UNITED STATES OF AMERICA

SURFACE TRANSPORTATION BOARD

+ + + + +

ORAL ARGUMENT

IN THE MATTER OF:	:	
UNION PACIFIC CORPORATION, UNION PACIFIC RAILROAD COMPANY, and MISSOURI PACIFIC RAILROAD COMPANY	:	Finance Docket No. 32760 Sub 26
- 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.	:	

Tuesday
December 15, 1998

Surface Transportation Board
Hearing Room 760
1925 K Street, N.W.
Washington, D.C.

The above-entitled matter came on for hearing, pursuant to notice, at 10:00 a.m.

BEFORE:

LINDA J. MORGAN — Chairperson
GUS OWEN — Vice Chairperson

APPEARANCES:

On Behalf of Union Pacific Corporation, Union Pacific Railroad Company, and Missouri Pacific Railroad Company:

MICHAEL L. ROSENTHAL, Esq.
ARVID E. ROACH, II, Esq.
MICHAEL HEMMER, Esq.
S. WILLIAM LIVINGSTON, Jr., Esq.
KAREN KRAMER, Esq.
DAVID L. MEYER, Esq.
of: Covington & Burling
1201 Pennsylvania Avenue, N.W.
P.O. Box 7566
Washington, DC 20044-7566
(202) 662-5388

LOUISE A. RINN, Esq.
General Attorney
Union Pacific Railroad Company
1416 Dodge Street
Omaha, Nebraska 68179
(402) 271-4227

On Behalf of Southern Pacific Rail Corporation, Southern Pacific Transportation Company, St. Louis Southwestern Railway Company, SPCSL Corp., and the Denver and Rio Grande Western Railroad Company:

PAUL A. CUNNINGHAM, Esq.
GERALD P. NORTON, Esq.
of: Harkins Cunningham
1300 19th Street, N.W.
Suite 600
Washington, DC 20036-1609
(202) 973-7600

APPEARANCES (continued):

On Behalf of Kansas City Southern Railroad Company:

WILLIAM A. MULLINS, ESQ.
SANDRA L. BROWN, ESQ.
of: Troutman Sanders, LLP
1300 I Street, N.W.
Suite 500 East
Washington, D.C. 20005-3314
(202) 274-2953
(202) 274-2959

On Behalf of Kansas City Southern Railroad Company:

ALAN E. LUBEL, Esq.
DAVID FOSHEE, Esq.
of: Troutman Sanders, Attorneys at Law
Nationsbank Plaza, Suite 5200
600 Peachtree Street, N.E.
Atlanta, Georgia 30308-2216
(404) 885-3174

On Behalf of Texas Mexican Railway Company and Sierra Pacific Power Company:

RICHARD A. ALLEN, Esq.
JOHN V. EDWARDS, Esq.
JENNIFER OAKLEY, Esq.
SCOTT ZIMMERMAN, Esq.
of: Zuckert, Scoutt & Rasenberger, LLP
888 17th Street, N.W.
Washington, DC 20006-3959
(202) 298-8660

APPEARANCES (continued):

On Behalf of Railway Labor Executives Association and United Transportation Union:

DONALD F. GRIFFIN, Esq.
RICHARD S. EDELMAN, Esq.
of: Highsaw, Mahoney, & Clarke, P.C.
Suite 210
1050 17th Street, N.W.
Washington, DC 20036
(202) 296-8500

On Behalf of the National Industrial Transportation League:

FREDERICK L. WOOD, Esq.
of: Donelan, Cleary, Wood and Maser, P.C.
Suite 750
1100 New York Avenue, N.W.
Washington, DC 20005-3934
(202) [illegible]

On Behalf of Western Coal Traffic League:

C. MICHAEL LOFTUS, Esq.
CHRISTOPHER A. MILLS, Esq.
JOHN H. LESEUR, Esq.
of: Slover and Loftus
1224 17th Street, N.W.
Washington, DC 20036
(202) 347-7170

On Behalf of International Paper Company and Utah Railway Corporation:

ANDREW T. GOODSON, Esq.
EDWARD D. GREENBERG, Esq.
CHARLES H. WHITE, Jr., Esq.
of: Galland, Kharasch, Morse & Garfinkle, P.C.
1054 31st Street, N.W.
Washington, DC 20007
(202) 342-6750

APPEARANCES (continued):

On Behalf of the Department of Justice:

JOAN S. HUGGLER, Esq.
MICHAEL D. BILLIEL, Esq.
Trial Attorneys
Antitrust Division
of: The Department of Justice
555 Fourth Street, N.W.
Room 9409
Washington, DC 20001
(202) 307-6666

On Behalf of the Save the Rock Island Committee, Inc.:

WILLIAM P. JACKSON, Jr., Esq.
JOHN T. SULLIVAN, Esq.
of: Jackson and Jessup, P.C.
3426 North Arlington Blvd.
Arlington, Virginia 22201
(703) 525-4050

On Behalf of the Society of the Plastics Industry, Inc.:

MARTIN W. BERCOVICI, Esq.
of: Keller and Heckman
1001 G Street, N.W.
Washington, DC 20001
(202) 434-4144

On Behalf of Geneva Steel:

JOHN W. ONGMAN, Esq.
of: Pepper, Hamilton & Scheetz
1300 Nineteenth Street, N.W.
Washington, DC 20036
(202) 828-1415

APPEARANCES (continued):

On Behalf of Coastal Corporation:

ROBERT M. BRUSKIN, Esq.
ROSEMARY H. McENERY, Esq.
MARK JOSEPHS, Esq.
of: Howrey & Simon
1299 Pennsylvania Avenue, N.W.
Washington, DC 20004-2402
(202) 783-0800

On Behalf of Burlington Northern Railroad Company, and The Atchison, Topeka & Santa Fe Railway Company:

RICHARD WEICHER, Esq.
of: Burlington Northern Santa Fe
1700 East Golf Road
Schaumburg, Illinois 60173
(708) 995-6887

ERIKA Z. JONES, Esq.
ADRIAN L. STEEL, Jr., Esq.
of: Mayer, Brown & Platt
2000 Pennsylvania Avenue, N.W.
Washington, DC 20006
(202) 463-2000

On Behalf of the International Union of Machinists and Aerospace Workers:

DEBRA L. WILLEN, Esq.
of: Guerrieri, Edmond & Clayman, P.C.
1331 F Street, N.W.
Washington, DC 20004

APPEARANCES (continued):

On Behalf of the Transportation Communications International Union:

LARRY R. PRUDEN, Esq.
3 Research Place
Rockville, MD 20850
(301) 948-4910

On Behalf of Illinois Central Railroad:

KEVIN M. SHEYS, Esq.
of: Oppenheimer, Wolff and Donnelly
1020 19th Street, N.W.
Suite 400
Washington, DC 20036
(202) 293-6300

On Behalf of Consolidated Rail Corporation:

WILLIAM J. KOASKY, Esq.
A. STEPHEN HUT, Jr., Esq.
STEVEN P. FINIZIO, Esq.
of: Wilmer, Cutler & Pickering
2445 M Street, N.W.
Washington, DC 20037
(202) 663-6235

On Behalf of the International Brotherhood of Teamsters:

MARC J. FINK, Esq.
of: Sher & Blackwell
Suite 612
2000 L street, N.W.
Washington, DC 20036
(202) 463-2503

APPEARANCES (continued):

On Behalf of Kennecott Utah Copper Corp. and Kennecott Energy Company:

JEFFREY O. MORENO, Esq.
JOHN K. MASER, III, Esq.
of: Donelan, Cleary, Wood & Maser, P.C.
Suite 750
1100 New York Avenue, N.W.
Washington, DC 20005
(202) 371-9500

On Behalf of Arizona Electric Power Cooperative, Central Power and Light Company, City of Austin, Texas, Commonwealth Edison Company, and Lower Colorado River Authority:

C. MICHAEL LOFTUS, Esq.
of: Slover & Loftus
1224 17th Street, N.W.
Washington, DC 20036
(202) 347-7170

ALSO PRESENT:

G. Randy Speight
Jerry Martin
Albert B. Krachman
Kenneth B. Cotton
Donald G. Avery
Nicholas DiMichael
Ralph W. Whitfield
Andrew Goldstein
Richard Davidson
Mary Mc Auliffe
Bill Mullins
Larry Thomas

C-O-N-T-E-N-T-S

Opening Remarks

Chairperson Morgan 12

Proponents of Conditions

1. Sponsors of the "Consensus Plan"

The Chemical Manufactures Association
G. Randy Speight 14

The Texas Mexican Railway Company
Richard A. Allen 22

The Railroad Commission of Texas
Jerry Martin 36

2. The Burlington Northern and Santa Fe Railway Company
Richard E. Weicher 51

3. Capital Metropolitan Transportation Authority
Albert B. Krachman 80

4. Houston and Gulf Coast Railroad
Kenneth B. Cotton 89

5. Central Power & Light Company
Donald G. Avery 102

6. The Dow Chemical Company
Nicholas DiMichael 108

7. E. I. du Pont de Nemours and Company
Ralph W. Whitfield 118

8. Formosa Plastics Corporation, U.S.A.
Andrew Goldstein 123

C-O-N-T-E-N-T-S (CONT.)

Responses to Proponents of Conditions

1. Union Pacific Railroad Company
Arvid E. Roach 129
Michael Hemmer
Michael Rosenthal
Richard Davidson
Mary McAuliffe

2. The Texas Mexican Railway Company
Richard A. Allen 176

Rebuttal

The Kansas City Southern Railway Company
Bill Mullins 180

The Society of the Plastic Industry, Inc.
Larry Thomas 196

Closing Remarks

Chairperson Morgan 202

P-R-O-C-E-E-D-I-N-G-S

(10:10 a.m.)

CHAIRPERSON MORGAN: Good morning. You may notice that some of our staff here today look a little somber. Over night, we lost one of our family, one of our friends here at the Board. His name was William Freddie Hall. He was 49 years old. He served 31 years in the Federal Government. He was with the ICC, STB since 1968 in various offices. Can people hear me? He was a veteran, so our flag is flying at half staff.

Needless to say, when you have a staff of 135 people and you lose one person, it affects us all. Freddie was one of our most valuable. He was one of our most spirited. He was one of our most decent. He was one of our best.

As those of you who know me know, I always have a few quotes when I'm talking about something or someone. I picked two quotes out in honor of Freddie. The first is "Make your love visible in the world through your work." Freddie always did that. He always had a smile on his face. Believe me, we need

smiles at the Board. He always provided that to us. We will miss that.

Another quote which sort of represents this morning I think for everyone at the Board, and it reads as follows: "Sadness flies on the wings of morning. Out of darkness comes the light." Freddie was a light. We will remember your light, Freddie, today and in the future.

With that, I would just like to have a moment of silence in Freddie's honor. Then we will take a brief two or three minute recess. Then we will begin with the hearing.

(Whereupon, a moment of silence was taken.)

CHAIRPERSON MORGAN: Thank you all. I know that the staff here appreciates that. Gus and I will be back in a minute.

(Whereupon, the foregoing matter went off the record at 10:12 a.m. and went back on the record at 10:15 a.m.)

CHAIRPERSON MORGAN: Today we are holding an oral argument on proposals for permanently altering

the way in which rail service is provided in the Houston Gulf Coast area. This oral argument is part of the proceeding that the Board initiated as part of its oversight of the Union Pacific/Southern Pacific merger.

The Board has received voluminous filings in this proceeding. Today I do not expect that we will have a rehash of all of the pleadings, but rather that the parties will use this opportunity to focus on the key issues in the proceeding. The Board members intend likewise to focus their questions on the key issues under review.

Today we have divided the witnesses into three groups, but I will call groups of people up as appropriate. Just a minute about the timing lights. Most of you are familiar with it. But when the green light comes on, you have one minute left. When your time is up, you will see a red light and a double chime.

Also, let me point out that the statements that were submitted for today's oral argument are on the Board's website.

With respect to breaks, we will have none. Now if the Vice Chairman has any remarks before we begin, I'll turn it to him.

VICE CHAIRMAN OWEN: None, thank you.

CHAIRPERSON MORGAN: Let us begin then with the sponsors of the Consensus Plan. We have Randy Speight, representing the Chemical Manufacturers Association; Richard Allen, representing Tex-Mex Railway; and Jerry Martin, representing the Railroad Commission of Texas. Do you all want to come forward?

Good morning.

MR. SPEIGHT: Good morning, Chairman Morgan and Vice Chairman Owen. I am Randy Speight, managing director of distribution programs and distribution staff team leader at the Chemical Manufacturers Association.

I appreciate this opportunity to appear before the Board to discuss the Consensus Plan from the shipper perspective. With me today are Jim Woodrick, president of the Texas Chemical Council, which represents the chemical plant managers in that state, and CMA's counsel, Tom Shick.

On behalf of the Consensus parties, I will discuss the competitive impacts of the UP/SP merger, and why merger conditions adopted by the Board in 1996 should now be revised.

Dick Allen will speak next for the Texas Mexican Railway to address two aspects of the Consensus Plan. The specific use in area rail infrastructure improvements that are included in the Consensus Plan, and why the Board should permanently remove the restriction on Tex-Mex trackage rights.

Following Mr. Allen, Jerry Martin will explain why the Railroad Commission of Texas joined with shippers and carriers to develop the Consensus Plan.

CMA's membership consists of approximately 200 companies that account for more than 90 percent of the basic industrial chemical production capacity in this country. The U.S. chemical industry depends heavily on railroads for the safe and efficient transportation of a wide array of raw materials and finished products.

The importance of rail transportation is

highlighted by the fact that the chemical industry annually ships 140 million tons by rail, spends $4.5 billion on rail freight, and contributes 14 percent of the total U.S. rail industry revenue.

High quality rail service is critical for CMA members with production facilities on the Gulf Coast. Texas leads the nation in chemical manufacturing. With shipments valued at $57 billion in 1996, Texas accounts for nearly 16 percent of total U.S. chemical output.

CMA participated in the UP/SP merger docket, the subsequent oversight proceedings, and ex parte 573. CMA urges the Board to adopt the Consensus Plan to restore and enhance rail competition in the Houston Gulf Coast region. Competition in turn will improve service to all shippers and promote investment in rail infrastructure.

We are here today because of a significant condition that the Board imposed on its approval of the UP/SP merger. That condition is five years of oversight. As the Board declared when it opened this docket, the oversight condition established not a

static process, but a continuing one. The Board noted that it retained jurisdiction to monitor the competitive consequences of this merger and to impose additional remedial conditions if those previously afforded proved insufficient.

CHAIRPERSON MORGAN: If I could stop you right there, because I want to make sure we go through some key issues here today with you. We have a set schedule.

I presume you and I are in agreement as to the legal standards by which we would adopt the Consensus Plan or some other proposal. That is, we must find that market power created by the merger resulted in competitive harm for which whatever proposal has been presented addresses the harm. Is that correct?

MR. SPEIGHT: That's correct.

CHAIRPERSON MORGAN: Are we in agreement with that, so that if the Board doesn't find one of those things, doesn't find for example, that the market power did result in the harm that you are addressing or that the proposal does not specifically

address the harm, assuming we find it, that then in order to get to the remedy that you and others are supporting, we would basically be going to open access. Is that right?

MR. SPEIGHT: Chairman Morgan, we are in agreement.

The Consensus Plan responds directly to the Board's March 31st statement that it would thoroughly explore anew the legitimacy and viability of longer term proposals for new conditions to the merger that pertained to service and competition in the Houston Gulf Coast region. CMA and the other Consensus parties believe that the time for new conditions is now.

BNSF's trackage rights on UP's lines were to provide competition for shippers that were previously served by both UP and the SP. This approach has not succeeded in the Houston Gulf Coast region. The record contains numerous statements of CMA members who have experienced a lack of competition since that merger.

This absence of competition is shown by

the fact that during the service crisis, UP's share of Houston rail traffic remained high. UP's contracts were open to allow shippers access to other carriers, and those carriers obtained expanded rights. Yet UP retained a remarkably high share of the traffic, despite its service difficulties.

Data for the first six months of 1998 show that the UP maintained overwhelming shares of the traffic, especially between Houston and points in the northeast and the southeast. If there were effective competition in the Houston Gulf Coast area, UP could not have maintained its market share under those conditions.

I would like to emphasize several significant points. We acknowledge that the UP has recovered much of the ground it lost during the service crisis. CMA commends the UP on that achievement. But a Board finding that the Consensus Plan is in the public interest should not hinge on UP's current level of service. To the contrary, this proceeding was established explicitly to examine the remedies and proposals that were available to the

Board under service order number 1518.

CHAIRPERSON MORGAN: Let me stop you again there, Mr. Speight. In terms of service, let me make sure I understand. Do you agree that service has improved since the Board initially got into this matter relative to Houston and the emergency order?

MR. SPEIGHT: Indeed, service has improved relative to the period of time during the service crisis, Madam Chairman.

UP clearly agreed that the Board could consider such proposals through the five year oversight condition. UP's representative stated in 1996 that the Board, and I quote, "Will have unrestricted power to impose additional conditions. There is no reason that a year or two or three, if the Board concludes that divestiture is appropriate, you can't require it."

The Consensus Plan is a joint product of a unique coalition consisting of three shipper groups, two railroads, and the Texas state government agency designated to address rail mergers and competition. Further, in developing the Consensus Plan, we

consulted with other interested organizations, including the Greater Houston Partnership, the Port of Houston Authority, and the National Industrial Transportation League. I urge you to review their comments, which are substantially consistent with the Consensus Plan.

In conclusion, CMA urges the Board to adopt the Consensus Plan with its eight inter-related provisions. The Consensus Plan will restore competition that has been lost in the Houston Gulf Coast area. Competition in turn will stimulate better rail service and additional rail infrastructure.

Chairman Morgan, Vice Chairman Owen, thank you.

CHAIRPERSON MORGAN: Let me ask you a couple other questions if I might. Your organization has been quoted as saying that granting the relief that you support here in Houston would be the first step in getting open access throughout the system. Is that your organization's position here today?

MR. SPEIGHT: Madam Chairman, I don't recall that CMA has addressed this as a first step in

getting open access, the quotes that I am familiar with with CMA. If you have quotes that I am unaware of, I would certainly like to be made aware of those.

CHAIRPERSON MORGAN: It has been reported that that has been said by someone at CMA. My follow-up question to that is getting back to my first question to you, which is that in the context of this proceeding, we have I think you and I agree on the legal standards that we're applying here. In terms of granting open access, that is something that perhaps is better debated in Congress. Do you agree with that?

MR. SPEIGHT: And I would agree, Madam Chairman, that the purpose for CMA being here today is limited to the scope of this Consensus Plan in the Houston area, expressly to restore competition that was lost in the Houston Gulf area as a result of the UP/SP merger. That's the extent.

