docket No. 32760 (Sub-No. 26) filed June 8, 1998 at 7;  
V.S. Richard A. Heinle at 10-11.

Shell Chemical Company and Shell Oil Company, which assert that UP is unable to "provide timely and efficient rail service . . ." *Joint Comments of Shell Oil Company and Shell Chemical Company*, Finance Docket No. 32760 (Sub-No. 26) filed September 18, 1998 at 2.

"This merger has adversely impacted our entire supply chain network and our service levels are not yet back to the levels prior to the merger."  
BASF, *August 28, 1998 letter to STB* (emphasis added).

"While UP service in the Gulf Coast area has improved recently, it is still far from the levels experienced prior to the merger, and even further from the efficiencies promised as a result of the merger with SP." Mobil Oil Corporation, *August 31, 1998 letter to STB*.

"Mr. Secretary, as a shipper who must rely on UP service throughout the Midwest, I can attest that the UP is far, far removed from 'recovery.' If recovery means customers must settle for whatever service level UP chooses to provide or accept a 'lower bar' of service, than maybe UP is recovering. By almost any other measurement, UP has a long way to go."  
MFA Incorporated, *September 24, 1998 letter to STB*.

Even shippers supporting UP in this matter agree that UP's service has not "recovered."

"OxyChem has not experienced the improved service that was expected by this time . . ." *UP's Opposition to Condition Applications*, Vol. 4, Finance Docket No. 32760 (Sub-Nos. 26-32) filed September 18, 1998 ("UP/SP-359"), Letter of Occidental Chemical Corp;

and "Service levels in the Houston area and Southern Texas has improved dramatically but they still have a long way to go." UP/SP-359, Letter of Baroid Drilling Fluids.

Whether from direct shipper testimony, or based upon the plastics industry's transit times statistics developed pursuant to a procedure mutually agreed upon by SPI and UP, there is no doubt but that service has not returned to pre-merger levels, let alone



UP having delivered upon its promise to improve transit times and car utilization, reduce costs, and create efficiencies for the shipper community.

## **2. The Merger Reduced Shipper's Service Options**

It may be that UP's market power did not directly cause the service crisis and that part of the cause lies in SP's pre-merger fragility. Indeed, UP's witness Alan B. DeMoss explains that a similar crisis on the SP system occurred in 1978 without a change in the competitive conditions, UP/SP-358, V.S. DeMoss, but the 1978 crisis proves the precise point that the Consensus Partners are trying to make: service to shippers and other railroads' operations did not suffer the same fate as they did in the most recent crisis because SP had little, if any, market power. In 1978, shippers had alternatives and the operations of the other railroads were not dependent upon SP's infrastructure, switching, and dispatching practices. In 1997-98, UP had tremendous market power gained from the merger and shippers and other railroads had no alternatives available to them.

While UP says "other railroads, not affiliated with SP, suffered from congestion" during the 1978 crisis, UP/SP-356 at 64, UP provides no support for this statement. In contrast, Harlan Ritter, who was President of the HBT during the 1978 crisis, states that SP's 1978 service crisis had little impact on shippers or the operations of other railroads because shippers and other carriers had alternatives available to them. Rebuttal Verified Statement of Harlan Ritter ("R.V.S. Ritter") at 9. During that crisis, shippers were able to switch to other carriers in the Houston area. R.V.S. Broussard at 10. Due to the market

power that UP gained through its merger with SP, shippers and carriers, with few exceptions, had no alternatives.<sup>51</sup>

### **3. UP's Reduction In Service Is An Indication Of Market Power**

The Board recognizes that an indication of a carrier's ability to exercise market power is the ability to profit from raising rates or reducing service (or both). UP's own witness notes that "[a] firm with market power can . . . lessen competition by reducing product quality or service, while holding price constant. Reducing product quality [service] at the same price is similar to raising price, because in terms of units of quality per dollar charged, the price of quality has increased." UP/SP-358, V.S. Hausman at 3. Thus, the fact that service levels are nowhere near the pre-merger levels evidences UP's market power since there is no effective competition serving to drive UP to achieve improved service levels.

#### **B. UP Is Unlikely To Resolve The Service Problem**

While principally blaming BNSF for causing the service crisis, UP/SP-356 at 67-68, UP takes full credit for solving the problem, declaring "It can be said with complete confidence, though, that implementation of the UP/SP merger brought the crisis to an

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<sup>51</sup> Curiously, the Association of American Railroads ("AAR"), of which UP is a member, recognizes that in any given market, a shipper should have service alternatives available to them in the event of a service meltdown. See Comments of the Association of American Railroads, Ex Parte No. 628, June 15, 1998. While Houston shippers did have an alternative available to them before the merger, the service crisis in the Gulf Coast has shown that contrary to the Board's expectations, BNSF has not been effective in providing that alternative service to shippers affected by UP's poor service levels. One of the objectives of the Consensus Plan is to allow KCS and Tex Mex to provide capable, alternative service to Houston area shippers that have suffered decreased service levels due to UP's dominance of the Gulf Coast market.



end. No one has even ventured any other explanation." UP/SP-356 at 63. Such claims ignore the multitude of factors that have helped bail UP out of the service crisis so far, including:

- The Board's Emergency Service Order, which relieved pressure on UP by diverting traffic to other carriers;
- The Asian financial crisis and good grain harvests worldwide, which have depressed domestic grain prices and have caused farmers to store rather than ship huge volumes of grain;
- A milder than normal winter, reducing needs for coal shipments;
- The General Motors strike, which eliminated at least 7000 carload shipments from UP's system; and
- Diversion of substantial amounts of rail traffic in the Houston area to truck.

All of these factors have combined to help dig UP part way out of the hole into which its service crisis plunged most of the western United States for the past year. Such a confluence of events certainly will not continue.

UP has repeatedly admitted the facts, for the sake of rhetorical convenience, it ignores when taking credit for "curing" its service crisis. For example, UP told this Board on July 28, 1998, that the emergency service order had diverted large amounts of freight from UP:

UP's total carloadings are down by almost . . . 9% in the first six months of this year compared with the first six months of last year. . . . UP needs to . . . not lose more traffic pursuant to compulsory service order provisions . . .



[T]he two provisions of the emergency service order that are in dispute here . . . have resulted in the diversion of substantial volumes of UP traffic originating and terminating in the Houston area.

*UP's Reply In Opposition to the Petition*, Service Order No. 1518 (Sub-No. 1) at 24 and Verified Statement of Richard B. Peterson supporting same at 1-2. In other words, UP admits that the emergency service order was effective in removing traffic from UP's lines. Even shippers supporting UP in this matter agree:

- "The temporary access that was granted was effective to help alleviate some of the problems that UP created . . ."

Statement of TexPar Energy Inc.,  
dated Sept. 8, 1998, in UP/SP-359

- "Nevertheless, service orders instituted at the direction of the Surface Transportation Board . . . have all contributed to returning Union Pacific operations to normal.

Letter of Koppers Industries, Inc.  
dated June 22, 1998 in UP/SP-359.

Clearly the Emergency Service Order played a large role in allowing UP an opportunity to put its house in order. The wind-down period of the emergency service order has been concluded for less than a month, and the effect on UP of the lifting of that order is yet to be seen.

UP has been more forthright in other publicly-available statements than it has been in its filings with the Board about the confluence of factors, including UP's poor service itself, that drove traffic away from UP to other railroads and to truck, easing pressure on UP's system. In its August 14, 1998, 10-Q report for January through June 1998, filed with the Securities and Exchange Commission, UP said:

Agricultural Products: . . . Carloadings declined 6% . . . primarily the result of a 24% decrease in corn volumes due to soft export demand caused by strong foreign harvests (primarily in China), as well as the continuation of system velocity issues.<sup>52]</sup>

Automotive: . . . [C]arloadings were flat . . . Lower parts volumes (down 6%) led the decline in traffic, primarily the result of slow cycle times and diverted business due to service issues. . . . Finished vehicle results were also affected by strike-related declines at GM, which reduced . . . carloadings by approximately 7,000. . . .

Chemicals: Carloadings declined 9% . . . principally from congestion-related diversions to other modes of transportation as well as to other rails. . . . In addition, the Asian crisis reduced demand for exports of soda ash while warm weather in some areas hurt demand for LP gas. . . .

Energy (Primarily Coal): Commodity revenue fell . . . driven by a 3% decrease in carloadings. . . . Slow systems speeds, diversions of business to competing railroads and weak export markets led the decline . . .

Industrial Products: Carloadings decreased 11% . . . result[ing] primarily from equipment shortages and service issues, including diversions of traffic to other modes of transportation and to other rails. . . .

Intermodal: . . . [C]arloadings fell 13% . . . the result of lower system speed and related diversions of traffic to BNSF and other rails, as well as weak exports. . . .

In short, when obliged by federal securities laws and the discipline of potential shareholder derivative suits to take a reasonably objective view of factors which enabled the Board, by the date of UP's 10-Q, not to extend the emergency service order, UP had to admit that purging its system of cars was not a result of merger efficiencies, as claimed

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<sup>52</sup> UP's May 13, 1998, 1<sup>st</sup> quarter 1998 10-Q stated, "This decrease [in carloadings] reflects continuing congestion, the impact of the Asian crisis on export grain and intermodal markets and weak grain demand as farmers delay shipment due to the current grain price environment." <http://sec.yahoo.com/e/980513/unp.html>.



here before the Board, but rather was the result of UP's poor service plus a unique combination of reduced agricultural and intermodal shipments, due in part to the Asian financial crisis, mild weather, the GM strike and diversions of freight to truck. UP's very own words highlight the transparency of its claim to have "fixed" the service crisis by having implemented the merger.

Not only UP, but also shippers (including shippers whose statements UP filed as supporting its position in this matter), recognize that factors other than implementation of the merger have led to whatever measure of service recovery UP can thus far claim. In fact, many shippers have cited their forced reliance on more expensive, motor carrier service as a result of UP's service meltdown. For example:

- "Truck transportation for long haul moves was substituted at great expense."  
International Paper Company letter to  
Hon. Vernon A. Williams, Aug. 27 1998 at 2.
- [Champion International's] "Camden [TX facility] shipped an average of 825 trucks a month in 1997 as compared to 700 trucks per month in 1995. . . . [Champion's] Corrigan [TX facility] has consistently shipped its maximum capacity of 380 trucks per month to avoid rail service."

Verified Statement of Champion International Corporation,  
CIC-2, dated Sept. 15, 1998 at 5 and 6.

- "With the exception of a few spot situations, we have not been forced to truck material that would normally have moved via Union Pacific since the end of March 1998."

Verified Statement of Koppers Industries, Inc.,  
dated June 22, 1998, in UP/SP-359.



These and many other shippers have confirmed that UP's service problems shifted their freight from rail to truck, providing further relief to the congestion which UP claims that its merger implementation caused.

UP's own data and methodologies show that even UP's supposedly "recovered" current operating conditions continue to result in a significant diversion of traffic from rail to the highways. In their original merger application UP and SP presented a traffic diversion study which purported to predict the diversion of traffic from truck to rail intermodal service in specified traffic lanes where UP believed it would be able to generate particular efficiencies that would attract traffic off the highways. UP/SP-22 at 465-467. The study's conclusions predicting shipper logistics cost savings were accepted by the Board in its Decision No. 44 granting the UP/SP merger application. Decision No. 44 at 109.

Re-running UP's study using inputs that represent UP's current operating conditions, drawn from the bi-weekly service reports posted on the Internet by UP, shows that even using UP's model, which unrealistically undervalues quality of service issues by treating them only in terms of their direct cost impact, shows that rather than attracting rail freight to intermodal service, even now UP is still pushing shipments off the rails and onto the highways. Whereas UP predicted total truck-to-intermodal diversions of 34 truckloads per day in specified lanes, using UP's current operating statistics yields total diversions from truck to rail of only 117 truckloads per day. Rebuttal Verified Statement of Joseph J. Plaistow ("R.V.S. Plaistow") at 6. Moreover, if the same current UP service parameters are applied to determining the effect of UP's diminished service capabilities

on existing rail carload freight, UP's model also shows diversion of over 40,000 truckloads of freight to the highway from the rail system each year. R.V.S. Plaistow at 7.

These projected diversions are reflected in actual Texas highway traffic data. Heavy truck vehicle miles traveled in Harris County, TX (the county in which Houston primarily lies) grew 8% in 1997. This increase occurred while overall Texas industrial production grew less than 4% and while non-truck vehicle miles grew only 2%. Thus, statistics show that as UP's service meltdown occurred, truck vehicle miles rose. These statistics confirm the results of the modeling performed for the Consensus Parties and demonstrate how UP's service crisis has burdened the roadway system in and around Houston with more trucks.

The Consensus Plan must be implemented to ameliorate the effects of UP being unable to remedy its own service problems. The Consensus Plan offers the prospect of more coordinated, more efficient and more economical rail service for the Houston area, which has the real potential of transferring shipments from truck back to rail and increasing the overall amount of traffic available to all of the railroads. These were the benefits which UP promised in its merger application that it would bring to Houston and the Gulf Coast. Now, more than two years after UP took over SP, those benefits still have not materialized. It thus is time for the Board to adjust the conditions it prescribed in Decision No. 44 to satisfy the need for adequate rail service in Houston and along the Gulf Coast.

**C. UP's Failure To Invest In Houston/Gulf Coast Infrastructure Indicates A Lack Of Competition**

**1. The Board Has Determined that Inadequate Infrastructure Was a Contributory Cause of The Service Crisis In The Houston/Gulf Coast Area**

Without presenting any specific evidence, witness statements, or studies, UP complained to the Board on December 1, 1997 that the lack of infrastructure in the Gulf Coast region had been a significant cause of the service crisis. UP claimed that after decades of decline and contraction, traffic volumes had continually grown while the infrastructure had not kept pace. According to UP, it was necessary to meet this challenge by making new investments in additional capacity.

In a decision denying a request by the Railroad Commission of Texas for added competition in and around Houston, the Board accepted UP's argument of December 1, 1997 that capital improvements and upgraded infrastructure were needed in the Gulf Coast region. The Board noted that the service emergency "was caused in large measure by a transportation infrastructure in and around Houston that is not adequately equipped to deal with natural surges in a growing economy or with temporary reductions in railroad capacity caused by derailments, weather and so forth. To protect against future crises, and indeed to provide adequate service during "normal" periods, the physical plant in Houston will require major upgrading in order to meet the needs of shippers." ESO-1 at 6-7.



a. The Board Orders UP to Address the Infrastructure Problem

The Board again referred to the infrastructure problem in the Houston/Gulf Coast area on February 25, 1998 and ordered UP to report to it on May 1, 1998 as to its plans for addressing the problem. Decision served February 25, 1998, Ex Parte No. 573, Service Order No. 1518 at 5 ("ESO-2"). The Board clearly believed that UP would make the investments required to address the perceived infrastructure problem in the Houston/Gulf Coast area.

b. UP Files its Infrastructure Report

In response to the Board's order on February 25, 1998 that UP file plans addressing Houston infrastructure, UP filed its Report on Houston and Gulf Coast Infrastructure on May 1, 1998.<sup>53</sup> In its Infrastructure Report, UP promised to make infrastructure investments of "over \$1.4 billion over the next five years to improve the quality of rail service in the area from New Orleans to San Antonio and south to the Mexican border." However, to keep the Infrastructure Report within the realm of promises only, UP's Infrastructure Report was issued with many caveats and reservations. UP claimed that (i) the timing and specifics of many of its planned capital expansion projects were likely to change; (ii) since UP engineers did not have adequate time to complete a detailed costing exercise for the dozens of projects involved, the costs shown were best estimates only; (iii) changing shipper requirements and traffic patterns

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<sup>53</sup> See *Union Pacific's Report on Houston and Gulf Coast Infrastructure*, filed May 1, 1998 in Ex Parte No. 573, Service Order No. 1518 ("Infrastructure Report").

would force reevaluation of the projects over time; and (iv) significant changes in the current regulatory regime would undermine UP's ability to make the necessary investments and require UP to reevaluate the investment program and could also affect already planned capital spending.

UP's Infrastructure Report was widely criticized by rail carriers and shipper organizations alike. In a Reply of the Chemical Manufacturers Association ("CMA") and The Society of the Plastics Industry, Inc. ("SPI") to the Infrastructure Report,<sup>54</sup> CMA and SPI observed that the Infrastructure Report (i) did not offer any apparent hierarchy or prioritization of the 95 projects that it described and (ii) there was no accountability in the process to ensure that UP follows through and completes the projects it had identified. CMA and SPI suggested that UP should be required to match each project to a schedule over the next five years so as to offer the shipping public a clear understanding of what will be done when and where.<sup>55</sup>

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<sup>54</sup> *See Comments of The Chemical Manufacturers Association and The Society of the Plastics Industry, Inc.* filed June 1, 1998 in Ex Parte No. 573, Service Order No. 1518.

<sup>55</sup> BNSF and The Port of Houston made the same observations regarding the failure of UP to commit itself to the capital investments proposed in the Infrastructure Report, its failure to establish a time frame for completion of the proposed projects and its failure to include a detailed costing for the proposed projects. *See Reply Comments of The Burlington Northern and Santa Fe Railway Company on Houston and Gulf Coast Infrastructure*, filed June 1, 1998, and *Port of Houston Authority's Response to Union Pacific's Report on Houston and Gulf Coast Infrastructure*, filed June 1, 1998.



In a verified statement supporting the Reply of KCS to the Infrastructure Report,<sup>56</sup> Tom O'Connor calculated that: (i) UP had actually funded or begun investments in the Houston terminal area totaling \$29.3 million, a mere 2 percent of the planned total of \$1.4 billion, and (ii) UP had actually funded or begun investments in other Gulf Coast areas totaling \$46.5 million, a further 3 percent of the planned total of \$1.4 billion. These calculations enabled Mr. O'Connor to conclude that many of the investments proposed in the Infrastructure Report would not occur in the near future and may not occur at all, depending on UP's subjective evaluation of future events. Verified Statement of Tom O'Connor ("V.S. O'Connor") at 1-2.

**2. Despite its Promises, UP Is Not Investing In Houston/Gulf Coast Infrastructure**

In its 1997 Annual Report, UP stated that it expected to increase its level of capital spending system wide to \$2.5 billion in 1998 from \$2 billion in 1997. *Union Pacific Annual Report for the Fiscal Year Ended December 31, 1997*, Form IO-K at 28. UP's Infrastructure Report stated that UP expects to spend a total of \$1.4 billion on infrastructure in the Houston/Gulf Coast area over the next five years. In 1998, however, documents produced in discovery clearly show that UP has actually spent (or authorized the spending of) a total of only \$116.9 million<sup>57</sup> in the Houston/Gulf Coast area.<sup>58</sup> This

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<sup>56</sup> See Reply of The Kansas City Southern Railway Company to Infrastructure Report of Union Pacific Railroad Company filed June 1, 1998, Ex Parte No. 573, Service Order No. 1518.