CHAIRPERSON MORGAN: Thank you.

MR. SPEIGHT: Thank you.

MR. ALLEN: Good morning, Chairman Morgan, Vice Chairman Owen. My name is Richard Allen. I am

here speaking this morning in support of the Consensus Plan on behalf of the Texas Mexican Railway, one of the proponents of that plan.

With me here today are Larry Fields, the president of Tex-Mex, and Pat Watts, Tex-Mex's vice president for transportation. We very much appreciate your giving us the opportunity to be here this morning.

In the time I have, I would like to emphasize the following points. First, as Mr. Speight has explained, the essential purpose of the Consensus Plan is to restore rail competition in the Houston Gulf Coast area to pre-merger levels. The purpose of the plan is not and has never been to remedy UP's service breakdown in rail service over the past year and a half, as devastating as that breakdown has been to shippers and to the economy of the entire nation.

Nevertheless, the UP's service crisis is highly relevant to the need for the Consensus Plan because its dramatically illuminated the loss of rail competition in and around Houston caused by the UP/SP merger.

Perhaps the clearest evidence of this loss can be seen in the analysis of what's happened to service to so-called two-to-one shippers since the UP/SP merger. These are shippers which before the merger were served by two railroads, UP and SP. In its decision approving the UP/SP merger, the Board concluded that giving trackage rights to the Burlington Northern Santa Fe to serve these shippers would preserve the competition that existed before the merger.

But the facts have shown dramatically and conclusively that that didn't happen. Before the merger, the Southern Pacific had 32 percent of the traffic to those two-to-one shippers, and UP had the other 68 percent. In the first half of 1968, however, not withstanding the meltdown of service on the merged UP/SP system, the BNSF accounted for only nine percent of the service to those two-to-one shippers. The merged UPSP system retained an astounding 91 percent.

If those shippers really had a competitive alternative, a meaningful competitive alternative when faced with UP's terrible service, surely BNSF's share

of their traffic would have been at least as high as SP's had been before the merger. Clearly the remedies the Board counted on in its decision to preserve rail competition have not worked.

Each of the eight elements of the Consensus Plan will help significantly to restore competition in the Houston Gulf Coast region to its pre-merger levels. By doing so, the Consensus Plan will help to ensure that any future breakdown in rail service by any one railroad will not have the devastating impact on shippers and on the economy that UP's breakdown has had.

CHAIRPERSON MORGAN: Let me just stop you, if I might, on this issue of pre-merger competition. Because I think I want to make sure I understand your position.

You obviously have one-to-one shippers, two-to-one shippers, three-to-two shippers. I mean that's the world we're talking about.

MR. ALLEN: Basically.

CHAIRPERSON MORGAN: Pre-merger. And all those shippers, as I get it, are being addressed in

the context of this plan that's before us. Am I right?

MR. ALLEN: Yes.

CHAIRPERSON MORGAN: So when you talk about pre-merger competition, shippers that were served by one carrier are served by one carrier today. Shippers that were served by two carriers and would have gone to one were dealt with in the context of the UP/SP merger approval. Right?

MR. ALLEN: That's correct.

CHAIRPERSON MORGAN: Then of course we have the interests in going from shippers who are served by two carriers today to three, which is the other part of this. As you know, when the Board approved the merger, they believed that going from three to two was not anti-competitive.

Have I described the situation?

MR. ALLEN: Yes, you have, Madam Chairman.

CHAIRPERSON MORGAN: Then the other piece of this is that in terms of the share that you are talking about, it is possible that BN Santa Fe, the presence of BN Santa Fe as a competitor, for example,

might have lowered the rates for shippers that are served by UP. So while those shippers did not go to BN Santa Fe, they stayed with UP, but they paid lower rates.

MR. ALLEN: That's possible.

CHAIRPERSON MORGAN: Do you disagree with that? That is in the record. Do you disagree with that?

MR. ALLEN: Well, I think it's possible, but I don't think that the record establishes that the rates for those shippers did go down from pre-merger levels.

CHAIRPERSON MORGAN: So you disagree with the evidence that's in the record on that point?

MR. ALLEN: Well I don't believe there is any evidence.

CHAIRPERSON MORGAN: There is. But in any event -- so have I described the situation pre-merger, post-merger accurately?

MR. ALLEN: Well, yes you have.

CHAIRPERSON MORGAN: And described the plan that you are proposing in terms of which shippers

you are seeking for us to address?

MR. ALLEN: Well, the plan that we have proposed would affect all shippers in the Houston Gulf Coast region, including two-to-ones, one-to-ones, and three-to-twos. That's correct.

CHAIRPERSON MORGAN: That's fine. I just want to make sure I'm with you on that.

MR. ALLEN: Okay.

The second point I want to stress this morning is that two of the elements of the Consensus Plan will help restore competition by adding very substantially to rail infrastructure in the region. The Board itself has identified lack of rail infrastructure as a major cause of the UP service crisis. These two elements of the plan specifically address that problem.

One involves Tex-Mex's proposal to acquire and restore the out-of-service line between Victoria and Rosenberg, Texas. The other involves Tex-Mex's proposal to construct a second track on UP's Lafayette subdivision between Houston and Beaumont.

The restoration of the line between

Victoria and Houston -- between Victoria and Rosenberg will enormously add to Tex-Mex's efficiency and competitiveness. It will reduce the distance of Tex-Mex's route from Laredo to Houston by 70 miles, and it will take Tex-Mex off 157 miles of UP trackage, including the heavily congested Glidden subdivision that's now used by UP, BNSF, Tex-Mex and Amtrak.

The proposal of Tex-Mex to construct a second track between Houston and Beaumont will also add very substantially to the capacity between -- on that very heavily used route, and thereby add substantially to the competitiveness and competitive alternatives available to shippers.

The third point I want to stress is that these infrastructure proposals are not stand-alone proposals, but are vitally dependent on other elements of the Consensus Plan. These infrastructure proposals will require an investment by Tex-Mex of more than $120 million of its own funds. Tex-Mex could not make that investment unless other elements of the Consensus Plan are granted.

This leads to my final point. The

linchpin of the Consensus Plan on which all other elements depend, is the first element, the lifting of the restriction on Tex-Mex's trackage rights that prevent it from carrying traffic between Houston and Beaumont unless that traffic has had a prior or subsequent move on Tex-Mex's line.

We have shown in our filings how that restriction has been a serious and wholly artificial obstacle to Tex-Mex's effort to be an effective competitive alternative to UP. Whereas UP and BNSF too, for that matter, can go to their customers in Houston and say we can handle all of your business, Tex-Mex has to tell them I'm sorry, we can handle only part of your business.

How can you compete effectively like that? It would be like saying to a service station you can provide any service to your customers except you can't check their oil or fill their tires. No service station could compete effectively in the long run against other full-service service stations with those kind of conditions.

Furthermore, unless the restriction is

lifted, there is simply no way that Tex-Mex could make the investment in infrastructure that the Consensus Plan calls for. As we have shown, in 1997, Tex-Mex actually had a net loss of $1.2 million. While we are hopeful that the reduction in congestion on the UP lines will help Tex-Mex improve that performance, there is simply no way that Tex-Mex could justify an investment of $120 million in capital investments outside of its own lines unless the restriction on its trackage rights were lifted.

VICE CHAIRMAN OWEN: Excuse me, Mr. Allen. Could I interrupt for a moment?

MR. ALLEN: Yes, indeed.

VICE CHAIRMAN OWEN: Going back to the merger, what were the economic benefits that were gained by Tex-Mex from that? I believe they were fairly substantial, were they not, from the conditions we imposed upon the merger, that were benefitted to Tex-Mex?

MR. ALLEN: The merger certainly granted Tex-Mex very significant --

VICE CHAIRMAN OWEN: Economic benefits,

right?

MR. ALLEN: Very significant trackage rights. In terms of the economic benefits, as it turned out, in 1997, we actually lost money. So economic benefits remains an open question.

VICE CHAIRMAN OWEN: But then based upon that, then you should have been encouraged to make investments such as UP is making investments in the infrastructure. Is that accurate?

MR. ALLEN: We have been encouraged and have indeed made very substantial investments on our system.

VICE CHAIRMAN OWEN: And now you are back to expand upon those economic benefits that you want granted additional economic benefits. Do you see any tradeoffs that you might give to Union Pacific to grant you any of these things?

Typically this is the reason that we advocate that you stay in the private sector, resolve these issues before coming before a regulatory body such as ours.

MR. ALLEN: I think the major tradeoff is

that we would provide $120 million of capital investments in the Texas Houston Gulf Coast area that's going to benefit all carriers and all shippers that serve that area.

CHAIRPERSON MORGAN: If I could follow up on the Vice Chairman's question just for a minute. I do believe in the record that you do project improved revenues for the future. Is that right?

MR. ALLEN: Yes.

CHAIRPERSON MORGAN: I mean you have just mentioned the losses, but you do have in the record a projection for improved revenues.

MR. ALLEN: Yes. We do. Yes.

CHAIRPERSON MORGAN: I do have one other question related to dispatching, if your -- your time is up, but I'm trying to --

MR. ALLEN: I am happy to answer your questions if I can.

CHAIRPERSON MORGAN: You in the record have indicated the concerns about discrimination in dispatching.

MR. ALLEN: That is very true.

CHAIRPERSON MORGAN: That has been mentioned in your filing. That you would prefer entities other than UP and BNSF to be handling the dispatch.

MR. ALLEN: Absolutely.

CHAIRPERSON MORGAN: No we do have the Spring Center. It seems to me that it would help if you were there. Do you disagree with that? If you were participating in the Spring Center dispatching activity, that that would be helpful?

MR. ALLEN: Well, as we have said in our filings, we don't really think that our participation, at least in the sense that UP envisions, that is particularly helpful because UP still controls the dispatching. Yes, we could move our dispatchers on the Tex-Mex lines up to the Spring Center, but that wouldn't particularly help our problems in Houston. Our trains would still be dispatched by UP from the Spring Center. They would tell us when our trains could move. They would tell us where our trains have to go. That's the problem. That's the fundamental problem.

CHAIRPERSON MORGAN: But, and you can help me with this now, the concept of a joint dispatching center where the three of you would participate jointly is that there is equal participation in dispatching.

Now is there something I am missing in that?

MR. ALLEN: I think there is, because the fundamental problem is that UP would continue to control the dispatching on UP lines at the Spring Center. They are not proposing to give us any control over the dispatching.

CHAIRPERSON MORGAN: Are you participating now in the operations of the Spring Center?

MR. ALLEN: We have an observer there, but we don't do our dispatching from there.

CHAIRPERSON MORGAN: So in terms of actual experience at the Spring Center with joint activity, you don't have that. You have an observer, but in terms of active participation --

MR. ALLEN: Of actually dispatching, that's correct. We don't have any experience.

CHAIRPERSON MORGAN: Thank you.

MR. ALLEN: Thank you very much.

CHAIRPERSON MORGAN: Thank you.

Mr. Martin?

MR. MARTIN: Chairman Morgan, Vice Chairman Owen, good morning. My name is Jerry Martin. I am director of the rail division of the Railroad Commission of Texas.

The Texas Railroad Commissioners are today, in fact at this very moment, they are in their final public meeting of this year and consequently they are unable to be here. But as you know, they have great interest in the issues being addressed today, issues which have had and will continue to have such a profound impact on Texas, and wanted very much to be a part of this critical dialogue.

I am here on behalf of the Commission to urge this body to permanently restore rail competition to the Houston Gulf Coast area by imposing as new remedial conditions on the Union Pacific/Southern Pacific merger those elements set forth in the Consensus Plan.

We believe that these new conditions will help to alleviate the competitive problems in the Houston Gulf Coast area by restoring genuine competition to the region and help ensure that Texas manufacturers, shippers, and our citizens will never again suffer the devastating financial losses experienced in the last 18 months.

Since Governor Bush asked us over three years ago to evaluate the proposed merger, our focus as public servants and not those that have a personal financial interest at stake, has been on simply attempting to determine what is in the best interest of Texas.

As you know, we have not taken this task lightly. After an extensive and comprehensive analysis of the proposed merger, which included listening to potentially affected citizens through public hearings around the state, and receiving input from a team of economic and rail industry experts, we concluded that without the imposition of significant additional conditions, the merger would not be in the public interest, because it would effectively reduce

rail competition in Texas.

As you will recall, promises were abundant throughout the deliberative and approval process that the merger would bring tremendous service improvements to UP/SP customers, and that any competitive harm would be heavily outweighed by broad-based positive effects of the merger.

VICE CHAIRMAN OWEN: Excuse me, Mr. Martin, if I could interrupt and go back just a moment there.

MR. MARTIN: Yes, sir.

VICE CHAIRMAN OWEN: You're indicating that the merger was not in the best interest. My question is to you then where do you see the investment coming from to build out the infrastructure in the sense that UP is trying to do it now? Where would you have proposed that investment come from to do all of those capital improvements required by the port and by the Houston area there?

MR. MARTIN: Well, it is the Commission --

VICE CHAIRMAN OWEN: The taxpayers? Would you have it fragmented amongst a number of different

railroads?

MR. MARTIN: I think probably the latter as opposed certainly not, I don't advocate that the taxpayers per se pay it. But as you just heard the previous witness, there are other railroads. Union Pacific is not the only railroad that advocates infrastructure. We believe that when other railroads are allowed to serve companies there, they will have the encouragement they need to spend money.

VICE CHAIRMAN OWEN: I agree with you on that point, but when you take a look at the railroad system, the infrastructure in Houston, the criss-crossing of the tracks there and so forth is just horrendous. It's what seems like you needed a single entity of such to give some guidance to it.

It's just a question. You didn't answer me as to where the money would come from on that infrastructure investment. That's what I was asking about.

MR. MARTIN: Okay. Well, and what I was saying is is I think that other railroads. But to be more responsive to your question, Vice Chairman Owen,

the Railroad Commission has impaneled a rail advisory committee in Texas to discuss -- do I need to continue?

CHAIRPERSON MORGAN: Please proceed.

MR. MARTIN: Do discuss these issues. They have just given a report to the Commission. While there was not any definitive answer to that, there were a number of funding-related mechanisms that were discussed. The Commission may propose something, you know, that would be a mix of industry funds, general revenue funds in Texas. I agree with you it's a problem, infrastructure is a problem.

VICE CHAIRMAN OWEN: Thank you.

MR. MARTIN: Hopeful that these assertions were true and somewhat buoyed by the STB's retention of jurisdiction for a five year oversight period, we did not persist in our efforts to oppose the merger following its approval.

But then the summer of 1997 arrived. We discovered that the promises that we had relied on and that had given us some hope, turned out to be empty. Rather than positive merger effects, we saw instead

the unfolding of an economic nightmare for the state of Texas. Rather than realizing tremendous service improvements, we saw nothing but the infliction of great damage to the financial well being of hundreds of Texas companies and many other citizens in our state.

Although other parts of the country experienced hardships as well, there is no doubt that Texas and the Houston area in particular was hit the hardest. Dr. Bernard Weinstein, who conducted the study of economic impact, a study of the economic impact of the rail crisis on Texas at our request, and which is a part of the record in this proceeding, estimated that Texas business experienced losses in excess of more than half a billion dollars.

While UP has been critical of these estimates, neither they nor anyone else has made any effort to quantify the financial misery inflicted on the state of Texas.

Whatever deficiencies the study may have, what is unmistakably clear is that the countless citizens of Texas have been hurt by the UP/SP merger.

Overwhelmed by shipper complaints as the rail crisis began, we took other steps in an effort to assess the impact of the crisis, and if possible to identify its causes. Traveling to a half dozen or more cities around the state to hear from affected businesses and others, it wasn't unusual to hear affected shippers talk about among other problems, a lack of shipping alternatives.

Responding to these concerns, to this Board's request that solutions be offered, and our own deep convictions that the long-term interests of the state of Texas are best served by effective rail competition that provides meaningful service options for Texas shippers, we set about to develop a proposal that would restore all rail competition in the Houston Gulf Coast area.

Experiencing a temporary setback when this Board rejected the Railroad Commission's earlier proposal because of, among other things, a lack of evidence, we persisted in our efforts to develop a plan that would benefit the state. The Consensus Plan is that plan.

Although it is not as extensive as our earlier proposal, it has the critical advantage of being supported by those who are most affected by these concerns, and who have suffered the most, shippers.

The Commission believes that a decision by the Board to expand neutral switching and then to allow Tex-Mex to have its own line between Houston and Beaumont and permanent unrestricted access to customers on the port terminal railroad and HB&T for traffic moving between Houston and points north and east, will help to ensure that shippers in the Houston Gulf Coast area have meaningful shipping alternatives and will never again have to experience a rail crisis like the one they so painfully experienced in the past 18 months.

In closing, I would like to point out that the Consensus Plan will not do anything to jeopardize the efficiency of UP's operation in the Houston Gulf Coast area, nor will it deprive UP of any properties that are needed for continued implementation of the UP/SP merger.

Booth Yard is an inconsequential facility for UP in comparison to yards such as Ingelwood, Sedagast, and Strang. But it will have a vital impact to Tex-Mex.

The construction of a second main track between Houston and Beaumont on the jointly owned UP BNSF line will more than compensate UP for transfer of the old Missouri Pacific line to Tex-Mex, because a double track line, a one right of way, has more capacity and is easier to maintain than paired single lines that are miles apart.

The Commission believes the long-term interests of the state are best served by effective rail competition that provides meaningful service options for shippers. The Commission urges you to act favorably on the Consensus proposal, to protect the Texas economy and the well-being of our citizens by restoring lost rail competition in this most industrialized region of our great state.

Thank you for your consideration.

CHAIRPERSON MORGAN: Thank you.

Do you have any other questions?

VICE CHAIRMAN OWEN: I support your concern about the great state of Texas and the Houston area also. But with reference to the Port Terminal Railroad Association there and the Consensus Plan, you advocate that they take over the responsibility of UP and BNSF services. There is no place in there for the funding of the acquisition of those facilities or as to where they hope to get the funding for say locomotives or crews or anything along that line, I don't believe.

So in your Consensus Plan, we go back to the dollars again, as to how do you propose to do something of this nature. You propose that PTRA duplicate those services.

MR. MARTIN: Well, Vice Chairman Owen, it would not be our position that they would be duplicative of the currently existing services.

VICE CHAIRMAN OWEN: But to replace them rather.

MR. MARTIN: It would be a replacement.

VICE CHAIRMAN OWEN: That's what I mean.

MR. MARTIN: Union Pacific and the

Burlington Northern Santa Fe, along with the Port of Houston have an arrangement now that addresses the switching of freight cars in that general area. Ours is a conceptual issue. I think that we believe that the Tex-Mex and the Burlington Northern Santa Fe and the Union Pacific and the Port would come up with a plan that would support all the switching that is necessary.

VICE CHAIRMAN OWEN: Didn't the Port back out of a financial contribution to some type of an association? If I remember correctly, reading it there.

MR. MARTIN: I believe at one time they --

VICE CHAIRMAN OWEN: And they no longer financially contribute to it? And yet they want to be a decision making -- they want to cast a vote?

MR. MARTIN: They are a member of it. They do own the right of way that the tracks run on. So I don't think that they are there with empty pockets.

VICE CHAIRMAN OWEN: Long Beach and Los Angeles Ports, and I wasn't really part of that to

that extent, I voted on it and went down and looked at the Alameda corridor there, saw how the railroads participated along with the ports in solving a problem, that they came up with a pretty hefty solution there. I know it's considerably different, but it seems like that over this period of time, that the Railroad Commission being an active player in the Port of Houston, seeing the industry grow as it has, would have developed a Consensus Plan that would have brought in the major players such as BNSF and UP and KCS and Tex-Mex, at some previous time rather than waiting until now and then trying to piecemeal the situation.

Because I see it being very fragmented with some of the different proposals that are before us today. I don't see any tradeoff. Are we opening up Beaumont and Baton Rouge and New Orleans to UP if they lose customers in this particular area here? Are we going to open up, as the Chairman said earlier, open access to Oregon and Washington, where BNSF seems to have had a little bit of a problem up there lately with $100 access charges? Or not access charges, but

charges and above unit cost according to the cost in California.

I could ramble on about some of these things, but you know, I think a lot of the railroads have problems in other areas. They probably need to address some of those before you really get too over-reaching in some of these aspects. I still think you could come up with a good consensus plan that would include the active participation of the UP people and the BNSF people there, and the KCS and Tex-Mex, to solve it, without coming back before a regulatory body.

But the state of Texas and the Port really needs to be a financial player in this. Otherwise -- I really believe that.

MR. MARTIN: I appreciate your comment. There's lots to respond to. Very briefly, the Railroad Commission of Texas has offered to meet with Burlington Northern Santa Fe, has met with them, has met with Union Pacific, Tex-Mex, KCS, anybody that wants to meet and discuss how to make things better for our shipping industry in Texas.

As far as the other points, Beaumont, you will recall that the Railroad Commission did in its original merger filing with this Board advocate neutral switching areas in other parts of Texas. I think it might be a little out of our purview to speak about other points of the country, but I can almost assure you the Railroad Commission will support you if you want to open up other great industrialized areas in this country to something that benefits the people that use the services. That's the shippers.

CHAIRPERSON MORGAN: Let me just follow up with that. I think we all agree that infrastructure improvements are important. The debate seems to be how we get there. Is that a good summary of what's in the record?

MR. MARTIN: Certainly infrastructure is very important.

CHAIRPERSON MORGAN: So we all agree that we need to get to a place in Houston and elsewhere where the infrastructure is improved as necessary to respond to the needs of the community, in this case obviously Houston.

MR. MARTIN: I certainly agree that infrastructure is a very important element, yes.

CHAIRPERSON MORGAN: And I think the other follow-up question based on the Vice Chairman's question, is that in order for us to adopt a particular proposal, added condition, if you will, in the context of this proceeding, we would have to find, as I mentioned earlier, that it's specifically tailored to the harm that we're trying to address.

If it isn't, then it becomes essentially over-reaching, in which case then we're talking about possibly a taking or the need to look at exchange of property. Do you agree with that?

MR. MARTIN: Well I certainly understand your concern about over-reaching. I would believe, I'm not an attorney, but it's my belief that this Board has substantial power. You kept a five-year oversight period to look at this. Certainly you can impose, you know, whatever conditions that you deem are appropriate in the public interest.

So yes, we agree, as I mentioned to the Vice Chairman, that in our state we are addressing and

we intend to ask the legislature to address some of these infrastructure issues, but I would simply point to the fact that where there is competition, where there is an opportunity to make money, people will invest.

For our purposes, we believe the more the merrier. We want more competitors searching for that transportation service dollar.

CHAIRPERSON MORGAN: Okay. Thank you all very much.

Next we will hear from Richard Weicher, representing the Burlington Northern and Santa Fe Railway Company.

MR. WEICHER: Good morning, Chairman Morgan and Vice Chairman Owen. My name is Richard Weicher from the Burlington Northern and Santa Fe Railway Company. Thank you for the opportunity to appear.

Burlington Northern and Santa Fe's proposals are far more modest and we believe appropriate to this oversight proceeding than the Consensus Plan proposals we have just heard described.

With respect to the more controversial of our proposals, that for trackage rights of the Union Pacific to Laredo, we would like to ask that the Board defer action on that portion of our application because we are guardedly hopeful that we may yet reach a negotiated private sector solution to the issues involved in that part of our application.

Thus, we would ask if it could be held in abeyance for up to 30 days, by which time we would report back to the Board on the status.

CHAIRPERSON MORGAN: I don't have to ask that question then. Thank you.

MR. WEICHER: We believe the Board has broad authority to address the issues we have raised in oversight, and that our requests are fine tuning of the original conditions specifically tailored to address operating issues that affect competitiveness, not radical restructuring such as the Consensus Plan, to ensure that we play the intended role of a competitor to the two-to-one and new access points to which we did receive access in the original settlement agreements and the Board's decision.

They do not involve access to any new or additional shippers or industries or facilities. They are designed to address congestion issues and avoid future Houston and South Texas congestion problems and conflicts. We are here because of last year's unprecedented service crisis. Our proposals address those kinds of issues.

Union Pacific characterizes what we ask for as opportunistic. We disagree. We did not plan for the service crisis or for the major changes in Union Pacific operations we have all seen. We want to plan that it does not happen again.

When Burlington Northern and Santa Fe negotiated for the rights it received, it was based on what we knew and what we could foresee of operations and the outcomes of implementation of the Union Pacific's merger operating plans. We did not foresee nor as Union Pacific has said, did it foresee some of the operating effects to come. Union Pacific's operating plan filed with the STB did not predict how operations would have to change from its original plans in order to work effectively.

CHAIRPERSON MORGAN: Let me stop you right there so I make sure I understand. Some of your proposals then relate to future changes that will be made in the operations on the UP system and how that interacts with --

MR. WEICHER: Yes. They do. Our proposal for a condition that would require Union Pacific to provide us the opportunity to join future directional flows when they are implemented in the Gulf Coast region in areas that affect rights involved in the merger settlements in case do ask for future relief so that -- or not future relief, but a condition that requires Union Pacific to give us the opportunity to go with the flow and adapt to changes that may yet occur as it seeks efficiencies.

CHAIRPERSON MORGAN: So it's not so much what's happening right this minute on a particular line, but rather what you anticipate will happen and how you would want to be incorporated into those changes? I'm just trying to make sure I --

MR. WEICHER: That condition is directed at the forthcoming changes. Our request to continue

to have permanent bidirectional rights to operate on the lines from Caldwell to Flatonia to Placido and Caldwell to Flatonia and San Antonio, asked us to similarly be protected from the effects if Union Pacific changes the directional operations its doing there now.

Our broader condition asks that we stay in the flow. The principle there, if we look at the Dallas-Wachahatchie-Fort Worth triangle, where Union Pacific has proposed to implement northbound directional operations or said they may implement northbound operations from Wachahatchie to Dallas at some point in the future, would have us going against the flow with coal trains to a TU Electric, Houston Lighting and Power, and fighting upstream.

This is the kind of thing that had emerged in the Houston-Memphis issue in the original merger case the Board and shippers found unacceptable.

We now see that this is something Union Pacific may want to do. They have every right to do this, to use the lines that they acquired on their merger to become more efficient.

What we don't think should happen is that they should be able to denigrate service where we have rights in a way that denigrates our service on those lines.

CHAIRPERSON MORGAN: Thank you.

MR. WEICHER: Pre-merger Southern Pacific was not in the position where it would have had to repurchase or bargain with Union Pacific for competitive service because UP could affect operations on its lines. We have now created some integrated lines and integrated network issues in South Texas and the Gulf Coast particularly.

What we are asking for would preserve operating and routes found to be very useful in alleviating the service crisis between Caldwell, Flatonia and Placido, and Caldwell, Flatonia and San Antonio. Those routes helped get traffic out of Houston and reduced the congestion and make things work better.

Similarly, that we would be able to limit the impact on our service of future UP changes such as going directionally in new areas or new corridors. We

think shippers and Burlington Northern Santa Fe are entitled to a stable planning environment for investment, for service plans, for service commitments, to know where we'll be and how we adapt to it.

Our concern is that BNSF's ability to be an effective competitor in the Texas area to the merged Union Pacific Southern Pacific, for the shippers to whom we gained access, has become unreasonably dependent on UP's present and future operating decisions.

With respect to our specific requests, as I mentioned, our requests to have permanent bidirectional rights on the routes to Caldwell, Flatonia and San Antonio, and Caldwell, Flatonia and Placido, when directional operations may cease at some time in the future, for example, on the line to Placido, gives us a stable long-term environment on a route that works and keeps traffic out of Houston.

We are not asking for new access. No new shippers would be served by any of these. The Algoya route was a major problem. The route south out of

Houston, Algoya to Corpus Christi was a major point of congestion. Union Pacific says there will be a siding here of some investments that will make it better.

We think we learned from the experience of the service crisis that there is a better way, and it doesn't change the competitive balance. To the extent it makes us able to offer long-term more reliable competitive service, we think that's what was intended by the original merger decisions and agreements, not an unfair or imbalanced change in the playing field.

CHAIRPERSON MORGAN: Let me stop you right there, because in terms of all of your proposals, one that I wanted to make sure we address was the request for a clear path through Houston. Let me just ask you a question about that. Then you can elaborate as you wish.

Isn't that something, that concept something that could be handled through the Spring Center? Do we need to do more there at the Spring Center to make that happen? Talk to me about that.

MR. WEICHER: We definitely think it should be handled through the Spring Center. What we

are talking about is having all the routes in and out of Houston controlled. They are right now controlled by the Spring Center, but the Spring Center does not have the -- the dispatchers in the Spring Center do not have the authority to permit operation by Burlington Northern Santa Fe or Tex-Mex over certain of the routes in and out of Houston over which they do not presently have rights.

We believe, and in this area we share the view of the Consensus Plan as we understand it, not as to changing the access for carriers to serve industries on those routes, but that the dispatcher in the Spring Center controlling traffic through Houston should be able to use any of the trackage for any of the carriers in Houston to get traffic and cars through the terminal, in and out or by or if something is more congested on this side versus the line that we're particularly interested in, from Rosenberg up across the middle of the Houston terminal, but any of the lines that are there.

If there's a line open, the dispatcher should have the authority to permit passage over that

line, even if today the carrier doesn't have trackage rights to operate on the line.

CHAIRPERSON MORGAN: So what I hear you saying then is that to address your request for a clear path through Houston, additional authority at the Spring Center is your suggestion for getting at that issue?

MR. WEICHER: We believe the Spring Center would control it. I guess it's technically additional authority for the carrier who would run over in most cases the Union Pacific trackage where they don't have rights, the legal right to run over that under standard trackage right terms, so that the Spring Center dispatcher could say oh, we can get this train through town going this way. He can then let that happen and permit that railroad, be it Tex-Mex or BNSF to use that route to get through. Not to do things there, not to serve shippers there, but to get through and out of town or into town.

Our proposal for rights between Taylor and Milano, Texas, does also take trains and traffic out of Houston, replicates a former SP route for the same

traffic, and gets us off of Union Pacific sooner and has us on a route that we believe is better able to handle the traffic than other congested routes.

Our proposal for a neutral switching supervision within the Houston -- for Houston shippers is another extension of the Spring Center concept. It would promote efficiency and fairness, as we believe the Spring Center has done for over the road line haul operation and making economical use of existing terminal infrastructure, the structure that is there now, to be used effectively.

What we're talking about there is having the same kind of neutral, better informed control of switching such as on the Baytown Branch, where many shippers don't want to be served by two carriers. If we had true neutral supervision, we would obviate the issues of accusations and fairness and unfairness in the switching operation, and most of all bring the prospect of greater efficiency to how switching is done.

CHAIRPERSON MORGAN: Let me stop you there again because this follows up on my prior question.

You do address the concerns in the record and here again about switching and dispatching and some of the events that have occurred that have concerned you. Now again, to what extent can those issues be addressed through the Spring Center concept, with additional authority or with whatever you are suggesting?

MR. WEICHER: We think the Spring Center concept is the concept that should be applied. It's not quite the same for some of the switching supervision. For example, in the Baytown Branch, that individual switching is not presently controlled through the Spring Center structure, because it's not the over-the-road dispatching. But the same kind of neutral entity with participation by whoever has the right to switch the industry would control who does the switching, or in some cases a neutral party could be used.

But it would be -- for example, the Baytown Branch could continue to be switched by Union Pacific crews in situations where only one party was going to switch on behalf of both. But through a

similar in a given case as perhaps more locally controlled or closer to the actual switching, neutral coordinated supervision.

CHAIRPERSON MORGAN: But obviously the switching is directed by the dispatching. In other words, dispatchers direct when switching and how switching and priority and so forth. Am I right?

MR. WEICHER: That's right. In some cases switching, depending upon the individual line and the industry, is more closely controlled by whoever is controlling the local train on a given piece of line, ultimately coordinated by the Spring Center.

CHAIRPERSON MORGAN: On some of these issues that you have raised, have you been in discussion of these with respect to the Spring Center or other protocols that might be in place as a general matter? I'm not necessarily referring to the Baytown issues specifically, but just in general.

MR. WEICHER: Yes. We have.

CHAIRPERSON MORGAN: You have listed several areas where you had concerns.

MR. WEICHER: We have had dialogue with

other carriers and Union Pacific on many of these issues, on all these issues.

CHAIRPERSON MORGAN: With good progress?

MR. WEICHER: With mixed progress. We were glad that one of our original proposals that is no longer before the Board was to include additional lines into the coverage of the Spring Center, the line to Shreveport. There were two lines. We had some dialogue. We put that in our plan. Union Pacific has said great, and that's going forward.

So I would not want to say it's totally fruitless. No, we have made real progress.

On the issue that was raised earlier, Chairman Morgan, about our future, the condition for us to be able to join future directional rights, we think this is important and it fits with the overall issue of us being able to plan and us being protected from adverse effects of Union Pacific changes.

When Union Pacific went directional in South Texas on the Algoya line, they virtually told us to join. Now they say at some point we may be back on the Algoya line, in other words, not going southbound

on the line to Placido and northbound on the Algoya line. They same some improvements will be made.

We think that the tool that was used in the service order was effective, but we also think that whenever these sort of situations come up, we should not be at the mercy of UP. This shouldn't be a game of gotcha over what was in the original merger decision. Now they want to change something which they have every right to do, but they can by doing that denigrate our service on one of the lines affected by the merger rights.

CHAIRPERSON MORGAN: Just one question if you're finished with that sentence. Now you're not part of the Consensus Plan?

MR. WEICHER: We are not. There are a couple elements, such as the aspects of more neutral supervision of switching and the clear path proposal that I believe we share in common.

We don't oppose Tex-Mex's proposal to have permanent rights on the Algoya line, because it's similar to ours to keep the South Texas structure that was basically improved or that lessened the congestion

at Houston in tact.

We do oppose the access aspects of the Consensus Plan strongly, either with respect to neutral switching with open access at Houston or the general open access for industries at Houston. We do not agree with the characterization of the Consensus Plan of our competitive effect at two-to-one points. As our quarterly reports show, we believe we are steadily gaining in traffic at those points. We are focusing on competitive service issues that really start back in the service order crisis of last year.

CHAIRPERSON MORGAN: So then what I hear you saying is you as the competitor to UP, as part of the approval by the Board of the UP/SP merger, you are dealing with some of the service issues that you have concerns about, but as a competitor, you feel good?

MR. WEICHER: I would not want to say we are satisfied. I would not want to say we have gone as far as we should go. We are and intend to continue an extremely vigorous competitor, constantly going after all the traffic we have. We think we have established a major presence at the two-to-one points.

Are we where we want to be? Certainly not.

CHAIRPERSON MORGAN: Competition is working.

MR. WEICHER: Are we where we hoped to be? Certainly not.

We believe competition is working. We don't want to see a service reoccurrence, the service problem reoccurrence, not just because of what it's done to our industry and what it did to our company and what it did to -- and the tremendous impact on the shippers. We don't want to see those kinds of issues come back and affect our competitive service capabilities in the short-term or the long-term.

We think many of the tools that were utilized by the Board in the service, to deal with the service crisis through the service order, these elements in our plan should stay in place because they are good, concrete operating-driven improvements. Not changing competitive access.

VICE CHAIRMAN OWEN: I thought maybe I might jump in here. I would kind of like to go back to the neutral dispatching there and with reference to

your comments there that the dispatcher should be able to direct trains over any line that is open. I think that's what you said.

MR. WEICHER: Yes.

VICE CHAIRMAN OWEN: So that in some way might be construed as open access, or would that be limited access with no solicitation of shippers on that?

MR. WEICHER: It would be strictly overhead access, as we call it, limited access. We are not talking about the right to serve shippers, industries, or utilize yards. We are talking about the right to get a train through town, as it were, on its way in and out of wherever the party already had the right to go, but get it in and out of the terminal, to keep it as fluid as possible.

VICE CHAIRMAN OWEN: Now I'm not quite clear as to why Tex-Mex and KCS aren't participating in the neutral dispatching here or why there seems to be portrayed some type of favoritism in dispatching. Can you elaborate upon that a little bit?

MR. WEICHER: I don't know the answer to

that. I visited the Spring Center. I have seen the cubical for the Tex-Mex where they have the right to be. We wish they would become more active in it because it brings the opportunity for greater efficiencies, and the flow of information by having these people together. We believe the Spring Center has worked, has worked well to promote efficiency and fairness.

Does that mean we'll never claim something didn't go wrong? Of course not. But we believe it works. We believe the concept of better information through having people there provides more efficient service. And in many cases, diffuses the issues of when you think you are being treated unfairly.

VICE CHAIRMAN OWEN: I would think they would want to participate. I know the leadership of both the railroads, and they don't appear to be shy and wallflowers. In that sense, I think they would express their concerns.

One of the other things that you mentioned as neutral switching are switching and some favoritism there. Reading through the material, it indicates

that the cars are commingled or intermingled, whatever, and that your cars seem to be getting to your yard faster than they get to UP's yard in this one particular case.

Now I am just saying, you know, we read these reports and one says one thing and one says the other. So I'm just countering that.

MR. WEICHER: I think, and I'll briefly comment. I think the data is unclear. There are different effects such as on the Baytown Branch, our cars are brought to a different place than Union Pacific's cars and have additional infirmities or additional steps that have to go through that don't necessarily mean our net service is as equivalent from our standpoint.