<sup>57</sup> See Summary of Gulf Coast Investment attached to R.V.S. Grimm/Plaistow as Figure 14.



amount represents only 4.7% of the total of \$2.5 billion that UP plans to spend system wide and only 8.4% of the total of the investments planned for the Houston/Gulf Coast area. These two percentages show UP is scarcely investing in Gulf Coast Infrastructure.

**3. UP Is Not Investing In Gulf Coast Infrastructure Because UP Invests Where There Is Competition**

In its decision approving the UP/SP merger, the Board accepted UP's assurances that it would make extensive investments in SP's infrastructure to increase its competitiveness. The Board claimed that UP/SP's "merger related investments will improve rail service and strengthen competition." Decision No. 44 at 114. The Board stated further that "it is undisputed that UP will have adequate financial resources to supply the SP system the capital that it needs to provide truly competitive service over SP's routes." *Id.* at 116. At that stage, the Board did not anticipate that UP has not made many of its promised merger investments in the Gulf Coast region, but that is what has occurred.

UP's investments have concentrated on locations where UP competes with trucks for intermodal traffic and rail carriers for other traffic, especially coal. UP is simply not investing in the Houston/Gulf Coast in the same manner as it does where it faces competition. In its First Annual Report on Merger and Condition Implementation<sup>59</sup> filed

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<sup>58</sup> This amount differs from the amount provided by Mr. O'Connor because it includes updated amounts actually authorized for 1998 from a document KCS/Tex Mex received in discovery.

<sup>59</sup> *Applicants' First Annual Report on Merger and Condition Implementation*, Finance Docket No. 32760 (Sub-No. 21), filed on July 1, 1997 ("UP/SP-303") at 23-26.

with the Board on July 1, 1997 and its Second Annual Report on Merger and Condition Implementation<sup>60</sup> filed with the Board on July 1, 1998, UP described various merger-related infrastructure projects which were underway or planned. These included:

- the rebuilding of its intermodal yard facility in Roseville, CA at a cost of \$128.9 million;<sup>61</sup>
- the building of a new intermodal facility at Marion, AR at a cost of \$69.5 million;
- the upgrading of Livonia Yard in Livonia, LA at a cost of \$15.5 million;<sup>62</sup>
- the construction of a locomotive fueling and servicing facility in Livonia, LA at a cost of \$4.3 million;
- double-tracking on the Sunset Route in New Mexico at an undisclosed cost;
- upgrading of the Kansas Pacific Line between Topeka, KS and Denver, CO at a cost of \$58.2 million;
- the expansion of capacity on a bottleneck SP segment in southeastern Missouri at a cost of \$10.3 million;
- the construction of connections between UP and SP mainlines in Avondale, LA at a cost of \$37 million;<sup>63</sup>

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<sup>60</sup> UP/SP-344 at 11-12.

<sup>61</sup> UP claimed that it was reconstructing its intermodal facility at Roseville Yard to compete better with trucks for intermodal traffic. *See UP Gives Roseville Site Big Overhaul*, The Sacramento Bee, Friday, July 25, 1997 at G1. Messrs. Grimm and Plaistow explain that intermodal traffic is, by definition, the most competitive traffic. *See Consensus Plan*, Vol. 1, V.S. Grimm/Plaistow at 164.

<sup>62</sup> One of UP's reasons for expanding Livonia Yard was to enable it to compete better with BNSF, KCS and IC for traffic moving through the New Orleans Gateway. *See UP's 1997 Annual Report to Shareholders* at 5.

<sup>63</sup> UP claims that this investment will allow it to reroute traffic from the former SP line between Iowa Junction and Avondale (now jointly owned by BNSF and UP) to UP's line through the classification yard at Livonia. *See UP/SP-344* at 12.

- upgrading the SP Tucumcari Line between Topeka, KS and El Paso, TX at a cost of \$48 million; and
- upgrading the former Texas and Pacific Line between Fort Worth, TX and El Paso, TX at a cost of \$58.8 million.<sup>64</sup>

This list of investments and the reasons for the investments show how UP invests in locations where it is competing for intramodal and intermodal traffic. Since UP faces very little competition in the Houston/Gulf Coast area, its investments are relatively minor.<sup>65</sup>

Another example of a huge investment taking place as a result of competition is the construction project underway in the corridor linking Chicago and Salt Lake City. UP is spending \$400 million this year alone in this corridor with most of the work taking place on a short segment between North Platte and Gibbon, NE. UP is making this investment to enable it to compete with BNSF for coal moving from the Powder River Basin to various locations in the United States. R.V.S. Grimm/Plaistow at 18.

UP's investment behavior is precisely what one would expect of a competitive carrier and closely parallels the investment behavior of other carriers. The vast majority of investments identified by rail carriers in their Annual Reports occurs in competitively

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<sup>64</sup> UP claimed that it was upgrading this line to compete with BNSF for intermodal traffic. See *Union Pacific Launches a Number of SP-Related Track Upgrades*, Traffic World, June 23, 1997 at 17.

<sup>65</sup> UP only mentions in passing, and does not mention the value of, its construction of connections between Englewood and Settegast Yards and its plans to add trackage at Strang Yard. UP/SP-344 at 14 and 18.



served locations and in response to competitive pressures.<sup>66</sup> This confirms that UP's decision to invest where there is competition is rational and normal.

Indeed, this principle was confirmed in UP's own original merger application. In the UP/SP merger proceeding, UP clearly recognized that competition stimulates the need for investment in infrastructure. In a verified statement in support of the UP/SP merger application, Professor Robert Willig, Professor of Economics and Public Affairs at Princeton University, pronounced that "competition is important not as an end in itself but because it leads, through the interplay of independent pricing, service-level and output decisions, to an efficient allocation of resources in the economy — i.e., one that confers maximal benefits on consumers at a minimal expenditure of scarce resources."

*See UP/SP Railroad Merger Application, Volume 2 at 578.*

Professor Willig stated further that the UP/SP's merger plans would result in a wide range of investments that would be made to improve the capacity of the merged system to meet shipper demand. The merger plans were not those of railroads bent on exploiting market power but, to the contrary, "reflect a desire to intensify competition with other transportation providers." *Id.*, Vol. 2 at 594 (emphasis added).

The clear statements by Professor Willig that competition would promote investment were echoed in statements by other proponents of the merger. In a verified statement in support of the merger application, Lawrence Yarberry, Vice President-Finance of SP, explained that each of the major western railroads was required to expend

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<sup>66</sup> R.V.S. Grimm/Plaistow at 18.

hundreds of millions of dollars annually to maintain its track system and equipment fleet. In addition, railroads were also required to make "competition enhancing investments." *Id.*, Vol. 1 at 263. SP's competitive environment made it imperative for SP to make the required competition-enhancing investments but, owing to its poor financial condition, SP was not in a position to make the required investments and thus the proposed UP/SP merger was a solution which would fully address SP's capital needs. *Id.*, Vol. 1 at 286.

The notion that there is a relationship between competition and investment in infrastructure was later confirmed when UP's own rebuttal statement stated that competition will encourage investment: "[UP] faces tremendous challenges to regain traffic and restore the sound financial condition that will permit the huge investments needed to become a truly effective competitor to BNSF." UP/SP-356 at 16-17.

**4. The Board Should Not Accept UP's Threats Not to Invest in the Houston/Gulf Coast**

Now, instead of claiming competition will drive investment, UP has resorted to threatening not to invest in the Houston/Gulf Coast. In a Report on Service Recovery filed with the Board on December 1, 1997, UP warned that (i) competition by other rail carriers would serve to stifle its investments in its Gulf Coast network and (ii) the Board must resist the "blandishments of proponents of re-regulatory steps that would undercut the incentives and ability of railroads to fund the huge investments that will be needed in the years to come." *Union Pacific's Report on Service Recovery*, filed December 1, 1997 in Ex Parte No. 573, Service Order No. 1518 at 90-92. In its Infrastructure Report, UP again threatened that should the Board order divestiture or require UP to open its traffic

base to other carriers, UP would have to reevaluate its investment program. Infrastructure Report at 6-8.

In its Opposition, UP again threatens to curtail its planned infrastructure investments if the Board introduces the competition that the condition applicants are requesting. UP indicates that it will halt its promised investments to Strang Yard, Manchester Junction and the Clinton Branch as well as various other locations in the Houston/Gulf Coast area if the Board grants any of the requests for additional remedial conditions. UP/SP-356 at 171-173.

These "threats" to stop investment if the Board restores competition in the Houston area are, of course, contrary to UP's actual practices. Indeed, as is clearly established above, UP actually invests where there is competition and is now investing in the Houston area sluggishly due to the heightened scrutiny the Board has placed upon UP. By contrast, when UP faced competition from SP in the Houston/Gulf Coast area, it invested more actively in additional infrastructure. For example, in 1994 when competition between UP and SP was still rife in Houston, UP invested over \$37 million to build trackage in Houston in order to serve prospective chemicals customers. R.V.S. Grimm/Plastow at 18.

Instead of threatening to reduce its level of investment in the face of competition and the imposition by the Board of additional remedial conditions, UP should be undertaking to increase its level of investment to strengthen itself against competition — a strategy which it promised in the UP/SP merger application and which it uses in other locations where competition already exists. However, as the Consensus Parties have



illustrated, UP faces little competition in the Houston/Gulf Coast area and it can exploit this fact by directing its investment resources elsewhere.

**5. Restoration Of Competition In Houston Will Actually Spur Investment**

As Messrs. Grimm and Plaistow state: "competition does not discourage investment, it spurs it on." Consensus Plan, Vol. 1, V.S. Grimm/Plaistow at 164. Messrs. Grimm and Plaistow explain that where UP faces little or ineffective competition in a particular area, such as the Houston/Gulf Coast area, the incentive to invest is dramatically reduced. The reason for UP's reduced incentive to invest is that it faces no threat of losing its traffic to a competitor who would be prepared to make the required infrastructure investments as necessary to compete against UP. Without competitive pressure, UP can make the required investments at its own pace or not at all, depending on its own judgment of what is needed. R.V.S. Grimm/Plaistow at 17. The strength of competition and the free market is such that if the Consensus Plan is adopted and UP follows through on its threats not to make its promised investments, then BNSF and Tex Mex will make those investments instead.

Where competition exists, a railroad's incentive to invest depends on the profitability of, and return on, the investment, even if that investment is shared. R.V.S. Grimm/Plaistow at 16. If the Board adopts the Consensus Plan, UP's incentive to invest in Houston/Gulf Coast infrastructure will still exist because the necessary investments will be made by all of the three carriers serving Houston and UP will not have to bear those costs alone. Indeed, the Consensus Plan calls for the PTRRA to operate over the

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various tracks and facilities in Houston which will enable UP, BNSF and Tex Mex to depend upon its efficient operations. To the extent there is an efficiency to be achieved by any one capital project, its costs will be borne by all of the owners of the PTRAs, not just the UP.<sup>67</sup> R.V.S. Grimm/Plaistow at 16.

The economic rationale for this assertion is borne out by UP itself at various points throughout its Opposition. UP suggests that if BNSF decides to invest in more capacity on various routes and UP then decides to make use of that route, then UP would likely share BNSF's cost. UP/SP-356 at 104, 125 and 132. This will enable UP to share the financial responsibility of making the required investments with other parties if the Consensus Plan is adopted.

In conclusion, the Board needs to restore effective levels of competition to the Houston/Gulf Coast area to ensure that the necessary infrastructure investments to support this traffic are made by UP at the pace that UP is making investments elsewhere. If the Board does not place some competitive pressure on UP, there is every reason to believe that UP's sluggish rate of infrastructure investment will continue.

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<sup>67</sup> It seems that UP is not averse to sharing investments on the PTRAs with BNSF. In a letter to the Board, UP's counsel stated that BNSF should not be allowed to avoid financial responsibility for costs, including investments on PTRAs. See letter from Michael Hemmer and Pamela Miles to the Board dated June 15, 1998.

**IV. THE CONSENSUS PLAN WILL RESOLVE THE COMPETITIVE AND SERVICE PROBLEMS**

**A. Removing The Northbound Restriction**

A crucial item of the Consensus Plan is the lifting of the northbound restriction that was placed upon Tex Mex in Decision No. 44. It is this lifting of the restriction that will give Houston shippers, especially PTR A and HBT shippers, a truly competitive option to the Northeast, Midwest, and Southeast gateways by restoring the competitive options that were lost when UP merged with SP. R.V.S. Grimm/Plai stow at 7. It will also ensure that Tex Mex can be a truly effective alternative to UP at Laredo.

**1. Removing The Northbound Restriction Restores SP's Competitive Presence For Northbound Houston Traffic**

The conditions the Board imposed to preserve competition in Houston did not necessarily fail for all shippers in all geographic locations. The conditions only failed for those shipments (routings) going to certain geographic destinations. The Plan is intended to remedy only those places where there has been a competitive failure, and where there has been a competitive failure, the Board has a legal obligation to remedy that failure. See Section I and Section II-A above. In this respect, the Consensus Plan is "narrowly tailored" to address these specific harms and is not an enhancement of competition, but merely a restoration of competition that was lost.

While, for the most part, the Consensus Plan will restore the number of carriers serving the Houston market to three, it does not request this action on the particular basis that the Board's finding with respect to so-called 3-to-2 traffic was erroneous. Indeed, the Consensus Plan does not take issue with the general notion that there can be intense



competition with only two railroads serving a given market or particular shipper. The issue (and the focus of the competitive analysis of Dr. Grimm and Mr. Plaistow) is whether or not BNSF is providing an effective alternative to UP and has sufficiently replaced SP so as to preserve pre-merger levels of competition in Houston.

As the rebuttal analysis establishes, whether or not any particular shipper was a 2-to-1 or 3-to-2 shipper is not the relevant factor. What is relevant is whether or not BNSF has sufficiently replaced SP so as to preserve the pre-merger level of competition provided by SP to any of those shippers.<sup>68</sup> BNSF has not sufficiently replicated SP's competitive presence. R.V.S. Grimm/Plaistow at 6. UP's market power over these shippers is thus a given regardless of what "category" that particular shipper may fit into.

It is not the number of railroads serving any particular shipper that matters. Indeed, the Board has often stated that it is not the number of competitors that matters. The Board's obligation is to preserve the level of competition.<sup>69</sup> While the Board usually makes this statement in the context of a discussion as to why a reduction in the actual number of competitors does not, in and of itself, reduce competition, the reverse is also

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<sup>68</sup> See Decision No. 44 at 163 ("In sum, we believe that the service that will be provided by BNSF over trackage rights is an appropriate replacement for the service formerly provided by SP."); *id.* at 124 ("With the conditions we are imposing, we find that BNSF will be an effective replacement for SP at these 2-to-1 points and affected 1-to-1 points.").

<sup>69</sup> See *CSX Corporation and CSX Transportation, Inc., Norfolk Southern Corporation and Norfolk Southern Railway Company — Control and Operating Leases/Agreements — Conrail Inc. and Consolidated Rail Corporation*, Finance Docket No. 33388, Decision No. 89 at 49 (STB served July 23, 1998) ("In assessing the probable impacts [of a rail consolidation] and determining whether to impose conditions, our concern is the

true: restoring a carrier, i.e., going from 2 to 3, does not in and of itself provide that shipper with more competition than it had before the merger nor does it mean the Board has reversed its findings with respect to 3-to-2 shippers. It may be that two carriers, both operating via trackage rights and having corresponding different route structures, i.e., BNSF and Tex Mex, are needed to preserve the same level of competition that was provided by a single carrier (SP) before the merger and to compete against UP for that shipper's traffic after the merger.

Indeed, the DOT recognized the principle that one must examine more than simply the number of carriers serving a particular point in order to determine whether or not competition has been preserved when it stated:

Effective competition goes beyond merely being able to serve the same two points. Effective competition implies that both carriers have reasonably comparable routes, in terms of distance and capacity, as well as adequate infrastructure to provide levels of service that offer shippers a realistic alternative. Competition between carriers may be judged most effective when it forces them to adjust rates and/or provide better service in response to each other's actions in the market.

DOT Comments at 5. For certain Houston traffic, BNSF has simply been unable to force UP to "adjust rates and/or provide better service in response to each other's actions in the market."

Likewise, despite its findings on 3-to-2 traffic, the Board itself has not only preserved three carriers serving a market, which is what the Consensus Plan requests, but

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preservation of competition and essential services, not the survival of particular carriers.").



has actually increased the number of particular carriers serving a market, going from 2 to 3, in order to preserve the same level of competition regardless of the actual number of particular carriers. The Board granted BNSF access to Westlake, Lake Charles, and West Lake Charles. Decision No. 44 at 152-154; Decision No. 63. In so doing, the Board, at Westlake and Lake Charles, actually preserved three carriers (pre-merger UP, SP, KCS — post-merger UP, BNSF, KCS) and at West Lake Charles it actually increased the number of serving carriers from two (SP and KCS) to three (UP, BNSF, and KCS). It did so because of concerns that KCS, acting alone, may not have a sufficient route structure to compete against UP. Decision No. 63 at 7. Similarly, the Board also preserved three carriers in Houston for traffic destined to Mexico. In partially granting Tex Mex's trackage rights request and granting the BNSF trackage rights, the Board gave HBT and PTRR shippers the option of using three carriers to Mexico — UP, BNSF via Eagle Pass or Brownsville, or Tex Mex.<sup>70</sup>

One thing is clear — BNSF has not replicated SP's pre-merger Houston presence for certain destinations. As in some of the instances noted above, it may be, that standing alone, neither BNSF nor Tex Mex can fully replicate SP's competitive presence in Houston, but restoring the ability of Houston shippers to access two other carriers (BNSF

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<sup>70</sup> While granting Tex Mex's request merely preserved two competitive routings from Houston to Laredo, *i.e.*, the pre-merger UP and SP/Tex Mex routing became a UP v. BNSF/Tex Mex (or KCS/Tex Mex routing), the fact remains that BNSF's access to the Eagle Pass and Brownsville gateways means that Houston shippers do benefit from having three independent routings to the Mexican market. The Board fully intended BNSF to compete against UP using these gateways. Decision No. 44 at 147, 148 n. 181, and 149.



and Tex Mex) does fully replicate SP's pre-merger route structure and will provide the same level of competition to UP as before the merger.

There are numerous solutions to the fundamental problem of BNSF's inability to provide the level of competition the Board intended it to do and the Board has broad discretion to fashion appropriate conditions to resolve that problem,<sup>71</sup> but if it takes providing shippers with service from both BNSF and Tex Mex as a means to fully replicate the pre-merger level of competition provided by SP, then the Board has the authority, indeed, the legal obligation, to do so. Only the Consensus Plan is a comprehensive solution to that fundamental problem. Indeed, it is the only comprehensive plan that has been set forth which improves service, adds infrastructure, and resolves the competitive problems.