But one of the reasons we are proposing the expansion of concepts like the neutral switching supervision is to extend the Spring Center concept we discussed earlier to make the information flow better, and lessen the issues of alleged discrimination or unfairness through a better process.

VICE CHAIRMAN OWEN: You indicated earlier

in your remarks also that you had no desire to pick up additional shippers or were not trying to do that. I didn't say no desire, that was an input on my part.

From the Clinton Branch, if PTRA takes over the grain train, wouldn't it also pick up the port traffic there which UP has just invested a little over $4 million --

MR. WEICHER: Actually we withdrew our proposal for altering the sense of the Clinton Branch, but our proposal never included any new access to any shipper on the Clinton Branch, including that facility. We are not advocating that.

One of the reasons we think we have been competitively effective in South Texas and in Houston has been the impact of the service order rights for routing and opportunities in South Texas that the Board approved last year. We think they worked. That's one of the things that's helped us.

VICE CHAIRMAN OWEN: In the Baytown yard there, isn't that the real problem there is capacity and not really neutral switching?

MR. WEICHER: It's not -- there are

capacity constraints there. Those capacity constraints are one of the reasons why we advocate the neutral switching. We are putting money in. We are adding tracks up near the Showrinder facility for our storage.

One of the reasons we advocate the ability to go with the flow on when you UP has directional operations such as they do coming up from the south to the north on the Baytown Branch is so that if we do switch ourselves shippers on the line like that, we don't have to go against the flow.

There are capacity issues. We are prepared to make the investments on lines where we have the right rights and can fully utilize those investments to address capacity issues.

VICE CHAIRMAN OWEN: And on the Taylor Milano line there, to add bidirectional Vienna South, wouldn't that create a problem there, delay and congestion on that?

MR. WEICHER: No. We don't believe so. The Taylor to Milano route, first of all, it gets us off UP faster. From an operating standpoint, we

believe it's a better route, better control. It has less congestion than the more southerly route we go today.

Also, the traffic that we would put over that route, essentially this aggregate traffic coming off the Georgetown Railroad, is a lower priority in the dispatching protocols than the manifest or intermodal traffic that UP may have over it. It would clearly go at the bottom or below all those, and would never be -- should not be permitted to be a cause of delay of that kind of traffic. Again, it keeps us out of Houston.

VICE CHAIRMAN OWEN: Weren't there a couple of areas that BN could contribute some money to assist in laying some other tracks or doing some other things there that they should be a party to in assisting in the effort down there?

MR. WEICHER: We are always looking at those issues and those opportunities. We again will have an over $2 billion capital budget.

One of the reasons we want to know we will have or we are asking for the permanent bidirectional

trackage rights on for example, the line from Flatonia to Placido, the line by which we get to the Tex-Mex and we get to Corpus Christi, is so that we know whether we should be investing in that line or we know whether we'll be there if operational directi... cease.

We put in 75,000 feet of tracks at the Dayton facility on the Baytown Branch for storage of our cars. We are planning more. We are always open to those opportunities.

These proposals are directed to make us more predictable and make our operations more predictable and stable so we can better judge the return on those investments and we'll be able to fully utilize them.

VICE CHAIRMAN OWEN: And the 17 mile buildout that UP did on the old KATY line there, did that help any at all on the Caldwell Flatonia?

MR. WEICHER: The Caldwell Flatonia line is operating better, yes.

CHAIRPERSON MORGAN: Can I just follow up?

VICE CHAIRMAN OWEN: No more.

CHAIRPERSON MORGAN: Because when you were asking questions, something triggered. Because I think, I want to make sure I understand this.

Does the director at the Spring Center have the authority to resolve dispatching disputes?

MR. WEICHER: Yes. There is a process --

CHAIRPERSON MORGAN: So that is the neutrality --

MR. WEICHER: Yes.

CHAIRPERSON MORGAN: Concept that is embodied in the directorship at Spring Center. Do I understand that right?

MR. WEICHER: That's right. Some of the dispatchers -- there is a difference between the truly -- some dispatchers, there are coordinated lines and there are lines that are dispatched by the dispatchers for each company under the joint. They are all under the joint supervision of a process to reconcile disputes and disagreements.

CHAIRPERSON MORGAN: I just want to make sure I understood that.

VICE CHAIRMAN OWEN: Revenues were up

considerably for Vienna South and down for UP. In as much as you are asking for some additional perks here or something off the Christmas tree, what are you willing to trade to UP in exchange for that so that their revenue enhancement will grow, that they can continue to invest in the infrastructure?

MR. WEICHER: We believe Union Pacific is coming back. We are ready to trade in areas where it's appropriate to trade. We don't think we should have to trade to be where we were supposed to be in the first place under the original Board's decisions and the settlement agreements to be the effective competitors on where we are.

We are willing to participate in capital investments on lines we share where it makes sense and where we know we have the stability to use them properly.

If I could make one last comment on our Brownsville request, the request we have at Brownsville is pretty straight forward. We want to be able to have the right to go down the Southern Pacific line and go on the bypass to the Port of Brownsville

that keeps us out of downtown Brownsville.

We were heartened by what we saw yesterday in the summary of argument that Union Pacific put in, where it appears they are prepared, and we had some exchange of letters, and people have talked, and there may be confusion, but we think that if we are going to be out of downtown Brownsville and have the rights to use the improvements that have been paid for by government money, that if they had been put in before, that Southern Pacific would have had the right to utilize. That's basically what we are asking for. If that's where Union Pacific is, that issue may go away.

We still think there are good reasons for us. We also continue with our request to be able to use the BRGI in the Brownsville Railroad as an agent to avoid further congestion. But we are there also guardedly hopeful that maybe the Brownsville thing will work out.

But our goal is to stay out of the city streets of Brownsville and be in the kind of position SP would have been to be able to use these kinds of tracks.

CHAIRPERSON MORGAN: Well you have answered another of my questions.

MR. WEICHER: Okay. We think our proposals are modest adjustments tailored to deal with service issues that we have seen very concretely within the last year and a half that the Board's tools helped us address. They don't change the competitive landscape and give us new access. To the extent they keep our service competitive, we think that's what was intended in the original merger decision and should remain in place.

Shippers have told us that they don't want to see this happen again. These are plans to ensure that they don't, and that keep us in the competitive position we believe we were intended to be in. Thank you.

CHAIRPERSON MORGAN: Thank you.

VICE CHAIRMAN OWEN: One last comment, a question before you go. In all of this combing and intermingling down there with KCS, Tex-Mex, UP and so forth, how's labor treated and the implementing agreements. Is there any problem in all of these

agreements going back and forth or anything like this that you envision?

MR. WEICHER: No. We are not -- none of our proposals are intended or should disturb the labor balance. One of the things, when we talk about, for example, the neutral switching supervision, we are talking about how things are run. We are not talking about any wholesale or any unnegotiated or any push through changes in how any of the work is done. We are talking about, shall we say, the process and the system.

But no, I am not aware that we have had problems in that area or issues in that area.

VICE CHAIRMAN OWEN: I saw that seniority was preserved on the respective railroads, and so I was just wondering.

MR. WEICHER: We have tried to deal with those issues up front and in a straight forward manner.

VICE CHAIRMAN OWEN: Thank you very much.

MR. WEICHER: Thank you.

CHAIRPERSON MORGAN: Thank you.

I think what I would like to do is to get a couple of people up and then a couple of other people up. Let's start with Albert Krachman, representing Capital Metropolitan Transportation Authority, Kenneth Cotton, representing Houston and Gulf Coast Railroad, and Donald Avery, representing Central Power and Light Company.

Kenneth Cotton, we want you to join up here. Then we'll hear from the three of you and then move to the next three after that.

Mr. Krachman, did I get that?

MR. KRACHMAN: Yes you did. Yes, thank you, Chairman Morgan.

Good morning, Chairman Morgan, Vice Chairman Owen. My name is Al Krachman. I represent Capital Metropolitan Transportation Authority, transit authority for the city of Austin. We are here on Capital Metro's request for limited conditions seeking 4.4 miles of trackage rights for BNSF to come down from Round Rock to McNeil, Texas, as well as interchange rights for BNSF at McNeil.

Chairman, the city of Austin has

approximately one million people in its metropolitan area. It is regarded as one of the fastest growing sectors of the state and in the country. However, there's only one shortline railroad that provides any shipper service in Austin. That is the Longhorn Railway, LHRR.

The Board's decision on the limited condition that's sought by CMT here is effectively the decision on whether to preserve or extinguish shortline service in the Austin metropolitan area. The reason is, as outlined in our briefs, that Longhorn simply can not survive without this requested interchange and Capital Metro being obligated under the common carrier obligation, has no resources by which under these circumstances it could possibly find a replacement carrier.

So we truly are in an exigent circumstances here. We request this special relief, which we believe is authorized in this proceeding and by the oversight authority of the Board.

CHAIRPERSON MORGAN: May I just stop you? Because as I am listening to you, I want to make sure

I have the facts correct here.

MR. KRACHMAN: Certainly.

CHAIRPERSON MORGAN: This is how I understand it. Tell me if I'm wrong. UP now serves McNeil. Is that right?

MR. KRACHMAN: That is correct.

CHAIRPERSON MORGAN: SP used to serve Giddens.

MR. KRACHMAN: That is correct.

CHAIRPERSON MORGAN: You were given access to BNSF to replace SP, and you were given an interchange at Elgin because that is where -- you didn't want Giddens, you wanted Elgin. Is that right? Have I got it right so far?

MR. KRACHMAN: In 44, the Board gave the option to choose Elgin or Giddens at that time. That's correct.

CHAIRPERSON MORGAN: But now you are concerned that things haven't worked out quite well enough or well, so you are seeking an interchange with BNSF at Elgin?

MR. KRACHMAN: At McNeil.

CHAIRPERSON MORGAN: I mean at McNeil. Excuse me.

MR. KRACHMAN: What happened, Your Honor, and exactly you are correct. As a result of the Houston meltdown that we have had so much testimony on, Longhorn has been put in an untenable situation. As a result of the congestion in the Houston area, the financial effects on Longhorn have weakened it to the point where it is unable to survive without this.

So what at the time looked like a viable alternative at Elgin, it looked like a reasonable choice, no one anticipated the meltdown. No one anticipated the effects on Longhorn. No one anticipated that BNSF wouldn't be able to live up to the condition or live up to the representation in its operating plan that it was going to be able to run through trains.

So as a result of all those conditions, you had a convergence of circumstances that so significantly weakened Longhorn, that it's essentially on the verge of financial ruin and inviability.

So what we have come back to the Board

for, which is exactly what the Board asked us to do in decision number 12, which is come in and say have the conditions that we imposed last time been effective. Because of the change in circumstances that's happened since those conditions were imposed, we are here requesting this alternate relief. We are here because the conditions due to a variety of circumstances, including the meltdown, did not -- destroyed the viability of Longhorn and put it in the position where it must have that limited interchange at McNeil.

Again, all we are looking for is 4.4 miles of trackage rights from Round Rock to McNeil. We ask for that so that Longhorn will survive, so that Longhorn will have a chance to take the western shippers off the Austin line, out up through that segment and get it out to market. It will additionally help alleviate the Houston congestion.

So yes, the scenario is exactly correct. What happened is that the conditions imposed last time were not sufficient to save Longhorn because those conditions ended up depending on through traffic for BNSF at Elgin, which didn't happen because of the

Houston area congestion. So it's essentially a chain reaction.

CHAIRPERSON MORGAN: I think I understand. I think you presented your case.

MR. KRACHMAN: Okay. So the ultimate issue, Your Honor, is whether the public -- may I continue? Whether the public interest in maintaining shortline shipper services in Austin, in affecting the Board order condition, and in alleviating Houston area congestion outweighs the claim by UP that it would be inconvenienced by having to schedule 4.4 miles of new trackage rights for BNSF.

We don't believe the question is close, Your Honor. We believe that the applicable legal standard here, which is argued in our brief and not opposed by UP, is a public interest test. And that if a public interest test is applied here, and specifically we have cited the public interest test under the terminal facilities provision at 49 USC 11102, which says that the Board is to apply a public interest test in deciding whether to grant a rail carrier a condition that would allow it to use the

track and the facilities of another rail carrier.

Under that analysis, the test is satisfied if the Board finds that its practicable and in the public interest to grant the condition without substantially impairing the ability of the rail carrier to use its own facilities.

We submit here that this test is clearly met. This test is met on several planes. First of all, it's in the overwhelming public interest to allow shortline service to survive in Austin. There's captive shippers. There's many circumstances in which without this rail service, there would be significant traffic on the Houston highways and the Austin highways. It would clearly be a significant harm to lose short-term shipper service in Austin.

Second of all, Your Honor, this condition will affect the Board-ordered competition in decision 44. To allow this condition to occur, you will save Longhorn. You'll give the substitute, you'll give the remedy that the Board has already determined should be granted to CMTA, because it did find that there is a two-to-one situation.

So therefore, by granting this limited condition, the Board will be affecting its condition that it imposed on decision 44. Also, as outlined in our briefing, Your Honor, the effect of this condition will be to help to alleviate Houston area congestion because the traffic will be able to get north and into Houston through a northbound route, specifically through Taylor at Caldwell. So there are specific public interest considerations that would warrant granting this limited condition.

Now UP claims that there might be --

CHAIRPERSON MORGAN: Could you wrap it up? I think I understand. We've got a lot of people here today that we need to hear from.

MR. KRACHMAN: Certainly.

CHAIRPERSON MORGAN: I want to get to the rebuttal.

MR. KRACHMAN: I certainly will. In summary, Your Honor, I'll just cite one last point. Senator Hutchinson wrote a letter on September 10, 1998, to the Board, indicating that it's important that rail traffic be preserved, that the flow of

traffic continue in our area. We believe that if the Board grants this limited condition, it will give affect to that charge.

So we ask, Your Honor, that the Board grant this limited condition, extend the 4.4 miles of trackage rights for BNSF and the interchange. Thank you.

CHAIRPERSON MORGAN: Thank you.

VICE CHAIRMAN OWEN: Just a moment, if I could, Mr. Krachman, please.

You indicated BN could not perform. Could you respond, could not perform in what way there if the original designation there at Elgin that you had chosen in the merger?

MR. KRACHMAN: What happened, Vice Chairman, was that the BNSF operating plan that was relied upon at the time the original application was sought, had through trains going from Elgin to Smithville. Instead, because of the Houston area congestion, those through trains did not operate. What happened is all BNSF could do was run shuttle service back up and down to Taylor, only maybe two

times a week.

So the volume that was intended to flow through Elgin at the time that condition was chosen never materialized because of the Houston area meltdown and the condition south of Austin.

VICE CHAIRMAN OWEN: The other point is that you'll be switching there on a main line, will you not?

MR. KRACHMAN: There will be an interchange at that main line. However, there's a side track sufficient for 90 cars. So there is no conceivable problem with an interchange there because there's more than ample side track to handle the switching necessary. UP handles many more complicated interchanges here. I think it is significant that the side track is so extensive and would permit easy coordination.

VICE CHAIRMAN OWEN: Thank you.

MR. KRACHMAN: Thank you.

CHAIRPERSON MORGAN: Mr. Cotton?

MR. COTTON: Good morning, Chairman Morgan, Vice Chairman Owen. My name is Kenneth

Cotton. I am owner and operator of the Houston and Gulf Coast Railroad.

Would it please the Board, I would like to show you a very short, about two and a half minute video tape, that will probably explain my case a heck of a lot better than I could. Perhaps you would have a little bit better understanding of what the use of the Gulf Coast Railroad does, and what we're trying to do to provide some competition in the Houston area, and on the service crisis.

Thank you for your attention. We'll be able to do some questions and whatever as soon as this is done.

VIDEO NARRATION: Over the years, the nation's major railroads have mostly abandoned hundreds of miles of track in Texas and in small towns -- the train has a new owner, as Charles Hadlock tells us in tonight's Assignment Texas.

To me it's a lot of fun. It's also a way of life for Kenneth Cotton. Both his grandfathers worked for the railroad. So did his uncles and cousins. "I loved it when I was a kid growing up. I

told everybody when I grew up I was going to be a locomotive engineer."

Kenneth Cotton not only went to work for the railroad, he and some partners bought one. He owns 13 miles of track in Wharton County, a line that was abandoned by the Santa Fe Railroad years ago. "Every now and then, people don't like to stop." He has one employee, the conductor, who makes sure the train stays on the right track.

"One thing, small railroads like this, we're real good on customer service." Kenneth Cotton is not only the train engineer, "my office, so to speak," he is the president, chief executive officer, salesman, bookkeeper, and brakeman. "I have never gotten tired of it, never gotten sick of it. I never wanted to walk off and never come back."

But there was a time when he thought it wasn't possible. The train hauls corn and wheat and milo from the grain silos in Wharton, past the farms and cotton fields to the end of his track at Cain Junction. The big railroads will carry the cars on from here to their final destinations.

"I mean you get to see the fruit of your labor when you're all done at the end of the day. You get to see what you did."

Kenneth Cotton has visions of expanding his railroad empire beyond its 13 miles. Today Wharton County, tomorrow the world.

Charles Hadlock, 11 News, on Assignment Texas. Something tells me that's not a 9 to 5 job. No. A little engine who could. Go for it.

MR. COTTON: At the time of this taping in 1996, Houston and Gulf Coast Railroad was in the middle of handling more cars that had ever been moved out of Wharton County by a railroad in at least 15 years.

In 1995, in six months of operation, I know this may not seem like a lot, we handled 232 cars. In 1996, like I said while this was going on, we had handled about 650 cars. In 1997, when the Gulf Coast rail crisis imploded upon us, and the ability to provide service to our customers worsened, our earnings and revenues plunged to 97 cars.

The H&GC vainly sought to work with the

Union Pacific for offering storage and car switching services to help alleviate the rail crisis. At the time, the Union Pacific was contracting with every shortline within 150 mile radius to provide storage service and switching services. I should say every railroad, but the Houston and Gulf Coast. We made every possible opportunity to work with the Union Pacific, but to no avail.

In 1998, the service crisis finished dealing a crushing blow to the H&GC. Revenues which at once were very, very promising are now almost non-existent due to the gridlock with Union Pacific. We have only moved this year a total of 50 cars.

The H&GC has petitioned the Board for two things. One, to give H&GC trackage rights on the Union Pacific between various points to access directly BNSF connection and to provide neutral storage sites for plastic shippers in the Houston and Gulf Coast area.

Two, we also request that the Union Pacific sell us its trackage between Congress Yard in Houston, Texas, to Galves Yard in Galveston, Texas,

along with the former Southern Pacific routes in Galveston County, Texas.

The Houston and Gulf Coast Railroad will provide a neutral rail service between these two communities and to the shippers in the Houston and Gulf Coast area. We would also provide two neutral storage facilities for plastic traffic in the Wharton and Gulf Coast area. One in Galveston County for customers near Houston, and also for customers in Wharton County near the Angleton, Bay City and that area.