It is not sufficient to simply give BNSF additional rights. BNSF's proposed plan does nothing to give BNSF independent infrastructure or reduce BNSF's reliance on its trackage rights over the UP. As the competitive analysis shows, BNSF is simply not effective in replicating SP's pre-merger market share to the Northeast, Midwest, and the Southeast. While BNSF's new joint ownership of the Houston to New Orleans line, in conjunction with its use of the Spring Dispatching Center, may help alleviate BNSF's inability to effectively serve the Southeastern market, those actions will do nothing to

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<sup>71</sup> Decision No. 44 at 100, 144-45. See also 49 U.S.C. 11344(c); Grainbelt v. STB, 109 F.2d 794, 798 (D.C. Cir. 1997) ("The Commission has 'extraordinarily broad discretion' in deciding whether to impose protective conditions in the context of railroad consolidations.").

alleviate UP's market power to the Northeast and Midwest. R.V.S. Grimm/Plaistow at 7. In contrast, the adoption of the Consensus Plan and the corresponding lifting of the restriction on KCS/Tex Mex's ability to serve the Houston market, will provide both Houston and NAFTA shippers with an effective independent alternative to the Northeast and Midwest destinations — the precise destinations where BNSF has been ineffective.

## **2. Removing The Northbound Restriction Provides Necessary Revenues To Tex Mex**

It is the lifting of the restriction which provides Tex Mex with the additional revenues necessary to buy and rehabilitate the Victoria to Rosenberg line, Booth Yard, and to double-track UP's Lafayette Subdivision between Dawes and Langham Road, Beaumont, TX. None of these infrastructure improvements can be made without the lifting of the restriction. UP had an opportunity to provide this Board with a study or analysis that would indicate that Tex Mex could afford these infrastructure investments without the lifting of the restriction. UP could have provided a traffic study that showed the financial effects on Tex Mex of each individual proposed condition. UP chose not to do either. The only references to Tex Mex's ability to afford these infrastructure investments without the Consensus Plan were contained in footnotes that contained nothing but broad legal argument and no evidentiary support. UP/SP-356 at 183-184, n. 58, and 192, n. 69.

Lifting the restriction is necessary to add traffic densities to the Tex Mex system in order to provide the necessary revenues for infrastructure investment. The Board clearly understands the need to provide sufficient traffic densities to carriers in order to

generate sufficient revenues to pay for infrastructure improvements and costs associated with operating via overhead trackage rights. Indeed, the Board has given similar rights to BNSF in several locations, including the Lake Charles area, Shreveport, Beaumont and Texarkana. *See* Decision No. 44 at 153, 167, 186. In granting these rights to BNSF the Board said, "the new facilities and transload conditions were intended, in part, to enable BNSF to achieve sufficient traffic density on the trackage rights lines, not only in the near future but in the more distant future as well." Decision No. 61 at 10. Tex Mex is requesting the same consideration from the Board in gaining more traffic density on its lines to continue to remain effectively competitive.

Furthermore, UP attempts to claim, without evidentiary support, that the diversions attributed to the CN/IC merger and the KCS Alliance will provide sufficient revenues to allow Tex Mex to be competitive. UP/SP-356 at 190-191. The ALK diversion study submitted in this proceeding accounted for the effects of that merger and the Alliance, Consensus Plan, Vol. 1 at 236, and Mr. Plaistow's financial analysis relied upon the diversions projected by ALK. Mr. Plaistow's financial analysis and its conclusion that Tex Mex cannot afford to make any of these infrastructure investments without the Consensus Plan remains the only evidence of record.<sup>72</sup>

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<sup>72</sup> Contrary to UP's implications, the diversion study submitted by Woodward/Rogers in F.D. No. 33556, CN/IC-7, is entirely consistent with the statements and arguments submitted in the Consensus Plan. The F.D. No. 33556 study shows Tex Mex as gaining approximately \$13 million in additional revenue (assuming no Consensus Plan). That analysis is entirely correct, but while \$13 million in additional revenue may justify Tex Mex's investment into its new Laredo Yard, it certainly does not provide enough



### **3. Removing The Northbound Restriction Makes Tex Mex An Effective Alternative In Mexico**

For a variety of reasons, UP claims that the lifting of the northbound restriction is not necessary in order to make Tex Mex competitive for Mexican traffic, but UP misses the point. The lifting of the restriction has two purposes: first and foremost, it will restore the competitive options that Houston shippers lost, and second, it will allow Tex Mex to be a strong competitor to UP at Laredo. The fact that a "preponderance" of the additional traffic that Tex Mex would gain is "Houston north traffic," UP/SP-356 at 192, proves the precise effectiveness of the proposed condition in alleviating the competitive harm for Houston shippers. UP's statement also implicitly acknowledges that the rest of the Tex Mex traffic gains would be for Mexican traffic. The Consensus Plan is thus an entire package that accomplishes both of its intended purposes.

#### **B. The Plan Is Not A Taking Or An Open Access Plan**

##### **1. The Consensus Plan Is Not A Taking**

UP claims that the Consensus Plan is a massive government confiscation of UP's private property and will cause UP to lose significant revenues. Not one piece of UP property will be confiscated by the government. While the Consensus Plan does request UP to sell an abandoned railroad right-of-way and an underutilized rail yard to Tex Mex

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additional new revenue to allow Tex Mex to make any of the infrastructure investments discussed herein.

as a condition for approval of its merger with SP,<sup>73</sup> UP will be fully compensated for any property that it sells and if UP is unhappy with the price, it has the right to request the Board to set a higher price. The Consensus Plan also calls for allowing UP to operate over the newly constructed Victoria to Rosenberg line and the newly constructed Houston to Beaumont line. In addition, under a lease from Tex Mex, UP will be able to continue to use any Booth Yard tracks that it currently uses to store cars until replacement storage is established by Tex Mex for UP. Accordingly, not only will UP receive compensation for any property sold to Tex Mex, but UP will not even lose the right to use any property that it currently uses.

Furthermore, the Board must recall the words of UP's legal counsel, at the oral argument of the merger case, to the effect that the Board could require "divestiture" as a condition under its exercise of its retained oversight jurisdiction. *See UP/SP Merger*, Finance Docket No. 32760, Oral Argument Transcript, July 1, 1996 at 59. Certainly, Mr. Roach understood at that time that divestiture is a standard remedial condition employed by the Board and by the Interstate Commerce Commission. He also certainly understood that he was not speaking to a "massive government confiscation of UP's private property" when he suggested divestiture.

Requiring merging companies to divest themselves of certain property as a condition to a merger are also standard conditions imposed in any merger in any industry

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<sup>73</sup> Indeed, the statute specifically authorizes the Board to condition any merger by requiring divestiture, trackage rights, or access to other rail facilities. 49 U.S.C. § 11324(c).

in America. For example, Shell Oil Company, as a condition of its joint venture with Texaco, was required to divest its Anacortes Refining Company plant, located in Anacortes, Washington, to one of its competitors, Tesoro Petroleum Corporation. Shell Oil Company, Docket No. C-3903 (June 11, 1998). To settle claims that Roche Holding Ltd.'s acquisition of Corange Limited eliminated competition, Roche was required to divest itself of one of its drug testing business to another drug company. Roche Holding, Ltd., Docket No. C-3809 (February 25, 1998). Certainly UP cannot be saying that the government, when it orders such divestitures as conditions to a merger, is somehow "taking" property.

The Consensus Plan also calls for UP to share some of its yards and tracks with the PTRA, BNSF, and Tex Mex. UP claims that this means the Consensus Plan would "take UP's yards, its industry trackage, its staging tracks, and its automotive facility for PTRA's exclusive use." UP/SP-356 at 149. This is simply not true. With the exception of the Bayport Loop and the proposed operations in Strang Yard, the PTRA would merely operate over tracks and yards owned by the PTRA itself or the HBT, not UP's tracks. To the extent PTRA operates over HBT tracks and yards, it will fully compensate HBT in the same way in which BNSF, UP, and Tex Mex today compensate HBT. It is curious to note that HBT itself has not objected to the Consensus Plan. Either HBT must not care, or as is more likely, despite UP's assurances that the HBT still exists, it really does not. In essence, the Consensus Plan merely restores neutral switching and operations for the HBT and is a merger of the HBT and PTRA. R.V.S. Ritter at 7-11.



Where PTR, Tex Mex, or BNSF operate over solely owned UP tracks, pursuant to either the neutral switching concept or pursuant to the terminal trackage rights proposed by the Consensus Plan — wherein UP, BNSF, and Tex Mex would each have the right to be routed over any of the tracks located in the Houston terminal pursuant to the directions of the neutral dispatcher — each will pay UP (or the owner of the tracks — HBT) a usage fee equal to the fee that UP currently pays to BNSF when it operates over BNSF's tracks. Consensus Plan, Vol. 1 at 7. Furthermore, nothing in the Consensus Plan requires UP to stop using its own tracks or yards where PTR will operate over or in. Indeed, UP, as the owner of that track, will continue to have the right to also operate over those tracks. R.V.S. Slinkard/Watts at 10. It is likely, however, that due to the efficiencies of the neutral switching concept, UP will find it more cost effective to participate in the neutral switching concept, rather than attempt to operate its own trains. R.V.S. Slinkard/Watts at 21.

Requiring merging railroads, such as UP and SP, to grant to another competing railroad, such as Tex Mex or PTR, trackage rights, yard access, or access to shipper facilities is a standard practice imposed in every single rail merger and as long as the owning railroad is provided compensation for the use of that property, the constitutional standard has been met and there is no taking. The issue whether granting the proposed access over UP's lines or yards to the PTR constitutes a "taking" has been fully addressed by the ICC in *St. Louis Southwestern Railway Company — Trackage Rights Over Missouri Pacific Railroad Company — Kansas City to St. Louis*, 1 I.C.C. 2d 776 (1984) (hereinafter referred to as "SSW Compensation"). In that decision, the ICC was

faced with a dispute between the Denver and Rio Grande Western Railroad Company (DRGW) and UP over the terms of compensation for trackage rights imposed by the ICC to address a competition problem in the consolidation proposal. UP claimed that the trackage rights granted to DRGW were a forced sale, or lease, i.e. a taking, and asserted that the DRGW should pay a 50 percent share of the interest rental value in the property and that the DRGW was a half-owner for purposes of property taxes associated with the line. Disagreeing with UP's position, the ICC held that the imposition of the DRGW's trackage rights "was not a forced sale, or a lease . . . as suggested by UP. Rather, the rights [the ICC] imposed are analogous to a license in the law of property, and compensation (rental) for licenses is often described in terms of usage. UP remains the sole owner of these properties and bears the risk of ownership. We will require rental from DRGW to be computed on the basis of its expected usage in each segment of the line." *Id.* at 790 (emphasis added). As the ICC noted during the BN/SF merger in 1995, "SSW Compensation . . . concluded that where [the ICC] prescribe[s] or set[s] trackage rights as a merger condition, the terms should permit competitive entry by providing for a reasonable return on the fair market value of the property." *Burlington Northern Inc. and Burlington Northern Railroad Company — Control and Merger — Santa Fe Pacific Corporation and The Atchison, Topeka and Santa Fe Railway Company*, Finance Docket No. 32549 (ICC served August 23, 1995) at 90.

This "reasonable return on the fair market value" is fully accounted for through the trackage rights fee that PTRR, Tex Mex, or BNSF would have to pay to operate over HBT's or UP's lines and yards. The SSW Compensation decision makes it crystal-clear



that the imposition of trackage rights does not constitute a taking; that UP would remain the sole owner of the property in question; and that imposing a license to use UP's property is constitutional if UP is compensated for such use. *See also St. Louis Southwestern Railway Company — Directed Service — Chicago, Rock Island & Pacific Railroad Company, Debtor (William M. Gibbons, Trustee) Between Santa Rosa, NM, and St. Louis, MO*, 363 I.C.C. 252 (1980)("[d]irected service over rail lines does not constitute a taking under the fifth amendment to the Constitution . . . [and] even if a fifth amendment taking were found . . . compensation [for the service satisfies] . . . the constitutional requirement of 'just compensation.'"). The plain fact of the matter is that UP would be compensated by the PTRR for its concurrent, and not exclusive, use of UP's tracks, and such compensation obviates any constitutional concerns.

## **2. UP Will Lose Little, If Any, Revenues**

UP claims that the Consensus Plan will cause UP to lose a significant amount of traffic revenue. First to the extent UP loses any revenues, the Board's obligation is to preserve and protect competition, not protect any particular competitor, such as UP, from the effects of competition. *See CSX/NS/Conrail*, Finance Docket No. 33388, Decision No. 89 at 49 (STB served July 23, 1998) ("our concern is the preservation of competition and essential services, not the survival of particular carriers").

Second, UP never estimates how much they would actually lose. Mr. Peterson claims that the Consensus Plan (combined with the Dow, Formosa, and CP&L proposals) will "expose" more than \$419 million of annual UP revenue to competition. UP/SP-356 at 84. Even assuming this statement is correct, such "exposure" does not mean UP will



actually lose that revenue. Competition means that shippers can choose whichever carrier they desire. If UP can provide good service, efficient routes, and good rates, there is no reason to believe that UP will lose even one cent of this traffic. Indeed, UP did not even attempt to quantify how much of this they would actually lose. Despite not quantifying their loss they then make an unsupported assertion that these losses would be "substantial." *Id.*

UP attempts to paint the potential that they would lose substantial amounts of traffic. UP/SP-356 at 84. It is simply not true that UP will have substantial losses due to the Consensus Plan. Of the approximate \$2.8 billion dollar Houston BEA market, UP controls (as stated by UP's own witness, Richard J. Barber) approximately \$1.9 billion (69%) of that total market. Of course, UP did not gain control over this revenue through competing for it in the free market, but by buying SP's share through a government approved merger. Nonetheless, of UP's \$1.9 billion share, the Consensus Plan projects that about \$155 million (or approximately 8% of UP's revenues from Houston) will be diverted from UP to other carriers. Consensus Plan, Vol. 1 at 241.

Of course, this is just a projection and even if this diversion does occur, such diversions will occur precisely because KCS/Tex Mex's and BNSF's routes are more efficient than the UP routes and provide a better alternative to Houston shippers than the existing UP route. In other words, these diversions will occur precisely because of the pro-competitive aspects of the Consensus Plan, not because the government ordered UP to "give" this traffic to the other carriers. Finally, in 1997, UP had gross operating revenues of approximately \$11 billion. Even if the pie remains fixed and all projected

diversions occur, the notion that a loss of less than 1.5% of UP's revenues will somehow cripple UP or require UP to forego infrastructure investment is preposterous.

### **3. The Consensus Plan Is Not An Open Access Plan**

With the exception of the Bayport Loop (including Strang yard), a few shippers located on the Clinton Branch and along the Houston Ship Channel, and shippers served by the GH&H, the Consensus Plan is about restoring the competitive and operating choices that were available to shippers prior to the UP and SP merger. Just prior to the UP/SP merger, a substantial number of Houston shippers were served, either directly or via reciprocal switch, by the PTR A and HBT. The PTR A and HBT provided these shippers with neutral switching and dispatching and gave them the opportunity to use either the BNSF, SP, or UP for the linehaul move to all gateways, including Mexico.

As a result of the UP/SP merger, these HBT and PTR A shippers saw their competitive options reduced to two — UP and BNSF — for all movements to all gateways, except for the Mexican gateways, where these HBT and PTR A shippers still have three options — UP, BNSF, and Tex Mex. When UP and BNSF subsequently eliminated the HBT, these shippers lost the benefit of neutral switching and dispatching and now must depend upon reciprocal switching and its resultant inefficiencies.

The Consensus Plan will restore neutral switching and dispatching to all of the former HBT and PTR A shippers by allowing the PTR A to neutrally switch all of the shippers located on its property and to switch all of the shippers who were formerly switched by the HBT, or were open to reciprocal switch on either the PTR A or HBT. The Consensus Plan does not displace UP's switching operations, but merely allows the



shipper to choose whether to be switched by UP or by the PTR A. The Consensus Plan will also restore meaningful rail competition to Houston, an environment not preserved by the UP/SP-BNSF trackage rights agreement, by restoring the ability of these HBT and PTR A shippers to utilize three carriers for the linehaul move — UP, BNSF, or Tex Mex — the same number of carriers they had before the merger.

This is not some radical, "open access" proposal. Indeed, these shippers can now utilize all three carriers, but cannot use Tex Mex for northbound movements; yet it is precisely for such northbound moves that BNSF has not been able to fully replicate SP's competitive presence for which shippers need access to the KCS/Tex Mex system to compete against UP. It is a relatively simple task to restore neutral switching for these HBT and PTR A shippers and to remove the Tex Mex restriction. Such actions are fully justified as merely preserving and restoring competitive options that were lost.

The only part of the Consensus Plan that could be considered some form of "open access" is the proposal to expand the geographic limits of the neutral switching entity to not only include former HBT and PTR A shippers, but also to include the Bayport Loop, all of the shippers located along the Houston Ship Channel who are not served by the PTR A, the Clinton Branch, and the GH&H. Some of these shippers are so-called "1-to-1" shippers who, prior to the merger were exclusively served by either the SP or UP and would under the Consensus Plan, have the choice to use either BNSF, UP, or Tex Mex, but the number of such shippers is small compared to the overall shippers who would benefit by the Consensus Plan. Despite the fact that some of these shippers are "1-to-1" shippers, the Consensus Parties believe these shippers did suffer competitive harm as a



result of the UP/SP merger so as to justify expansion of the geographical limits of the proposed neutral switching. See Section II B above. The Board has broad discretion when fashioning conditions and should do so as necessary to restore all forms of competition that were lost as a result of the merger.

Overall, the Consensus Plan is not about using "government regulation" to force UP to give up access to shippers which access UP had somehow gained through competing in the free market. Instead, the Consensus Plan is about restoring competitive and operating choices that were taken away when the government allowed UP to merge with SP in the first instance.

**C. The Consensus Plan Has Significant Shipper Support**

**1. Numerous Shippers Recognize UP's Market Power Has Prevented BNSF And Tex Mex From Being Effective Competitors And Support The Consensus Plan**

In response to the Board's invitation, both shippers and carriers filed requests for additional remedial conditions on July 8, 1998. In addition to those individual requests filed on July 8, this filing includes another 70 plus shipper statements endorsing some or all of the principles contained within the Consensus Plan. These 70 plus shippers include such companies as Shell Chemical, Union Carbide, Mobil Oil Corporation, International Paper, E.I. DuPont, Phillips Petroleum Company, Citgo Petroleum Corporation, BASF, Rohm and Haas, and Huntsman Corporation. Major shipper trade associations in the nation, CMA and SPI have endorsed the Consensus Plan and the National Industrial Transportation League, the nation's largest shipper trade association, has endorsed the principles contained within the Consensus Plan.