At the current time, Union Pacific pretty much has a stranglehold on traffic as far as storage traffic is concerned and storage space. They hold about 84 percent of all current available spaces for storage.

A neutral storage facility would seem to be needed by a company, for a plastic company if it would seem that they would want the option to move their plastics via another railroad. Union Pacific has pretty much got that sewed up. BNSF has very, very little storage room in the Houston and Gulf Coast

area.

Generally what I am proposing is essentially to work with the railroad. But you may have to force them to do that for some reason. But it's to make it so that everyone will have an opportunity in that area to pick whatever railroad they wanted to use.

As a shortline operator, that's what I do best. What these guys do best is to couple up 110 cars of coal and move between Wyoming and Texas. They can do that very well. But when it comes to switching cars and when you are storing cars and doing that sort of thing, that's not the sort of thing that Union Pacific and the BNSF do well at all. That's not what is in their purview.

I would also like to say that there are 550 shortline railroads in the United States of America. At this point in time, there are only two who are owned or controlled by African Americans. I happen to be one of them. Neither one of the railroads here have ever sold a shortline railroad to an African American, neither do they have anyone of a

vice president, CEO, or anyone of that ilk has ever been in a management position on a railroad.

So you see my problems and you see my circumstances. Working with these guys is something that's very easy for Tex-Mex to do, for KCS to do, for Union Pacific, they all work well together. But when it comes to working with me I've had nothing but stonewalling, difficulties and attitudes which would seem to be at a point where they just wish --

VICE CHAIRMAN OWEN: In other words, you're saying you can't get a return telephone call or any cooperation of that nature, Mr. Cotton, and --

MR. COTTON: I'm sorry. I'd like to apologize.

CHAIRPERSON MORGAN: That's all right. Do you want to sit down for a minute? We can move on and come back to you if you'd like.

MR. COTTON: No, I'm okay.

Frankly, if I don't get the conditions I'm asking for, I'm out of business totally. My employees, which depended so much on me, I've already had to furlough. No one in this room will lose

anything.

What I'm asking for is less than one-half of 1% of the traffic that the Union Pacific handles right now. That will keep my people alive and that will keep my business alive. Plus, it will provide the service that this community needs.

I'm not asking for a lot. I'm not asking to be given a break. I'm just asking to be given a chance for my business and my company to survive. This is my last chance. I've spent my entire adult life in this business, and I knew that the road would be tough for me.

But if I wanted to be an engineer, a very good engineer, for any one of these railroads, I could have done that very easily, and I could have done that for the next 40 years without a problem. I'm very, very good at what I do.

And during these proceedings, there were certain allegations that were made by the railroads involved that I didn't have the wherewithal to do what I do, which is one of the reasons why I brought that up to you.

CHAIRPERSON MORGAN: Could I ask you a question relative to what you've been talking about, if that would be --

MR. COTTON: Go ahead, go ahead. I'll be okay. I'll be fine.

CHAIRPERSON MORGAN: You indicate you've had conversations with the Union Pacific regarding your issues particularly during the service emergency.

MR. COTTON: Oh, yeah; oh, yeah.

CHAIRPERSON MORGAN: And what was the nature of those discussions in terms of what you were --

MR. COTTON: When I --

CHAIRPERSON MORGAN: -- seeking from them?

MR. COTTON: When I had talked with the Union Pacific on several occasions, I explained to them what I wanted to do, and they pretty much expressed an interest of practically nil. Even though, like I said, --

CHAIRPERSON MORGAN: And what you want to do is represented in your conditions or was it just general --

MR. COTTON: All of that.

CHAIRPERSON MORGAN: -- trying to address the service --

MR. COTTON: All of that.

CHAIRPERSON MORGAN: -- issues that you had?

MR. COTTON: I mean, you know, I wanted trackage rights over a railroad that practically they don't ever offer service over. I mean, they've got an intact, you know, railroad between Wharton and Rosenberg that they don't even use.

And there's really no impediment to me using it. I mean, it's connected to my end of the railroad in Wharton. It's connected there in Rosenberg to either the Union Pacific or the BNSF. It would make it -- you know, performing the duties would have been just a matter of, you know, doing the work.

And I couldn't get them to do that even though a lot of the local people were saying, you know, we're drowning here, we're dying here. And every time I would try to make, you know, an offer to the Union Pacific to do anything, I got nowhere,

nowhere at all.

Even though, you know, like I said, they've used everybody -- used everybody but me. They're switching cars for Houston in Georgetown, Texas. You know, I'm 35 miles away just south of -- near Rosenberg.

You know, I didn't do -- I didn't want to do -- I didn't want to switch the cars for Union Pacific just to be -- just because I needed the revenue, even though I did, but because I also realize the bigger picture.

And the bigger picture is this: If customers can't rely on the railroads to do what they need them to do, then there's always Joe Blow Trucking Company who may cost a little bit more, but he doesn't have to worry about what's going to happen.

I mean, when my shippers call me, I can tell them where their cars are and when they're going to get there, and also I can tell them when they're not going to get there and why.

And my shippers have been very patient with me, but they've also had to understood this --

that they're in a business, too. And if I can't get them cars in a timely manner, what are they supposed to do?

It cost them more money, but they also -- they have commitments that they have to keep.

CHAIRPERSON MORGAN: Well, I think we certainly understand your position here today, and we appreciate your coming and explaining your situation to us and sharing with us the video. I think you've made your case and I certainly understand where you're coming from, and we appreciate your being with us today.

MR. COTTON: I'd just like to thank you and thank God that I had the chance to at least be able to express what I had to express to you. I may never be in this position again, and all I can is, is that I'm a railroader. And I'm the best one around.

And that's what I'm talented and that's what I'm able to do. Whether it's running a 110 car coal train or sitting in the office doing what needs to be done, there's nothing on a railroad that I haven't done or I'm not capable of doing, and I just

want to be recognized for that.

VICE CHAIRMAN OWEN: We recognize you. Thank you very much for taking the time and the money to have come here. I know it's a hardship. Thank you very much.

MR. COTTON: Thank you.

CHAIRPERSON MORGAN: Mr. Avery.

MR. AVERY: Good morning, Chairman Morgan and Vice Chairman Owens.

My name is Don Avery, and I appear here on behalf of Central Power & Light Company of Corpus Christi, Texas.

CP&L got into this case last summer because UP, which is the only carrier serving its plant at Coletto Creek, Texas, for almost a year had been unable to deliver the coal that CP&L needed.

There's really no dispute about that starting point. Where we diverge is later on and what to do about it, what caused that and so forth. What we asked for is a remedy. It was pretty straightforward.

We asked that BNSF, which is already

operating into Victoria 16 miles away, and, of course, has asked that those rights be made permanent, be allowed to come out 16 more miles to our plant at Coletto Creek, which is on the SP Wharton Branch, to deliver a portion of our coal requirements.

That's the portion that comes from the Powder River Basin. This plant cannot burn pure Powder River Basin coal. UP is the only carrier serving the sources of the rest of our high value coal -- high caloric value coal, and thus will always have part of our traffic no matter what happens.

Now UP objected to our request on several bases. The first and foremost, I suppose, is the one that's their answer to everyone right now, and that's that "the crisis is over." Hey, service is back to normal. There's no need for any remedy based on the crisis. That time has passed.

Well, from CP&L's perspective, yes, the service has improved. We'd be the first to admit that. We congratulate and commend UP for the efforts -- the Herculean efforts they've put into restoring their service, including their service to Central

Power & Light.

Our service is much better than it was at the nadir last year, last spring, last summer. And indeed, we commend them for the work they did to get our service restored when it was disrupted for several weeks by the flooding down there.

They got that line back in service. As I say, we give them enormous credit for that and we appreciate it.

But the service isn't back to normal, if by normal you mean what we had before the merger. It's better, but it's not there. UP is trying hard, but they're not there. More ominously, from our standpoint, they don't seem to be confident they'll ever get back there to where we were before the merger.

In our rebuttal evidence filed October 16th, our witnesses, the management witnesses, stated without equivocation that if UP could offer Central Power & Light the quality of service commitments that it had in years past, even with multiple carriers interchanging to get the coal there, we'd withdraw

from this case.

This is a service case, pure and simple, from our standpoint.

CHAIRPERSON MORGAN: And let me just make sure I understand. You have been served by UP over the course here of time, and you have a contract with UP?

MR. AVERY: No, ma'am; no contract. There have been contracts in the past.

CHAIRPERSON MORGAN: But you have been singularly served by UP over time?

MR. AVERY: UP is the only carrier serving our plant. They're also the only carrier serving the origins of part of our coal. That's the high value coal, the Colorado coal.

Now, the fact that I stand here today is -- reflects the fact that UP, try as they might, have been unable to make the commitments that we think were rather reasonable to request, and that is a commitment to the service -- the cycle times that we had before.

UP, of course, also contends that, whatever our service problems were -- and as I say,

they don't really deny that we were having poor service -- they weren't caused by the merger and so they shouldn't be addressed in a merger related oversight proceeding.

Well, we don't contend that their service crisis as a whole was the product of the merger. That's for others to argue about. What we do contend is that it was exacerbated -- its impact on us was exacerbated by the merger.

As we explained in our opening evidence, and we had an expert testify to this -- before the merger, if UP had become unable to operate our trains reliably and effectively, we were captive to the SP at destinations, but we could have switched to BN as the origin carrier.

The SP would have had no reason to block that. Get the trains to the interchange faster. They would have gotten more traffic and more revenue. It would have been in their interest to go along with us. UP would have opposed it, presumably, had they been our carrier; but they would have been powerless to prevent it.

But UP contends that that's disputed -- you know, that's been proven by experience during the crisis. They say BN turned down their request to take over a lot of their coal traffic.

Well, the short answer to that is that BN didn't turn down their request to take our traffic because that request wasn't made. To the contrary, BN offered to take over our service on an interim basis, just for 1998, to help them out of their crisis and that offer was turned down.

That's why we're here today. And I'd be happy to answer any questions.

CHAIRPERSON MORGAN: But you are looking, as I understand it, for more permanent access to a second carrier. Is that what your request is really all about? I'm just trying to make sure I understand.

MR. AVERY: As long as they can't commit to provide the service that we have a right to expect, I submit, what alternative do we have? For part of our service -- this is supplemental. It's not a replacement.

CHAIRPERSON MORGAN: Thank you very much.

MR. AVERY: Thank you.

CHAIRPERSON MORGAN: Now we'll go to Nicholas DiMichael representing Dow Chemical, Ralph Whitfield representing DuPont, and Andrew Goldstein representing Formosa Plastics.

MR. DiMICHAEL: Chairman Morgan, Vice Chairman Owen, my name is Nicholas DiMichael. I'm here representing the Dow Chemical Company.

Dow has a chemical facility in Freeport, Texas. It's solely served by the UP. It's one of the largest, if not the largest, chemical complexes of its kind in the world. Over 20,000 cars a year originate at Dow's facility.

In my time before you today, I have just really three brief points to make, and I hope to be done before my allotted time so I will have some quick questions -- time for any questions.

First of all, the Board, in Decision No. 1 in this proceeding, asked the parties to address whether there was "any relationship between the market power gained by UP-SP through the merger and the failure of service that has occurred in the Houston

Gulf Coast."

The answer, Dow believes, to that question is yes. Because so much of the rail facilities in the Houston Gulf Coast area are controlled by one carrier after the merger, there was no safety valve in the form of independently operated infrastructure when UP service deteriorated last year.

The BNSF, which was the competitive alternative to UP in terms of rates, was not able to act as a safety valve for service because it also was using the very traffic -- it also was using the very track that the UP had and over which service was so congested.

And if there was a safety valve in the form of independently operated infrastructure, the crisis, we believe, would have been less severe in both duration and in scope. We believe that, because of the lack of a safety valve, the area remains vulnerable to future service crises.

As the Board has found -- the second point, the Board has found the key to the issues in Houston and the Gulf Coast area is infrastructure,

additional rail infrastructure. And the UP itself has said this.

In its oral argument summary, it said that the "service crisis in Houston was a Houston-wide capacity crisis." And Chairman Morgan, before I believe you even mentioned that certainly infrastructure improvements are crucial.

And Dow agrees with that and is prepared to do something about the lack of capacity in the Houston area. And this brings me to my third and last point. If the Board would Dow -- would grant Dow's requested conditions, mainly BNSF access to, via haulage rights, Dow's Freeport facility, Dow and BNSF will construct a new storage and gathering yard near Angleton, Texas.

Angleton is a point that UP itself has described as a primary choke point in its Brownsville subdivision. And you heard Mr. Weicher just before state that, during the service crisis, the Algoa route -- that's exactly the point -- was a major problem.

And the yard that Dow is proposing that it construct, partially with its own money, would be

located on the Algoa route. So, as you can see from Dow's filing, Dow and BNSF have entered into a formal Memo of Understanding that commits each of them to put up money to construct the yard which will cost, as I understand it, upwards of $20 million dollars if the Board grants Dow's requested additions.

Dow does not want something for nothing. It is prepared to put money on the table to invest in additional infrastructure at a precise point at which infrastructure is so needed. The yard could be used not only by Dow, but by other shippers in the Angleton, Freeport, Chocolate Bayou area.

The new yard would contribute measurably to investment and infrastructure in a critical space -- at a critical point in the UP system, and would enable traffic in the area to utilize just 23 miles of UP system before it got into the Houston mall.

Thus, Dow agrees with the Board that infrastructure is the key not only to the severity of the past service crisis, but also to the prevention of future service crises as well. Dow is willing to invest millions in infrastructure that can be used not

only by it, but by other shippers in the area.

And the Board can thus address, we believe, some of the underlying causes of the service crisis by granting Dow's requested conditions.

I thank you.

CHAIRPERSON MORGAN: So, let me just back up a second. Dow is a one to one shipper right now?

MR. DiMICHAEL: It is.

CHAIRPERSON MORGAN: It is seeking access to BN-Santa Fe?

MR. DiMICHAEL: And in exchange for that, Dow is prepared to invest in the infrastructure that is needed to make that -- not only that competition work, but to make the broader system work.

CHAIRPERSON MORGAN: Now, in terms of -- and I think you've validly raised a good issue, which is infrastructure. Now, in terms of the impact of this type of access on the infrastructure that UP might be investing in in that service area, how do you feel about that?

MR. DiMICHAEL: Well, this would obviously obviate the need for UP to invest its own money in the

infrastructure in that point. UP could obviously do that if it still wished, and that would be great.

But there is going to be -- there is a tremendous infrastructure needs in and around the Houston area, and Dow is willing to commit some of its own money to assisting in that. And that would mean less if UP believed -- if the UP believed it not necessary, it would be less that UP had to invest on that point.

CHAIRPERSON MORGAN: So you -- it may be that UP would decide not to invest in the infrastructure there?

MR. DiMICHAEL: The infrastructure needs are certainly great enough that there should be many people brought into this mix.

Vice Chairman Owen, you asked me for where would the money come from. Dow is saying it's willing to put up some of the money for the infrastructure needs. Now, if UP decides it doesn't need to, that is more then for UP to invest in other places still in the same -- for the same need.

If the needs are great enough, and they

certainly are, then there should be a spreading of the infrastructure burden. And Dow is willing to do that. And BNSF and Dow have entered into this Memo of Understanding to build this yard.

CHAIRPERSON MORGAN: So let's say we did what you're suggesting here, and then we did it elsewhere in the country, which some proponents have indicated is the way we should go.

What does that do to infrastructure overall throughout the country? I mean, obviously we're changing the incentives here for investment, which, of course, is something that all of us need to be concerned about.

So, while it may work in your particular area one way or the other, if we do it one place, then, if it's done another place and another place and another place, then what's the overall impact of that on infrastructure throughout the country?

MR. DiMICHAEL: I think -- well, those broader questions are certainly outside the scope of this particular proceeding, --

CHAIRPERSON MORGAN: Although I think some

have brought those issues --

MR. DiMICHAEL: Yes.

CHAIRPERSON MORGAN: -- into this proceeding --

MR. DiMICHAEL: But I think -- I was going to say --

CHAIRPERSON MORGAN: -- in a broader way.

MR. DiMICHAEL: -- that I think you're asking a very valid policy question. And really, in a sense, what we're asking the Board to do in this is to elicit a positive policy response by all participants in the rail system.

Here, for example, you would have an opportunity to elicit more money from a shipper who is willing to put it up if you grant these particular access rights. If you don't, there is no incentive for that particular shipper to invest his own money.

CHAIRPERSON MORGAN: But a key element is the shipper investment, as I hear it.

MR. DiMICHAEL: Absolutely, absolutely. And I think in terms of the broader policy applications, that is probably important elsewhere to

have as many investment vehicles, investment sources be available as possible.

CHAIRPERSON MORGAN: But there are probably shippers that might not be able to invest the way Dow is able to invest, I would presume.

MR. DiMICHAEL: I suspect that is true. But, on the other hand, shippers as a whole, you would think -- now again, I'm talking very broadly here and so we're talking in kind of hypotheticals. But shippers obviously with less resources than Dow might still be able to make investments appropriate to their own particular circumstance.

CHAIRPERSON MORGAN: But there is uncertainty there is what I'm saying.

MR. DiMICHAEL: Absolutely.

CHAIRPERSON MORGAN: We're talking about your situation and then --

MR. DiMICHAEL: Yes.

CHAIRPERSON MORGAN: -- what it means elsewhere.

MR. DiMICHAEL: That's right.

CHAIRPERSON MORGAN: Thank you.

MR. DiMICHAEL: Thank you.

VICE CHAIRMAN OWEN: So then a financially affluent shipper might gain greater benefits than some financially marginal shipper --

MR. DiMICHAEL: Well, I would say --

VICE CHAIRMAN OWEN: -- in a build out situation which would gain greater competitive advantage there.

MR. DiMICHAEL: Well, I would think -- in this particular instance, Dow has said that the yard that it is building would not be used just for itself. It would be able to be used by other shippers in the area.

So that concern, although it might be a hypothetical concern for the future, is certainly not present here.

VICE CHAIRMAN OWEN: That would be very generous. Thank you.

MR. DiMICHAEL: Thank you.

CHAIRPERSON MORGAN: Thank you very much.

Mr. Whitfield. Glad to see you again. I think we sat one another -- next to one another in

Newark at lunch.

MR. WHITFIELD: Yes, ma'am. Kind of you to remember.

CHAIRPERSON MORGAN: Amazing what I can remember sometimes.

MR. WHITFIELD: Chairman Morgan, Vice Chairman Owen, DuPont appreciates the opportunity to appear before the Board this morning.