When one analyzes these filings, a number of factors immediately are clear. First, there is widespread consensus between shippers and carriers about the direct relationship between UP's market power and the failure of service in the Houston/Gulf region. Second, there is overwhelming consensus about the need for the Board to establish remedial conditions which will provide long term solutions to the problems of service and competition in the Houston/Gulf Coast region. Third, both shippers and carriers support part, and in some cases all, of the long term solutions set forth in the Consensus Plan.

Formosa Plastics Corporation submits that UP's overwhelming market power is clearly evident in its failure and/or unwillingness to take responsibility for its poor service. UP has no fear that its customers will take their business elsewhere, and consequently UP has failed to fix the problem or compensate its customers accordingly. *Comments and Request for Remedial Conditions of Formosa Plastics Corporation, U.S.A.*, Finance Docket No. 32760 (Sub-No. 26), filed June 8, 1998 at 14-15. Dow Chemical Company agrees and maintains that in a truly competitive market, shippers would have shifted their business to alternative service providers. DOW-1 at 9. Dow further states that other carriers have been denied sufficient incentive to invest in additional infrastructure due to UP's market power. *Id.* Shell Oil Company and Shell Chemical Company note that their worldwide operations "have been significantly impacted by the UP service meltdown in the western United States and particularly in the Houston/Gulf Coast region." Shell believes that the "degrad[ation in] service levels are a direct consequence of the diminution of rail competition in the Houston/Gulf Coast region," and that the "objectives and operational strategies" of the Consensus Plan would



facilitate the restoration of competition in the Houston/Gulf Coast region. *Joint Comments of Shell Oil Company and Shell Chemical Company*, Finance Docket No. 32760 (Sub-No. 26) filed September 18, 1998.

In addition, International Paper Company, the world's largest paper company, believes that "the service meltdown resulting from the UP/SP merger is unprecedented in all aspects. The International Paper Company has suffered economic damages, experienced inconsistent service and unparalleled delays in transit." International Paper advocates alternative rail service in the future to alleviate service problems and protect competition, including the expansion of rail capacity by the existing rail carriers and the fair and neutral dispatching of all rail traffic, all aspects of the proposed Consensus Plan. *August 27, 1998 letter to the STB*. Indeed, Phillips Petroleum Company recently decided to build additional plastics resin capacity in Canada and not the U.S., due in part to the "out of control rail service on the Gulf Coast." *July 1, 1998 letter to the STB*.

These and the other 70 plus shippers have expressed support for the Consensus Plan, either directly or indirectly, as a way to help alleviate the service problems in the Houston area by giving shippers equal access to competitive carriers. *See e.g. Rhodia, Inc., September 30, 1998 letter to the STB; MFA Incorporated, September 24, 1998 letter to the STB; Inland PaperBoard and Packaging, Inc., September 11, 1998 letter to the STB; Union Camp Corporation, September 3, 1998 letter to the STB; BASF Corporation, August 28, 1998 letter to the STB; Matson Intermodal System, August 4, 1998 letter to the STB; Amerigas Propane LP, July 29, 1998 letter to the STB; Longview Fibre Company,*



*July 29, 1998 letter to the STB; Lyondell-Citgo Refining Company Ltd., July 24, 1998 letter to the STB; Despachos Del Norte, Inc., May 27, 1998 letter to STB.*

Likewise, Mobil Oil Corporation notes that "the Consensus Plan effectively addresses [service] issues and provides solutions for service and competition in the Houston, Texas/Gulf Coast region." *August 31, 1998 letter to the STB.* E. I. DuPont de Nemours and Company, a \$45 billion diversified chemical and energy corporation with over 200 manufacturing sites and almost 100,000 employees worldwide, observes that "competition results in a more profitable and stable marketplace to the benefit of those both providing and receiving the goods and/or services. However, *where failure of the system occurs, some level of government involvement may be required* to restore the competitive balance." As a way to restore the competitive balance in and around the Houston area, DuPont requests that the Board grant Tex Mex permanent rights to access Houston customers. Request for New Remedial Conditions By E. I. DuPont de Nemours and Company, filed in *Union Pacific Corp. et al. — Control and Merger — Southern Pacific Rail Corp. et al.*, Finance Docket No. 32760, July 8, 1998.

Avi-Gran U.S.A., Inc. and CONDEA Vista Company support the restoration of neutral switching and dispatching in the Houston area and allowing KCS/Tex Mex to increase their infrastructure in the Houston area as a way to allow KCS/Tex Mex to provide and preserve service and a competitive alternative. Avi-Gran U.S.A., Inc., *June 5, 1998 letter to the STB; CONDEA Vista Company, March 17, 1998 letter to the STB.*

Jefferson Smurfit Corporation, U.S., a paper packaging corporation operating over 150 manufacturing facilities in the United States, "believe[s] that neutral switching and

neutral dispatching [and] allowing competing railroads to increase their infrastructure will ensure continuing competitive success of the United States in NAFTA trading." *April 22, 1998 letter to the STB.*

Joining these shippers are numerous public interest bodies, who have either endorsed the plan in total or the principles contained within the plan. These bodies include the Port of Houston, Greater Houston Partnership (the equivalent of the Houston Chamber of Commerce), and the Corpus Christi Chamber of Commerce. In addition, the Railroad Commission of Texas ("RCT") is one of the Consensus Parties. All three Republican Commissioners have been elected state-wide and have voted unanimously to endorse and support this filing. Indeed, the RCT has been a leading voice in support of the concepts contained herein. Moreover, last month, the Texas Democratic Party unanimously passed a resolution that calls for "at least three railroads [in the State of Texas] . . . with the ability to serve as many shippers as possible so that the shippers have real competitive choice." *September 15, 1998 letter to the STB.* Joining these bodies are U.S. Congressmen Nick Lampson, Gene Green, Max Sandlin, Kenneth E. Bentsen, Jr., Solomon P. Ortiz, Kenneth E. Bentsen, and the Texas Democratic Party.

Unlike previous Board proceedings, the voice of opposition has largely been unified and harmonious in its consensus that the general conditions imposed upon UP by the Board in the UP/SP merger have not proved sufficient to prevent the meltdown in UP service. Almost all affected parties therefore agree that, at a minimum, the Board needs to intervene by: (i) allowing the plans for improved infrastructure to proceed, (ii) restoring, and in some cases expanding, the access of rail carriers to the shippers and



shortline railroads who lost that access as a result of the merger, (iii) ensuring neutrality of switching and dispatching in the Greater Houston terminal area, and (iv) making permanent the rights granted to KCS/Tex Mex in the Houston/Gulf Coast region. Only when the Board imposes these remedial conditions will the anticompetitive effects of the UP/SP merger be mitigated.

## 2. UP's Position Has Little Texas/Gulf Coast Support

While UP's opposition filing attaches statements from shippers, railroads and governmental officials that oppose the condition requests, upon closer examination it is patently obvious that the majority of statements in support of UP's position come from entities outside the Houston/Gulf Coast area that have not been affected by the service crisis in the Gulf Coast area and that would not benefit from the solutions proposed by the Consensus Plan.

ANALYSIS OF UP v. CONSENSUS PLAN SHIPPER SUPPORT		
	UP	CONSENSUS PLAN
Percentage of total shippers with facilities in Houston, TX	10.7%	17.8%
Percentage of total shippers with facilities in Texas (not Houston)	12.8%	35.6%
Percentage of total shippers who ship through Houston, TX	17.1%	46.6%
Percentage of total shippers who ship through Texas (not Houston)	22.5%	17.8%
Chemical/Plastics shippers located in Houston	3.2%	15.1%
Chemical/Plastics shippers located in Texas (not Houston)	1.6%	11%



Over half of UP's support comes from government officials, the majority of whom are located in Colorado, Idaho, Illinois, Louisiana, Nebraska, New Mexico, Utah and Wyoming—not Texas. *See* Rebuttal Verified Statement of Margaret Kenney ("R.V.S. Kenney") at 25. In fact, out of 306 statements from government officials, over 89% come from outside the State of Texas. R.V.S. Kenney at 6. The other section of UP support consists of shipper statements. However, most of these shippers' statements do not say that they have facilities in Texas and most do not say that they ship through Texas. Out of 187 shippers giving statements, only 48 are located in Texas and only 20 of those are Houston-based. R.V.S. Kenney at 6. By attaching multitudinous statements to its opposition, UP artfully attempts to hide the fact that its position has meager support of the shippers that have suffered through the service crisis in the Gulf Coast and that would benefit from the solutions proposed in the Consensus Plan.

Conversely, the Consensus Plan has overwhelming support from the majority of shippers with facilities in the Houston area or who ship their goods through Houston. *See e.g.* Air Liquide America Corporation, *September 28, 1998 letter to the STB*; Amerigas Propane LP, *July 29, 1998 letter to the STB*; Axis International, *March 10, 1998 letter to the STB*; BOC Gases, *September 28, 1998 letter to the STB*; Conoco Inc., *August 26, 1998 letter to the STB*; LaRoche Industries, Inc., *August 24, 1998 letter to the STB*; Lone Star Steel Company, *August 26, 1998 letter to the STB*; M.G. Maher & Company, Inc., *August 28, 1998 letter to the STB*; and Reagent Chemical, *March 18, 1998 letter to the STB*.

Even more telling is the fact that the Consensus Plan is supported by a majority of chemical and plastics shippers located in and around the Houston area, who ship their products through Houston, and who have been hurt the most by UP's service problems in the Gulf Coast area. *See e.g. Castrol North America, Inc., August 24, 1998 letter to the STB; CertainTeed Corporation, July 24, 1998 letter to the STB; CITGO Petroleum Corporation, July 31, 1998 letter to the STB; FMC Corporation, September 2, 1998 letter to the STB; Huntsman Corporation, July 29, 1998 letter to the STB; Lyondell-Citgo Refining Company Ltd., July 24, 1998 letter to the STB; MG Industries, August 5, 1998 letter to the STB; Mobil Oil Corporation, August 31, 1998 letter to the STB; Rhodia, Inc., September 30, 1998 letter to STB; Rohm and Haas Company, August 7, 1998 letter to the STB; Joint Comments of Shell Oil Company and Shell Chemical Company, Finance Docket No. 32760 (Sub-No. 26), September 18, 1998; and Thermoplastic Services, Inc., September 29, 1998 letter to the STB.*

For example, CONDEA Vista Company, a petrochemical company headquartered in Houston with sales of approximately \$1 billion, believes that a long-term solution to the service problems in South Texas is needed. This long-term solution should include neutral dispatching or switching in Houston and additional yard space and infrastructure for Tex Mex. CONDEA Vista Company, *March 27, 1998 letter to STB*. Moreover, E.I. DuPont de Nemours and Company, which has a facility located on the south side of the Houston Ship Channel, states that despite efforts to work with UP to "alleviate problems arising from UP/SP system congestion," DuPont still found it necessary to turn to competitive routing alternatives. However, those routing alternatives failed to improve



service "because of UP service shortcomings," including UP switching services. Request for New Remedial Conditions by E.I. DuPont de Nemours and Company, Finance Docket No. 32760 (Sub-No. 26), July 8, 1998.

Houston is the location of the largest manufacturing site and export point for Ethyl Corporation ("Ethyl"), a manufacturer and distributor of petroleum additives, lubricants and fuel additives worldwide. Because "the UP/SP merger has disrupted service which has greatly affected [Ethyl's] business," Ethyl "support[s] equal access to all the carriers serving the Gulf Coast, along with the expansion of rail capacity and investment by all the existing carriers . . . to protect . . . future competitiveness [by] ensuring that adequate rail alternatives exist." Ethyl Corporation, *August 31, 1998 letter to the STB*. Similarly, Phillips Petroleum Company ("Phillips"), with major facilities in the Texas Gulf Coast area, states that "[i]t is clear the status quo is no longer acceptable if the rail service problems are to be corrected soon" and "reliable, cost effective rail service must be available in order for [its] plant to remain economically viable in the face of both foreign and domestic corporations." Phillips advocates lifting the restrictions placed on Tex Mex in Decision No. 44, to allow the KCS/Tex Mex infrastructure to help solve the Gulf Coast rail service issues. Phillips Petroleum Company, *July 1, 1998 letter to the STB*.

**D. The Plan Will Work Operationally**

**1. The Plan Is Based Upon Sound Operating Principles**

Notwithstanding UP's dire and over-dramatic assertions to the contrary, the fact is that the operating plans proposed by the Consensus Parties are sound, practicable,



workable, and will help ensure effective and efficient service to all rail shippers in the Houston terminal area.<sup>74</sup> As Mr. William Slinkard and Mr. Watts demonstrate in their Rebuttal Verified Statement herein, the operating plans set out in the Consensus Plan are sound and will permit the vigorous rail competition that the Board envisioned in approving the UP/SP merger to become a reality. *See* Rebuttal Joint Verified Statement of William T. Slinkard and Patrick L. Watts ("R.V.S. Slinkard/Watts").

Before specifically addressing UP's complaints about the Consensus Parties' proposed operating plans, it should be noted that the sponsors of those plans, William T. Slinkard and Patrick L. Watts, have extensive operating experience in the Houston area and elsewhere, and are intimately familiar with service and operational issues pertaining to the PTRRA and throughout the entire Houston rail complex. R.V.S. Slinkard/Watts at 2. Of Mr. Bill Slinkard's 34-year career with the Southern Pacific, he served a total of 11 years in Houston in various capacities, where he developed an intimate knowledge of Houston-area operations, including operations at Strang, Galveston, the PTRRA, the Bayport Loop, Englewood Yard, and the former HB&T. R.V.S. Slinkard/Watts at 1. Mr. Watts is highly experienced in operational issues in Houston having worked in the Operations Department of Southern Pacific and for many years as a dispatcher for, among

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<sup>74</sup> It is ironic indeed that UP now claims the ability to spot a mile away an impending service "meltdown" allegedly to be caused by its competitors, while it confidently forged ahead with post-merger operations of its own in the Houston area that have caused a service crisis of tragic proportions, resulting in billions of dollars in economic damage to the economy of Texas alone. Rather than a "meltdown" of service in Houston — which UP itself has already accomplished — what UP really fears is a meltdown of its own

others, UP. In addition, Mr. Watts has a thorough knowledge of operational issues throughout the Houston area, having worked as a locomotive engineer, conductor, field officer and train dispatcher in the Houston area. R.V.S. Slinkard/Watts at 2.

In general, as will be seen, a number of UP's criticisms fail to withstand scrutiny because UP considers various aspects of the Consensus Plan only in isolation from each other, rather than as an integrated whole whose components work together to form an efficient and workable system.

a. PTRA Operations in the Greater Houston Terminal Area.

In support of the Consensus Parties' proposal for neutral switching and dispatching by the PTRA, the Consensus Plan includes a detailed PTRA Operating Plan, which describes how inbound and outbound Houston and Galveston traffic would be handled, and the resources that will be required to do it. With respect to the handling of inbound Houston traffic, the operating plan provides that inbound Houston traffic will be delivered to one of three yards: Pasadena and Manchester Yards for traffic destined for Houston customers south of the Houston Ship Channel (Pasadena being the primary yard), and North Yard (with support from other satellite yards) for traffic destined for customers north of the Houston Ship Channel. All outbound shipments would be staged at Strang Yard. Consensus Plan, Vol. 1 at 334.

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stranglehold over Houston-area competition, which the Consensus Plan surely *would* cause.

The coordinated and directional use of Pasadena and Strang yards contemplated by the Consensus Plan is similar to plans that have been proposed in the past, including most recently by BNSF. R.V.S. Slinkard/Watts at 3. In fact, the PTRAs operating plan in the Consensus Plan was modeled on the earlier BNSF proposal, R.V.S. Slinkard/Watts at 3, and, understandably, BNSF has voiced no operational concerns about it in this proceeding. What is more, UP itself for the last several months has employed coordinated and directional yard usage, like that contemplated at Pasadena and Strang under the Consensus Plan, at its Englewood and Settegast Yards.

UP protests that the operations contemplated through Pasadena and Strang would not work, based largely on a claimed lack of capacity at those yards. UP/SP-356 at 157-59; UP/SP-358, V.S. Handley at 15-17. But, as Mr. Bill Slinkard and Mr. Watts point out, those concerns are misplaced. The essential flaw in UP's argument is that it fails to recognize — or ignores — the very significant operational efficiencies that will result in converting Pasadena and Strang from bidirectional operations to unidirectional operations. Currently, both yards "turn over" between inbound and outbound traffic several times every day. R.V.S. Slinkard/Watts at 4. UP's own witness acknowledges that under UP's current operation, Pasadena Yard must be turned over once every shift — that is, three times every day. UP/SP-358, V.S. Handley at 13. These multiple daily changes of direction are enormously inefficient, resulting in up to 8 hours — the equivalent of a full shift — of lost switching productivity for each of the two yards every day. R.V.S. Slinkard/Watts at 4. Eliminating that daily "turnover" at both yards will substantially increase the efficiency of switching operations and enable the yards to



accommodate the traffic contemplated under the Consensus Plan. R.V.S. Slinkard/Watts at 4. Furthermore, Mr. Bill Slinkard and Mr. Watts explain that, contrary to UP's argument, traffic will move between Pasadena and Strang smoothly, and not in the "awkward" fashion UP foresees. R.V.S. Slinkard/Watts at 4-5.

UP also asserts that the Consensus Plan would impair UP's current "bypass blocking" at Strang. UP claims that because PTRAs's operating rules require it to build the same number of blocks for all member carriers, making Tex Mex trains at Strang would limit PTRAs's ability to build the necessary UP blocks there. UP/SP-356 at 161-62; UP/SP-358, V.S. Handley at 16. But the PTRAs Operating Agreement does not require PTRAs to build the same number of blocks for all member roads; in fact, today PTRAs builds more blocks for UP, for example, than it does for Tex Mex. R.V.S. Slinkard/Watts at 5. Far from posing any operational impediment to creating sufficient blocks for UP, the Consensus Plan, by virtue of the efficiencies that will be gained by eliminating the constant turnover of Strang between inbound and outbound use will permit the yard to accommodate the one new Tex Mex block and two additional BNSF blocks expected under the Plan. R.V.S. Slinkard/Watts at 5-6.

With respect to service to customers on the former HBT and others north of the Houston Ship Channel, the Consensus Plan contemplates delivery of inbound cars to PTRAs's North Yard, with support from satellite yard operations at Basin Yard, Dallerup Yard, Congress Yard, and the Glass Track and Lead. UP questions the feasibility of the North Yard operations contemplated in the operating plan. But in doing so, UP simply ignores the capacity of Basin and the other yards to provide this support function. R.V.S.