I'm Ralph Whitfield, manager of bulk logistics. In that position, I am responsible for DuPont's bulk chemical transportation, including rail. With me today is Frederick Wood, our outside counsel.

DuPont is a $45 billion dollar diversified chemical and energy company with over 200 manufacturing sites and almost 100,000 employees worldwide. Rail transportation is fundamental for DuPont's diverse global supply chains and is, for many of our products, the only safe and practical mode of transportation.

DuPont's La Porte plant at Spring, Texas produces agricultural products and other chemicals. It ships 3,000 rail cars each year, most of which

contain hazardous materials for which no other practical means of transportation exists.

The La Porte plant has long been opened to reciprocal switching for interstate shipment.

But in 1961, when the Port Terminal Railroad Association, the PTRA, was being established to serve other Houston customers, DuPont's La Porte plant was specifically denied, without our participation or consent, PTRA access and was restricted to exclusive switching by then the Southern Pacific, now the Union Pacific, even though PTRA operates over the same tracks directly in front of our plant.

I might add that DuPont does not enter into the proceedings lightly. In fact, has never before sought specific individual conditions in merger reviews, DuPont believes, in a competitive, privately owned and operated, market-based and financially sound transportation industry.

As such, private solutions are always preferable. We now resort to Board intervention only because other solutions have failed, thus threatening

competitive harm to DuPont and increased risk to the public.

We enter this proceeding with no malice towards UP, which, in fact, worked with us very diligently through 1997 and 1998 to resolve service problems and to develop alternatives to mitigate economic damage.

But the fact remains that, despite the best efforts of DuPont and the best efforts of UP, the existing system still does not work at La Porte. We do not request additional access; only effective access that does work.

Five major points support DuPont's petition. First, because the exclusive UP switching service did not work during the service disruption, DuPont was prevented from using alternative routes that should have been available.

For example, DuPont attempted to develop such alternatives with BNSF, as well as the Texas-Mexican Railroad, Tex-Mex, which has been granted additional Houston access under the Board's emergency service order.

These routings were continually stymied by the four or more days of circuitous UP travel required within Houston prior to the interchange, a fact that even UP acknowledges.

Second point. Numerous changes since 1961 have increased and concentrated more market power in the hands of UP. DuPont originally had access to six railroads. The UP-SP merger was the final stage in a series of railroad combinations that reduced this number to two and, for all practical purposes, effectively to one.

The merger decision itself granted access in Houston to the Tex-Mex for shipments with prior or subsequent moves to Mexico which should also be available to DuPont.

Tex-Mex was further granted additional access under the Emergency Service Order of 1997 to Houston customers open to switching on the HBT or PTRA, but inadvertently excluded DuPont, which is uniquely captive to UP switching.

Although UP did allow DuPont to work with Tex-Mex during the emergency period, they afterward

unilaterally revised the tariff to limit reciprocal switching to BNSF interstate only, thus permanently excluding any use of Tex-Mex for either Mexico or expanded future access.

Third, only a solution that provides neutral and efficient switching to DuPont by PTRA combined with Tex-Mex access as a third carrier to all Houston customers open to reciprocal switching, as ordered by the Board during the service crisis, can restore DuPont's premerger options.

Tex-Mex, in fact, was the only alternative railroad that seriously tried to work with DuPont during the crisis.

Fourth, this solution will not only protect DuPont's competitive position, but it is also vital to the public interest by ensuring that hazardous materials move quickly and safely through the Houston area.

Fifth, as also noted previously, DuPont's requested remedy is specific, limited, operationally feasible, and will not cause significant economic harm to UP.

In summary, DuPont respectfully petitions the Board for the remedies outlined in DuPont's brief and earlier filings.

Thank you very much.

CHAIRPERSON MORGAN: Well, I think the essence of your position is that you are looking for more competition for your plant in the Houston area.

MR. WHITFIELD: And effective alternative routings in case we have -- experience delays in using the existing routings that we have available to us.

CHAIRPERSON MORGAN: Thank you.

MR. WHITFIELD: Thank you.

Mr. Goldstein.

MR. GOLDSTEIN: Good morning, Chairman Morgan, Vice Chairman Owen.

I'm Andy Goldstein. I'm representing Formosa Plastics Corporation today.

Formosa Plastics has asked the Board for a very limited form of relief which is narrowly tailored to meet the harm which Formosa has suffered as a result of the UP-SP merger. We seek an alteration of the closed door BNSF trackage rights

that were approved in the merger so that BNSF can serve Formosa directly on its line.

Formosa is a plastics component manufacturer located about 140 miles west of Houston on the Algoa-Corpus Christi line which you've heard discussed here today.

BNSF has stated on the record that Formosa's request is feasible, will help UP address its own infrastructure problems, and that BNSF is willing to provide that service.

Although Formosa was served only by UP prior to the merger, the merger enabled UP to increase by 50% the extent of its premerger market power over Formosa's routings to western destinations, which is a reduction in competition by any measure.

With that reduction, competition -- excuse me. With that reduction in competition has come a clear, lasting and costly deterioration in service. We chronicled and graphed examples of these problems in Formosa's opening statement, especially to former SP points.

I see from UP's argument summary that was

circulated yesterday on page one that UP will assert today that the "problem area" of transit times to California was -- and again, I quote -- "solved in September."

I don't know how UP can make that claim, at least as to Formosa's traffic, unless UP measures current performance against its own worst post merger performance and not against premerger service. There have been some improvements in UP's service, but the record does not support the "solved in September" claims as to Formosa's traffic.

UP's opposition statement filed in mid September contains only a speculative prediction that transit times for California "should improve significantly." I can tell you that the California service problem has not been solved, at least for Formosa.

In September and October of this year, it was still taking nearly 30% longer to cycle a Formosa car to former SP points than it did when SP served these same points. Before the merger, Formosa was captive to UP for pricing purposes, as it still is.

What the merger did was increase Formosa's captivity to UP for service purposes. Board precedent, as we see it, does not require that we demonstrate a post merger expansion of anticompetitive behavior only through an exercise by UP of anticompetitive rate or pricing action.

Anticompetitive post merger behavior, we believe, can be and has been by us shown through service failures, and Formosa has demonstrated that over a two year period.

The answer to Formosa's dilemma is not that the Board has found that a service emergency no longer exists, which is what UP argues. It is a question of whether UP has restored Formosa's service to premerger levels. UP has had two years.

It now states that it has solved the problem of delayed cycle times on California traffic. The UP solution leaves Formosa 30% worse off than before at an immense cost in equipment utilization and customer satisfaction.

Allowing BNSF to serve Formosa directly meets the remaining elements necessary for merger

related relief. It's operationally feasible and it will produce public benefits.

Formosa proposes to construct a new turn out from the UP main line to Formosa's yard, and testimony detailing how this can be accomplished feasible is undisputed and unchallenged by UP.

Formosa will also construct several miles of marshalling tracks on its own property, at its own cost. This will enable not only BNSF to serve Formosa, but will enable UP to improve its service to all customers relying on the Algoa-Corpus Christi line by terminating its present practice of blocking the main line for up to two hours while it switches Formosa.

This will materially aid UP in resolving its infrastructure problems in the South Texas area.

In conclusion, Formosa's requests meet the Board's test for merger relief, we believe. There is something in it for everybody, and we hope the Board looks upon it with favor.

CHAIRPERSON MORGAN: So your position, Mr. Goldstein, is that the market power created by the

approval of the UP-SP merger resulted in harm that we need to address, is that --

MR. GOLDSTEIN: That's correct, that's correct.

CHAIRPERSON MORGAN: -- the quick statement of your position?

MR. GOLDSTEIN: That's right, that's right. And that we are willing to make the investment, as you've heard others say, in the infrastructure to make this work. And that will benefit everybody, not just us.

But it will free up UP or other carrier resources to help those shippers who may not be in a position to make the same investments very much like private cars. Some shippers furnish private cars, others don't. And the ones who don't then benefit to a greater extent from the carriers' own fleets.

And I look upon these investments that we're proposing as the same sort of benefit indirectly to the -- all of the carriers' customers.

Thank you.

CHAIRPERSON MORGAN: Thank you very much.

Next we will hear from Union Pacific Railroad. I think we'll have Mr. Roach come up and we'll deal with you, and then we'll go to Tex-Mex.

MR. ROACH: I'm joined by my partner, Mike Hemmer. Richard Davidson, Dick Davidson, the Chairman of UP, is present.

Madame Chairman and Commissioner Owen, if I can be permitted a brief personal note. The high point of my career was standing before you and hearing you vote in favor of this merger. And the low point for me and for all of my friends and colleagues at UP was being here for hearings about the service meltdown a year later.

Our service is back. We're extraordinarily proud of that. You don't really hear anyone contesting that today, with the limited exception of Mr. Goldstein, whom I will address in a moment. But I'm not going to take a lot of time reviewing the service situation.

We put that in submissions to you and I've given you some charts to look at that illustrate parts of what I want to say. But quickly, it's clear in the

Houston Gulf Area service is back to normal and has been for months.

There are no longer the jammed yards that we saw this spring and last fall. The yards are clear and fluid. Englewood is operating better than before the merger thanks to directional running, which was tough to put in place but was the answer to this problem, and was a merger benefit.

The car inventories are down where they should be. The terminal itself is running smoothly thanks to the Spring Center which we innovated at great expense. We had to open up a lot of shippers to BNSF to induce them to come into that dispatching center, and it is working.

And we're ready to do the same with Tex-Mex. And they can participate in the management of that center. They can make decisions with us about dispatching. There's a mechanism of the Joint Service Committee where they can get decisions reviewed.

They're not being asked to sit on the sidelines, as they keep saying. And they should have been in that center six months ago. They've sat on

the sidelines and not helped as we've overcome this crisis in Houston.

Transit times are back to normal. They're not perfect, but they're darn good; and they're, in many cases, better than they were before the merger.

I will match data with Mr. Goldstein on Formosa. Our California transit times fell very dramatically in September. I looked at the Formosa data yesterday. They are as good as or better than they were before the merger.

And we'll be glad to make a supplemental submission on that for you to look at.

CHAIRPERSON MORGAN: And let me, Mr. Roach, just stop you right there because I think the issue of service is critical here. And I have a couple of questions along these lines, so let me just go at it.

You know, clearly we've seen service problems in the west, and people are before us here today saying please adopt these proposals so that this does not happen again.

MR. ROACH: Right.

CHAIRPERSON MORGAN: Now, the Vice Chairman and I are here, and we want to make sure this never happens again. And we need to be assured of that. Now, help me to get there.

What can you tell me to make sure that this never happens again?

MR. ROACH: Well, first of all, I've learned the lessons of hubris, and I'm not going --

CHAIRPERSON MORGAN: So have I.

MR. ROACH: -- to promise anything about the future of this world because we've learned some hard lessons about what we thought we knew and what we didn't know.

But I'll tell you this. This is a resilient railroad. We've seen some tremendous weather crises strike the railroad in Texas and the Kansas City area over the last several months, and it has bounced back very quickly.

You heard the gentleman talk about the rebuilding of that branch to Central Power & Light. We did that in a week, and the engineers told us it would take three weeks. I mean, these people are out

there killing themselves to run this railroad better and better, and it is a resilient railroad.

Now, can I guarantee to you that if there is another surge of traffic or a natural disaster that there won't be some service problem? No, I can't. But I can tell you that we now have in place the TCS system so that the railroad runs as an integrated whole.

We have a decentralized management and operating structure that has been very effective. That's what pushed us over the hump on the California transit times was letting people run the railroad closer to the real action who could find the solutions to these problems.

And we have ahead of us most of the benefits of this merger: the shorter routes, the better service, the increasing efficiencies. Most of that is still in the future, and we don't know what's going to prevent us from pursuing that.

I think this whole industry has a capacity problem. I think you recognized that in your February order, and we tried to step up to that in our May 1

submission.

We exceeded our targets for spending in the Gulf Area this year, or will, by a little bit. We think we'll be at about $170 million.

We're trying out utmost to help to ensure there won't be another meltdown by overcoming the physical limitations that you heard about in our filing that have plagued SP for 20 years. SP had the same crisis and we were wrong not to understand how vulnerable they were.

If we had this transaction to do over again, we would have started in Texas, we would have started investing faster in more capacity, and that was a mistake. There's just no gain saying that it was a mistake.

We knew there was a need to make the most of those facilities. That's why directional running was the centerpiece of our operating plan. But we didn't understand how the whole fragile system down there in Texas could go under in a way that no one appreciated the disasters in the south, and how it would spread to the whole system, and how long it

would take to unwind.

These are fragile networks. It's striking, and no one understood that fully.

CHAIRPERSON MORGAN: And again, in terms of talking about how the service crisis occurred, why it occurred, I think the next step is to look at the argument related to the so-called strangle hold theory.

In other words, however we got to the service crisis, in order to make sure this does not happen again, we must respond to the problem of UP having a strangle hold in the Houston terminal.

MR. ROACH: Right.

CHAIRPERSON MORGAN: And that's the basis for the proposals that we have today. So how we got here, I think we'll be debating that probably for a long time. But what's before us today is the argument that, in order for this not to happen again, that we must do something about the strangle hold in Houston.

And the consensus plan, of course, is the response to that.

MR. ROACH: Right.

CHAIRPERSON MORGAN: Now, help us with that.

MR. ROACH: Well, I think that actually you answered that correctly in February when you ruled on the Railroad Commission of Texas proposal. And we've since, of course, put a lot more evidence in the record on this subject.

What you said then was, and it's true, that we had a Houston capacity crisis. We had SP particularly backing up disastrously because of a series of stresses that caused its yards to overflow and its main lines to overflow.

You could have, and you were asked to by Tex-Mex, produced a special clear route or super highway through Houston for Tex-Mex. You were asked to do that.

And the record showed, and the subsequent record reinforces this, that all that that would have accomplished is to let some Tex-Mex traffic get through this disaster and a lot of other traffic suffer even worse.

You can't solve a capacity problem by

helping some shippers at the expense of others. You held that in the de Bruce Grain case as regards to car supply, and you held it in the RCT ruling as regards to Houston.

What we need is to run the terminal more efficiently, and to have all the flexibility we possibly can, and to increase capacity. And the notion of a safety valve -- we were using all the safety valves that we possibly could.

We agreed to suspend all shipper contracts where that would help operation. We agreed to short haul ourselves, and we did repeatedly, including for some of the shippers you've heard from today who say otherwise.

We short hauled ourselves for those shippers over short junctions. And we have shown -- and this has never been disproven that the Tex Mex and KCS open access and PTRA plan would melt down this terminal tomorrow, twice as badly as it ever melted down in the last two years. They want to put all of the traffic into a few PTRA and other yards that are already filled to capacity with PTRA traffic.

It just wouldn't work. It wouldn't work for 24 hours. And they didn't offer any serious rebuttal to that. They are trying to design something that superficially talks about service but really is aimed at open access for their benefit. It's as simple as that.

CHAIRPERSON MORGAN: Well, let me just back up one second, which is that what you're saying is that the proposals that are before us wouldn't fix the problem of service, might aggravate the problem. Is that what I hear you saying?

MR. ROACH: Yes. I don't think any of the proposals that are before you would be beneficial, except the ones we have agreed to. We have agreed to changes in the Spring Center. We have agreed to sell the Horton branch to Tex Mex. If Tex Mex wants to invest money in infrastructure, more power to them.

But they shouldn't be investing money that they get by taking away our traffic where there was no competitive problem, and they shouldn't be arguing for access to traffic where there was no competitive problem on the theory that that will give them some

money they can invest. We need to invest. We need to invest.

We have a tremendous investment plan, $1.4 billion. They don't have a big investment plan. They have a plan to buy a rail line, to construct, and then in a very unfair swap take over a much more valuable rail line. And they've dressed that up as an investment, but it isn't an investment plan. The grant total of it is about a tenth of ours, and most of that is smoking mirrors, as I say, designed to self-aggrandize. These are harsh statements, but they're true statements.

CHAIRPERSON MORGAN: Well, let me ask you about infrastructure, because obviously another argument that's been made is that if you add competition to an area you will bring investment, that competition forces a carrier to invest more.

Now obviously, as I've said before, investment is something we're all interested -- infrastructure investment is something we're all interested in. There's disagreement as to how we get there. An argument has been made that the way we get

there is by adding competition.

MR. ROACH: More competitors. Yeah. It's a hard and an interesting issue because no one can deny -- and I don't deny -- that sometimes railroads invest heavily in competitive traffic. UP invested to enter the Powder River Basin. UP invested in intermodal traffic. We're not denying that.

But the issue is: everything else equal, what is going to maximize investment in this situation in the Gulf Coast, and, more generally, as a matter of theory. I don't think any of our opponents could seriously deny that if you opened up every closed shipper in this country to open access that would result in reducing rail rates very dramatically, and that would reduce the amount of investable funds available to the industry.

Yes, on occasion, railroads would invest some money to exploit those new traffic opportunities. But the overwhelming effect, the predominant effect, would be rate depression, revenue depression, and the elimination of this industry to cover its full cost and to invest for the future.

That's the whole story about differential pricing. We got into that in the bottleneck case. It's the issue on Capitol Hill or will be next year potentially. And I think that is the answer to your question. I think it's a slight of hand to say that there is this continual and infinite positive relationship between competition and investment.

There is occasionally a positive relationship. But the larger relationship in this industry, with its cost structure and its demand structure, is negative. You can't open up all of the closed industries. You can't take away the ability to price differentially. You can't deprive these railroads of their property without undermining their investment incentives.

Remember, railroads built where they built because of private capital market decisions. Where there are two railroads serving a shipper, it's because there was enough traffic to sustain that investment and make it pay for itself. Where there's one, it's because there wasn't.

What these folks want to do is force in

two where there's one force down the rate structure, and undermine the investment capabilities.

CHAIRPERSON MORGAN: So what I hear you saying at least is uncertainty. In other words, the impact of competition is uncertain as it relates to infrastructure.

MR. ROACH: Well, you've restated my point in very modest terms. I assert that the net effect is negative on investment -- of this kind of sweeping open access we're talking about in the proposals of KCS, Tex Mex, and the three or four very large shippers that want to open their facilities.

Now, take a shipper like Dow. You gave them the right to build out in the merger case. They then used that to secure a very attractive multi-year contract from UP. That's reported on in our annual submissions. All of the details are in there.

Now what they want to do is get direct access to another second railroad, just for a haulage fee. They want direct two-railroad service to bring the rates down even further. And they say, "Oh, if you do that, we'll invest $20 million. I don't want

to buy a $60 million rate reduction by promising the STB a $20 million yard investment."

If they really want to invest in a yard, we're ready to work with them. Let's build a yard. We'll put in some money. They can put in some money. We'll have more infrastructure. That's just, you know, bait and switch.

What they really want is to get their rates down or to get two-railroad competition where the merger didn't take away any competition. And you very carefully preserve the competition they had from potential buildouts, and they used it to get their rates down.

CHAIRPERSON MORGAN: Now, let me take that one step further -- infrastructure -- because clearly with respect to Houston the Port of Houston and the Houston Partnership are concerned about the economic development in the entire area and the role that the rail infrastructure in the Houston terminal play in that development.

So obviously, they're focused on infrastructure in the rail system as well as

elsewhere. Tell me about how you feel what UP is doing in the Houston terminal clearly advances their interest, which is the long-term economic development of that whole area.

MR. ROACH: Right. Well, you asked everyone interested in this matter to file on May 1 their proposals for infrastructure investment in the Gulf. Nobody else filed one except UP. There wasn't a BNSF plan even, and they have some investment plans and some incentive to invest, but they didn't even file a plan. Port didn't file any plan. City didn't file any plan. The Railroad Commission of Texas didn't file any plan.

They aren't proposing to invest their funds. They are proposing to take over UP's property without compensation, and then take the earnings from the traffic and pay for the service. That's really the gentleman's theory from the Railroad Commission of Texas. Where is the money? I don't know. I'll get it by taking over the traffic, and I'll have some money. But that doesn't yield net investment, and they haven't given you an investment plan.

Now, let me say, to invest we've got to have earnings, which is just making the same point I was making about the need to price differentially within limits of fairness. You've got rate regulations. We've got lots of competitive constraints on us. Dow pushed our rates down; Even though they don't have two-railroad service, they pushed them down. They've got ships and they've got buildouts.

But we've got to be able to price differentially to somebody or the investment money isn't going to be there. It's got to either come from the shipper/user of the railroad or from the taxpayer, or there isn't going to be investment. There are only those three choices.

CHAIRPERSON MORGAN: So you're saying that in terms of adding competition throughout the nation, starting here and perhaps going elsewhere, would have a serious impact on the infrastructure throughout the nation?

MR. ROACH: Yes. And --

CHAIRPERSON MORGAN: I mean, you're taking

it beyond Houston is what I'm saying.

MR. ROACH: I am. I am. And --

CHAIRPERSON MORGAN: I'm just trying to get your point here.

MR. ROACH: Yeah, absolutely. And to bring it back to the subject of this case --

CHAIRPERSON MORGAN: Right.

MR. ROACH: -- you framed a test for this case. The opening speakers all agreed with it. There has to be proof of competitive harm from the merger. There has to be proof that that reduction in competition caused the service prices, and there has to be a carefully tailored -- if you find those two things, there has to be a carefully tailored condition that will solve the problem.

Now, everybody who has spoken before me has totally defaulted on those tests. They all got up and said, "We're not claiming the merger reduced competition. We can't prove it." So I can skip the second third of my remarks which went through the two to one, the three to two, the one to one, the source competition, the vast evidence that the NSF is

competing for two to one traffic and pushing the rates down, as you point out, Chairman Morgan.

The 91 percent figure, I've got to tell you, is completely phony. Most of that 91 percent is LCRA traffic that isn't even open to BNSF until the contract expires. And as to much of the rest, you have sworn testimony from the Houston two to one shippers that the competition is vigorous.

Exxon, the biggest one, came in and swore they have entered into a new contract with us that is better than the contract before the merger. The confidential appendix shows right down the line for every one of those shippers -- I won't name them because they are highly confidential -- but it shows the names, the reductions in rates, the amount going by BNSF, the amount going by UP.

There is no dispute on this record about competitive impact. There's also no serious contention by any of these parties that some crazy scheme was mounted by UP to use market power to melt down its service. That would have been lunacy. No one seriously asserts it.

One of the world's leading antitrust authorities came in here and gave it the horse laugh it deserves. You don't lose a billion dollars and melt down your service to show how much market power you have. That isn't what happened, and no one contends it is what happened.

CHAIRPERSON MORGAN: But I think that they may be taking it one step further -- and, you know, help me on this -- is that once the service crisis occurred, the market power that was created did not help to relieve that service problem.

MR. ROACH: Well, you know --

CHAIRPERSON MORGAN: Therefore, we need to address that for the future. Is that the way you understand that second argument?

MR. ROACH: I hear the argument. I hear KCS say, "I didn't have to prove causation," although in their opening brief they claimed causation. But now, in their rebuttal, "I didn't have to prove causation. All I had to prove was some relationship." And the relationship is that if you hadn't controlled all of these routes, it would have been solved faster.

Well, I just explained to you a little while earlier, that isn't true. There wasn't some way to reshuffle the routes that would have solved the meltdown faster.

Secondly, we showed, through a very in-depth study that no one has said a word about, that only a third of the traffic in Houston is exclusive to UP. It isn't a market power issue. Only a third of that traffic is exclusive to us.

Now, why didn't it all immediately go to another carrier? A lot of it did. Eleven percentage points did, so the claim that it didn't change is false. But a lot of it didn't. Why didn't it? Because it was a capacity crisis. It wasn't a solution for a shipper to hand the traffic to any other railroad because all of the railroads were jammed up.

Now, it's true that BNSF has fewer routes through the city that it owns than UP does. But BNSF has rights over a lot of lines in the city, virtually all of them except the two they want additional rights over. Where they had previously agreed to trackage

rights agreements that restrict their rights, they'd like to get rid of those restrictions. Well, fine, let's sit down and do a trade, as you say, Commissioner Owen. They can lift some restrictions on us somewhere; we'll lift some on them.

Before the merger, neither UP nor SP had the right to run over every track in Houston, nor did BNSF, nor did anybody. Why should they now unless we agree on it? Let's agree on it. We're ready to talk. But they want you to force things that are one-sided.

I think maybe the most constructive thing I can do is talk about some of the specific conditions and answer any other questions you have as I go along. One of the Tex Mex conditions that was stressed was the Houston North rights, and I think I've commented on their theory that they should be given those or other rights simply to raise some money that they can spend on investment.

I think that's just, you know, moving things around under the walnut shells. That's not a theory that there was competitive harm from the merger that needs to be solved.

You have ruled literally three times against these Houston North rights. The reason that you gave Tex Mex any rights in Houston was not because of so-called three to two effects; they specifically disclaim that they are arguing three to two in this case. It was to make sure they had enough traffic to be viable.

Now, have they been viable? Well, let me use at least one of my little charts here. If you go to chart 11, you see their share of Laredo traffic is up from 12.8 percent to 23.6 percent since the merger. And you see their crossings on the next one are up dramatically in each of the two years after the merger. They've got a lot of traffic.

Now, he says, well, they're losing money. Well, their statement on their web page, which we cite in our oral argument summary, is that in 1997 they had an operating ratio of 94. I don't know where he gets this claim they're losing money.

They were losing money a little bit of the time during the service crisis, in significant part because they were running crazy, inefficient trains

north from Houston, 20 cars, to try to get a foothold in that market. And that has been stopped with the cessation of the service order.

But they -- as you pointed out, Chairman Morgan, they have themselves projected very positive earnings in future years. They are doing very well at Laredo. They've got this new alliance with KCS and CN, and so forth, that's being successful and attracting auto traffic. And they just haven't made any case for financial viability or for the need for arbitrary slices of traffic as a subsidy.

We also showed that those rights would be very disruptive in the terminal operationally. You see, people are supposed to be in this case finding solutions to service problems. But they're so eager for give-me's that they don't even pay attention to whether their solutions are going to complicate the terminal and make service worse.

As far as the Horton branch, which Mr. Allen focused on, I don't know why he focused on it; we're talking to them about selling it. We have agreed to arbitrate the price. We're talking about

some other details that he didn't raise today and that I don't think are going to hold the transaction up.

So they can buy the Horton branch. That's not something you need to order. You don't need to order any conditions unless you find A, B, C, harm to competition, causation, and careful tailoring, none of which have been proven for any of these conditions.

Now, as to the swap of the Beaumont line and the construction, I have commented on that a little. I would just also say that capacity in that corridor is sufficient with directional running. We don't need a third track in that corridor. It's all a pretext to get Tex Mex and KCS its own railroad.

If they want to invest, we listed a lot of places that really need investment in the Gulf Coast area. But they don't want to invest for the sake of the public interest. They want to take over a rail line at a subsidized price.

I would very strongly urge you not to defer ruling on BNSF's Laredo proposal. I think they are up against recognizing that they don't have a case, and they'd like to string out this leverage they

are trying to exercise with Tex Mex on divisions by holding this in abeyance. There is no basis for holding it in abeyance.

We've been held in abeyance for six months on a ruling here. They have made no case for adding a second single line route to Laredo. We have shown it would be operationally very harmful. That's a congested, difficult line where we're investing heavily to help make it run more smoothly. Adding multiple additional blocks to cross that international bridge every day would be terribly disruptive.

We've had a lot of trouble getting that to operate smoothly down there as it is, and the last thing we need is three railroads trying to move blocks through windows on that bridge every day.

CHAIRPERSON MORGAN: Well, my impression is there must be some sort of private sector discussions going on, which, of course, this Board never discourages.

MR. ROACH: Let them talk after you deny their request. And let them come back and reassert it if they don't reach agreement. Or let them come to

you, as they proposed as an alternative, and have you resolve the divisions dispute but deny the request for trackage rights because that is just totally unjustified and no case has been made for it.

CHAIRPERSON MORGAN: Are you in any of those discussions?

MR. ROACH: No. This issue of neutral switching supervision is a hard one to get your hands around. We never did get to the point of understanding what BNSF means by that. Mr. Weicher is correct that the Baytown branch switching operations are not dispatched out of the Spring Center. They are controlled by a yard limits person who moves that train up and down the little loop, around the loop.

What Mr. Weicher didn't tell you is that there there is a private sector solution going on. We've had a whole series of meetings with BNSF and with the shippers over finding ways to make that operation run better. It is capacity constrained. BNSF would like to serve some of the shippers directly.

The settlement agreement and the merger

conditions gave them the right unilaterally to decide if they wanted to serve a shipper directly or by reciprocal switching, or through an agent. It didn't give them haulage, which is what we have voluntarily given them. That's another theme I would love to expand upon but won't take the time with. We've done all kinds of things for BNSF that they never credit us with.

But I think there is a consensus emerging that the way to run that branch is through reciprocal switching rather than haulage, and for us to move the BNSF cars in reciprocal switching. And the shippers seem to like that idea, and we're moving toward that.

There is no discrimination issue. There is no fairness issue. There is no equal treatment issue. There just isn't. The data are not ambiguous, as Mr. Weicher says. They show that their cars are getting a fair shake, and it's impossible for them not to. As someone pointed out, they move in the same trains. And they're going essentially the same place.

Yeah, they are two different yards, but they're at the top of the branch. This notion of

discrimination is just a joke.

On the Taylor to Milano request, this is a good sort of case study of the whole BNSF approach here. The standard for conditions ought to be: are they needed to preserve the level of competition that existed before the merger? And BNSF sort of uses those words from time to time, but they don't apply the test.

They turn around and say, "Well, that's a little bit less congested line, and we'd love to use it. And it will keep cars out of Houston." That's bogus. That has nothing to do with Houston. They want to move aggregates cars to Beaumont and Silsbee and places not within 150 miles of Houston.

They already have rights from the Georgetown Railroad over SP's best route to Houston, and they're using it and competing like the devil to move aggregates into Houston. And the Georgetown Railroad has testified to that effect in the oversight proceedings.

What they'd like is to have another route that will get them to another place where SP didn't

compete before the merger. Only UP competed in the Silsbee area for aggregates movement. That's the other end market for that business, and they'd love to be in it. And they just dressed this up as something to do with service. It has nothing to do with service.

CHAIRPERSON MORGAN: Well, let me just stop you there, Mr. Roach, because I think there is sort of a general question that I want to ask relative to some of the proposals that the BNSF has made here. They are suggesting that these are proposals to address operational concerns, which, of course, is always of interest. And given that we're coming off a service situation in the west that was troublesome, operational efficiency is --

MR. ROACH: Right.

CHAIRPERSON MORGAN: -- a very appealing thing. Now, I presume that on some of these at least there are conversations going on with BNSF regarding operational issues that could occur in the future and how BNSF could continue to compete as we intend them to compete in respect to those changes. Could you

fill me in a little bit on where some of those issues and discussions might be?

MR. ROACH: Sure. We have had preliminary discussions with BNSF about the whole issues of directional running. We have said we'd like to return the lines up and down to Brownsville to bidirectional running, if we can. We need to add more capacity before we can do that.

But we'd like to do it because the Flatonia route is very circuitous, and the service that we can provide to all of these major chemical shippers on the Algoa line is not as good as it would be if we were operating that line bidirectional. So we'd like to get there. We'd like to get to bidirectional running.

But we're not going to do that unless we can do it without any adverse effect on service whatsoever. And I assure you of that. And you ask about conversations. I mean, that's what we're saying to BNSF.

Now, what do they want? We put them with your reinforcement and direction. We put them on the

route down from Caldwell to Flatonia to Placedo, and that's being operated directional.

Well, as with many of BNSF's requests, there are commercial dimensions to this. This gives them a much better route than the one they negotiated for in the merger. And it's better than they need to preserve free merger competition. And so they'd like to have it forever. That's no hard thing to figure out.

But they're not entitled to have it forever just because they'd like to have it forever is what I'm asserting to you. Yes, if it would solve a competitive problem, but they don't assert that and can't prove that. Maybe if it would solve a service problem.

We can have a philosophical discussion about whether that should be a merger condition or an 11123 or something else. But we're not going to ask them to get off that line if there is going to be any adverse service effect either. And I assure you of that, and that's what we're talking to them about.

The same issue with respect to the

Smithville line versus the Caldwell-San Antonio line. We're putting a lot of new capacity on the Austin sub and the Smithville line, and we're hoping to get them back onto that line, which is what they bargained for in the merger case and get them off the other very congested line that they're using and that they would like to use forever because it's a better route for them.

I mean, that's really what you're confronted with here. You've got to look at each one of these requests in terms of: is there a competitive rationale for it? And even is there a service crisis rationale for it? Because we're not proposing to make any changes that will jeopardize our service recovery.

CHAIRPERSON MORGAN: And I certainly hear you. I think that, you know, obviously we're struggling with legal criteria that we need to apply as well as these general public interest concerns that are before us --

MR. ROACH: Right.

CHAIRPERSON MORGAN: -- of which obviously service is one.

MR. ROACH: Can I say a word about Mr. Cotton and the Houston and Gulf Coast? I just want to say we had some problems with classification or sit on his railroad because we don't connect with his railroad, and it's difficult to get the cars there.

But I just want to say we're ready to talk further with Mr. Cotton and find positive win-win ways of doing business. We have a need for sit capacity. We're building sit capacity. Shippers have a need for sit capacity, and they ought to be interested in exploiting his property and his capabilities. So if he thought we were shutting the door to discussions, that wasn't the intent and that won't be the way we'll behave.

CHAIRPERSON MORGAN: Let me just move on to a couple of other things. Brownsville -- where do we stand on that?

MR. ROACH: Where we stand on that is that we sent a letter to BNSF and BRGI on September 5, I believe, that they've never answered. BNSF said they are studying it and they haven't answered it. We are ready, as we said in the letter -- and it's attached

to our filing -- to agree to what I think Mr. Weicher now says they are ready to agree to, which is to let them use the more direct route, appending the construction of the new bypass.

We cannot agree to a general agency role for BRGI, and I think I heard Mr. Weicher say they are not going to press that proposition. So I think we've got the makings of a deal there.

CHAIRPERSON MORGAN: Clear path through Houston, which was another thing that BNSF raised, and others have suggested. Now I sense you're opposed to that proposal. It seems to me that it would improve the function -- as a general matter, it would improve the functioning of the Houston terminal.

Again, I'm going to ask you the same question I asked earlier, and that is, couldn't this whole issue be handled through the Spring Center? Because obviously, the intention here overall is to bring efficiency, which I think was your word earlier, to the Houston terminal area.

MR. ROACH: Absolutely. Absolutely. Let me say, first of all, that nobody stood on ceremony in

terms of detours and use of available routes during the service crisis. But again, there is a commercial dimension to this issue. There are a couple of lines, only a couple, in the Houston terminal that BNSF doesn't have unrestricted rights to use. There's one line where they're limited to grain trains. There's another line where there's another limit.

They would like for commercial reasons to be able to use those lines. And they say it's just overhead, but, you know, overhead from here to there is what railroads do, and they want to deliver the traffic more efficiently to the end point.

We don't have the right to use every BNSF line in the terminal. They don't have the right to use every UP line in the terminal. Could we talk about that? Sure we could talk about that.

We tried to point in our filing -- in terms of every one of these requests, we tried to give specific examples of where there is something they might be able to give us that we could -- that would justify our giving them what they're asking for. And we could talk about this one.

I don't think they've made any showing -- certainly not any competitive showing -- about this because neither SP, as I say, nor UP had the right to use all of the lines in the terminal before the merger. So you can't say competitively the fact that neither of us do today is some kind of harm of the merger to competition.

Operationally, I think our position is we're doing fine in the terminal. There are enough routes for the dispatchers to use, and there is every willingness to open up other routes if there are any service problems that develop. And if we want to talk about permanent, new trackage rights, let's do it on a trade basis.

CHAIRPERSON MORGAN: But given how the -- as I think I had a conversation earlier with someone about how the Spring Center works, where you have a director that resolves disputes in a neutral way, if the notion is a clear path through Houston for any and all --

MR. ROACH: Right.

CHAIRPERSON MORGAN: -- the director of

the Spring Center would make a determination, if there was a dispute, as to what the clear path through Houston would be in a given circumstance. Is that -- I'm just hypothetically playing it out in the context of how the Spring Center works.

MR. ROACH: Sure. But again, I mean, I don't want to mislead you. As Mr. Weicher said -- and he's right -- what the Spring Center people can do is constrained by who has rights over what lines, which is very close to every one over every line but not quite. And that's the whole BNSF issue. They'd like the last couple. We'd like the last of theirs.

But fundamentally, the dispatchers can put the trains anywhere in the terminal that is most efficient. And there are, you know, subtle patterns. It isn't as if they just make ad hoc decisions every hour. There are subtle patterns about how this traffic flows, and the whole effort of directional running and yard specialization is aimed at coming up with subtle patterns that are more efficient and decongest the terminal, and we've succeeded at that.

But yes, you're right -- in the final

analysis, the people in charge of that dispatching center can use any available route where anybody has trackage rights over anyone else, which is most of the lines in the whole terminal, to get a train through the terminal.

But it isn't -- I guess what I'm trying to say is it isn't sort of like, you know, a motorist just picking randomly one day how to drive through a city. It's much more stable than that. The trains run in well-organized ways. And then if you have serious problems, you cope in creative ways. But you still don't just dispatch them randomly.

CHAIRPERSON MORGAN: Well, I think the point is that we're trying to get at this concept of neutrality and efficiency.

MR. ROACH: Oh, yeah.

CHAIRPERSON MORGAN: Which I think is the guts of a lot of what we're hearing, is how do we achieve those two things?

MR. ROACH: Right. And I don't think --

CHAIRPERSON MORGAN: In terms of future service.

MR. ROACH: Forgive me. I don't think anyone is contesting that the Spring Center has behaved neutrally and efficiently. I think Mr. Weicher said that. I think the Tex Mex folks have made no such allegation. They have been there a little bit. We don't know why they won't come and join us and put their lines and the KCS lines into that common dispatching center.

One of the biggest problems we still have is that UP has to move over the KCS between De Quincy, Louisiana, and Beaumont. And we have big problems getting across that line. And we're not claiming they discriminate. That's, you know, difficult territory to get in people's minds.

But the fact is they've had their sitings fill the lot, and they've had trouble getting our trains moving, and it would simply be vastly more efficient if they were sitting at the same table with their CRT next to our folks' CRT and the BNSF folks' CRT, and all making the dispatching decisions together.

It's when you have these so-called black

holes that you get inefficiency and you have to have these dispatching turnovers. And that, by the way, is what they want to create in Houston. They want to give the center of Houston to PTRA, have them dispatch somewhere else than the Spring Center, and that would just be a disaster.

We have neutrality inefficiency. And the way to finish it is for them to come into that center. There is no reason they shouldn't and can't except willful exploitation of this regulatory process.

They made discrimination allegations that were conclusively disproven with very expensive electronic measurements that we went out and did. And you know what? No rebuttal. They didn't look at the work papers. They didn't second guess the data. They didn't cross examine the witnesses. We had the brother of one of their witnesses who is the head of the Spring Center swear that he is fair in dispatching trains. They didn't cross examine him.

CHAIRPERSON MORGAN: Let me just move on to one last question, and that is the Port of Houston as a voting member of the PTRA. We have this

discussion in the record about the PTRA and who is a voting member. And what is the issue there?

MR. ROACH: I don't know that there is an issue. Tex Mex has -- the Board has passed a resolution to make Tex Mex a voting member. The port needs to sign that resolution, which is a ministerial matter. They haven't signed it.

Apparently, the reason they haven't signed it -- maybe, reportedly -- is that they're thinking about the position of the other parties about the port's right to vote. They are also a voting member but -- or we've all agreed that they can become one, but we do take the view that the port should not vote on investment issues, because they're unwilling to invest, or on rate issues where their traffic is involved. It's a pure conflict of interest issue, and they're thinking about that. And if they agree to that, they're going to be a voting member, too.

CHAIRPERSON MORGAN: So there is an ongoing dialogue, then, on this --

MR. ROACH: Absolutely.

CHAIRPERSON MORGAN: -- issue --

MR. ROACH: Yes.

CHAIRPERSON MORGAN: -- of voting membership on PTRA as it relates to the port?

MR. ROACH: Yes. The agreement for Tex Mex to become a voting member was executed on the 18th of November. And it's awaiting the port's action. We didn't oppose Tex Mex being a voting member.

In the end, actually, we had reservations because Tex Mex didn't want to contribute any capital, and we've dropped that. We've dropped a lot of positions that we thought were fair during the course of the last couple of years of trouble, and this is another one. They are now a voting member and they're not contributing to the capital.

CHAIRPERSON MORGAN: Question?

VICE CHAIRMAN OWEN: Yes. If I could have a couple here just for a moment, Mr. Roach, please. What is the timetable for the completion of all of the construction projects in the Houston area and infrastructure there? Do you know that?

MR. ROACH: Wow. We put in a plan for five years of investment on May 1. There is no

timetable for the completion because it will go on forever. But --

VICE CHAIRMAN OWEN: It will probably go on forever. But, I mean, under the merger plan --

MR. ROACH: The --

VICE CHAIRMAN OWEN: -- it seemed like the bulk of them were going to occur within the first couple of years. And I was wondering when that might occur, that there might be a little bit more fluid movement. That's what I was getting at.

MR. ROACH: Well, you're right that the merger-related capital tended to be somewhat front loaded. And a lot of that is still going forward and really is separate from this new Houston plan that we submitted on May 1.

The May 1 plan is not really all that front loaded. There are some projects that you need to work up to, and some of the big dollar items are actually in the outyears. But as I say, we're ahead of where we planned to be this year by a little bit. We're going to get to close to $170 million on that overall plan, and we're planning to keep pursuing it.

We've got to earn the earnings to do it, but, you know, our loadings are coming back some. That's one of the other charts I wanted to show you is this chart 16. In chart 17, we're still down 6.2 percent from a year ago, and BNSF is still up eight percent. So we're --

VICE CHAIRMAN OWEN: I saw that.

MR. ROACH: -- going to get our traffic back and our revenues back, and we're kind of making these plans on the come in the hope that this railroad will track its shippers back. And they're coming back.

Dow, for example, has put all of its traffic back on our railroad. They were moving it by short haul to other railroads, or truck, or water. And pretty much everything they had diverted during the problems is back on our railroad. We're proud of that, and we're going to keep trying to get it all back and some more.

VICE CHAIRMAN OWEN: Well, some of these areas of requests here that have come in from some of the other railroads and some of the shippers that are

talking about a stranglehold or captive shipper, it seems like those might be precedent-setting policy decisions if the states were to make them in a particular way that they've requested. That might have repercussions throughout the nation in other areas where there might be so-called strangleholds or captive shippers, whether it be Oregon, Washington, New Orleans, or New York.

MR. ROACH: Right.

VICE CHAIRMAN OWEN: Is that not the case?

MR. ROACH: Of course. I couldn't agree with you more. We've got three major shippers here -- Central Power & Light, Dow, and Formosa -- that are exclusively served, always have been -- the merger didn't have anything to do with that -- that would like to have two railroads serve them and that have proposed a very, very thin pretextual connection to the service issue. They really don't have any serious argument. Their service is back where it should be.

CP&L, by the way, they said their service still isn't up to the contract cycle time standard. Well, fair enough, not always, and we have some

penalties that we have to pay if that's the case. But in terms of getting the trains there and building that coal pile, they are going great guns down there, and their stockpile is going to be where it needs be. And they are very happy with our service; they have told us so.

Formosa, I have told you, their cycle times are better than they were, or as good as they were, in the various lanes compared to before the merger, and the same with Dow. So, you know, they have really kind of run out of any connection to this proceeding for their desire for open access.

The other thing they talk about is investment, and I think I answered that. I said if they want to invest, let's do it. But you don't need open access to invest. You can work with us to invest. If you want to build a yard, we'll join you and build a yard.

VICE CHAIRMAN OWEN: Well, you and the Chairman have covered just about everything that I had to raise on this. But I am glad to see that you're working and negotiating back and forth on these

issues, because I think definitely there should be a tradeoff. If they are requesting something of you that is not already granted under our provisions here, then they should come to you and negotiate that position.

MR. ROACH: Yeah. I think we've learned some hard lessons about listening in this industry and this company. And, you know, this example of directional running -- we're not going to suddenly shift over to directional running if it's going to harm some shipper or another railroad. We're going to talk to people before we make these decisions.

But you ought to take them one by one and not have some blanket rule that says forevermore, if UP ever changes the directional running, BNSF automatically gets more trackage rights. That's a commercial issue. We've got to talk.

VICE CHAIRMAN OWEN: Thank you.

MR. ROACH: Thank you so much.

CHAIRPERSON MORGAN: Next we will hear from Mr. Allen.

MR. ALLEN: Thank you, Chairman Morgan.

First, I commend your stamina. Second --

CHAIRPERSON MORGAN: We have good practice in that arena.

MR. ALLEN: I'm well aware of that.

Second, Mr. Roach has said many things that I'd love to personally respond to, but my time here is allotted to respond to the BNSF proposal, and my colleagues, Mr. Mullins and Mr. Thomas, will be addressing Mr. Roach in more detail.

I do appreciate the Board giving Tex Mex an opportunity to respond to the BNSF proposal. And in view of BNSF's argument this morning, I think that response can be quite brief.

Much of BN's request Tex Mex does not oppose. In fact, Tex Mex supports BN's request for permanent bidirectional trackage rights over UP's Caldwell-Flatonia-Placedo line.

Tex Mex strenuously objects, however, to BN's request for trackage rights over the UP line between San Antonio and Laredo. We've shown in our written response that that request is completely unjustified and would, if granted, likely be fatal to

Tex Mex and thereby result in the loss of essential services to Tex Mex of some 30 shippers.

Since BNSF has not argued that claim this morning, I don't believe I need take more of the Board's time on that subject. For the reasons stated in our written submission, we think the claim is clearly without merit.

We also think -- and here I would strongly agree with Mr. Roach -- that there is no basis for BNSF's suggestion this morning that the Board defer decision on the trackage rights request between San Antonio and Laredo. Tex Mex, as we have stated in our filing, has been negotiating with BN assiduously since the merger was decided two years ago. We continue to negotiate with BNSF on commercial terms.

We're always hopeful that those negotiations will result in a mutually acceptable agreement. And we're still hopeful, but we haven't reached an agreement. And there is simply no basis for the Board to do what BNSF evidently attempts -- is attempting here, which is simply to give them another bargaining chip in that purely private commercial

negotiation.

We think there is no merit to their request and it should be promptly denied.

As I mentioned, other aspects of the BNSF proposal Tex Mex does not oppose. In fact, Tex Mex strongly supports BNSF's request for permanent bidirectional trackage rights between Caldwell and Placedo. Those rights are extremely important in giving BNSF an efficient connection with Tex Mex for a very important segment of traffic that is non-circuitous and that avoids Houston.

That connection is essential if interline BNSF-Tex Mex service is to be an effective competitor to single-line UP service to and from Mexico, as the Board clearly intended in its decision approving the UP/SP merger.

I also note that BNSF has indicated its support for several elements of the consensus plan, including item 1B, granting Tex Mex permanent rights over the Algoa route to Houston, and part of item 4, which would give all railroads serving Houston terminal trackage rights over all lines in Houston to

permit the most efficient movements and dispatching in Houston.

Unless the Board has any questions --

CHAIRPERSON MORGAN: I think that your position is clear.

MR. ALLEN: Thank you very much.

CHAIRPERSON MORGAN: Thank you.

Okay. Now we'll hear from Bill Mullins, who will be representing Kansas City Southern, and Larry Thomas, representing The Society of the Plastics.

MR. MULLINS: Thank you, Chairman Morgan. I'd really like to address three issues -- the competition issue, the infrastructure issue, and the dispatching issue. I don't believe we've had sufficient discussion of the competition issue because really what this plan is about is restoring the competition that was lost.

Now, you'll say, "Well, Mullins, if that's the case, then where have you shown that there has been market power from the merger so that competition has been lost?" Well, we've shown that in two areas.

First, we've shown that in the two to one shippers.

Now, we've talked about the market share, that prior to the merger SP had a 32 percent market share of this two to one traffic. Post merger, BN Santa Fe only has a nine percent market share.

Well, UP claims that this market share merely shows that there is vigorous competitive bidding between UP and BN, and shippers chose to stay with UP because UP was offering better rates and better service. But there are numerous problems with UP's claims.

First, why would the shippers decide to stay with UP in the midst of the service crisis? Certainly, UP wasn't offering better service during that time. Why didn't they switch to BN Santa Fe? Because BN Santa Fe's service depends upon UP's dispatching, switching, and control, while SP's service did not.

Indeed, BN itself admits that where they depend upon UP's switching or haulage, that they cannot be competitive at two to one points. The second problem with the UP's argument is if the reason

is truly that UP offered lower rates, one would have to search the record long and hard to find any evidence that that is the case.

Is there a UP rate study showing that rates are lower at two to one locations during the two-year period since the merger? Absolutely not.

CHAIRPERSON MORGAN: But I -- I just want to stop you there. But clearly, market share is not the only --

MR. MULLINS: Clearly, market share --

CHAIRPERSON MORGAN: -- evidence that you look at to determine whether competition is --

MR. MULLINS: No. But market share --

CHAIRPERSON MORGAN: I mean, rates are a valid --

MR. MULLINS: Rates are a valid indication, but market share -- absent a rate study or a rate analysis, you have to look at market share. But yes, absolutely, rates can be a valid indicator of market power as well as market share.

So, you know, what does UP point to in the record as to show that they've offered lower rates and

better service at these two to one locations? Well, they point to UP/SP 345, Confidential Appendix C, filed not in this proceeding but in the general oversight proceeding. This is simply a listing of various bid activities between UP and BNSF at some selected two to one points.

In this list, UP often mentions that it has offered "lower rates" to maintain that business, giving the impression that the shipper is benefitting from lower rates. But one must ask: lower rates from what? If it is merely lower rates than the rates offered by BN Santa Fe, without a reference point, that means nothing.

For example, if the SP market rate was $150 a car, but post merger it went to $200 a car, but then there was bidding and BN offered $190 and UP came in and offered $175, that doesn't prove the case. Yes, UP offered lower rates, but it was still a higher rate than the pre-merger rate that SP offered.

And even if you accept the notion that some UP rates were actually lower than the SP rates, then you must ask: why is this so? General economic

conditions? Changes in the marketplace? Better productivity? Or is it due to the competition between UP and --

VICE CHAIRMAN OWEN: Excuse me. Just a moment there, Mr. Mullins. But was it due to the fact that SP was basically bankrupt? Was that the reason the low rates were going on at that time?

MR. MULLINS: We don't know what -- I mean, you know, that's --

VICE CHAIRMAN OWEN: No, I don't know that. But I'm just saying, we --

CHAIRPERSON MORGAN: But I think the point he is making is --

VICE CHAIRMAN OWEN: You're making a lot about --

CHAIRPERSON MORGAN: -- the world changes, and, you know, there are factors that do enter into it.

MR. MULLINS: The world changes, but your test is whether there is market power caused by the merger. You have to look at the two to one shippers, and we've looked at it. We've looked at market share.

And even if you don't buy off that market share is an indicator, then let's go and look at the rates.

But what evidence is in the record to show that the rates are lower? All they have is this anecdotal evidence about the bidding between the two -- between shippers. But they don't give any reference point. There is no rate study. They haven't explained why those rates are different, how the market conditions have changed. And so, finally, then they say, "Well, there's no shippers in here complaining, no two to one shippers."

Well, take a look at that confidential appendix, and you look at those shippers. There's about 80 instances in that confidential appendix that deals with bidding back and forth. Only about 20 or 30 of them are Texas-based shippers, so -- and that's what the focus here is -- Texas-based shippers. And of those, six of those shippers have filed comments in this proceeding requesting conditions.

There is evidence that there is a harm at two to one locations, and those shippers have come in here and said there's a harm. Now, we can't deny it,

and UP has not presented evidence that the rates are better.

Now, let's turn to the issue of three to two shippers. Prior to the merger, shippers who were served by the HBT and the PTRA had three carriers -- UP, SP, and BN Santa Fe. Well, the consensus plan merely restores that situation. When you lift the restriction that is imposed on Tex Mex, all you do is allow HBT and PTRA shippers to receive service from the three shippers that existed prior to the merger.

Now, this is not adding competition. This is simply restoring competition that was lost. Restoring full Houston access for three carriers is necessary because BNSF has not been able to provide the same level of competition that SP provided to these HBT and PTRA shippers before the merger.

We know that in the northeast market that the market share that BN Santa Fe has is significantly less -- or they've actually gained a few. But if you look, for example, at the carload -- inbound carloads, BN's market share is actually less than what SP's market share was prior to the merger, yet alone the

fact that you have to look at the fact that UP and SP's market share is combined. They represent something like 89 percent of the market. This is in the record. And BN's is only 11.

So if we look at the northeast, we see that there has been a competitive problem -- market share information that BN Santa Fe has not replicated SP's situation. And the lifting of the restriction is merely going to restore this competition.

You know, this Board has often said that we should look at the level of competition, not the number of carriers. And the reason why you imposed conditions was to preserve the level of competition. Well, that level of competition is not being preserved by BN Santa Fe acting via trackage rights. It is necessary to lift that restriction on Tex Mex so that you can provide both BN Santa Fe and Tex Mex the opportunity to access those HBT and PTRA shippers.

If you do that, all you're doing is restoring the level of competition. You're not giving shippers new access. You're not opening up Houston. You're just restoring the level of competition, the

level, not the number of particular carriers. And that's what the Board's legal market authority is is to preserve the level of competition.

CHAIRPERSON MORGAN: Let me just stop you there. I just want to make sure I understand. We're talking about two to one shippers, three to two shippers, and one to one shippers.

MR. MULLINS: Right.

CHAIRPERSON MORGAN: And with respect to two to one shippers, you're saying that there isn't the evidence that the competition has been vigorous for those two to one shippers. That's what your argument essentially is -- looking at rates and market share.

Now, with respect to the three to two, you're saying that, well, the Board did make the determination that going from three to two was not anti-competitive, and we did make that determination in the merger. And what you're saying is, no, we need to go back to the three carriers that we had before.

MR. MULLINS: Not to necessarily replicate the level of competition that was representative by

three carriers, but to replicate the level of competition that was represented by SP. SP --

CHAIRPERSON MORGAN: But so what you're really saying to the Board is the argument that you -- I mean, this is an argument that we heard during the course of the merger, of course, if you go to three to two -- from three to two, that's going to be anti-competitive. What you're saying is, well, we did go from three to two, and that was anti-competitive. We needed to go --

MR. MULLINS: No, what I'm --

CHAIRPERSON MORGAN: -- back to 3.

MR. MULLINS: No. That is not what I'm saying. What I'm saying is that you put in BN Santa Fe there. You thought there was going to be vigorous competition. You said three to two is not a problem. BN Santa Fe was going to be there to provide the effective competition.

So if that's going to be the case, then you have to look at whether or not BN Santa Fe has actually replicated SP's level of competition.

CHAIRPERSON MORGAN: Well, then, why don't

we look at getting -- making BN Santa Fe a better competitor?

MR. MULLINS: Well, there's one way -- you tried to do that in the Board. And we know that BN Santa Fe has not been an effective competitor to the northeast. So what I'm saying is BN Santa Fe is sitting there competing with one hand behind their back --

CHAIRPERSON MORGAN: Well, no. But what I'm --

MR. MULLINS: -- via the trackage rights.

CHAIRPERSON MORGAN: -- saying is -- and I'm just trying to make sure I'm following your argument -- if your argument is that BNSF has not been an effective competitor --

MR. MULLINS: Right.

CHAIRPERSON MORGAN: -- the way the Board planned it to be --

MR. MULLINS: Right.

CHAIRPERSON MORGAN: -- so what I'm saying is then what the Board should be looking at is improving BN Santa Fe's competitive posture.

MR. MULLINS: The Board has -- that's not the only way you need to be looking at it. We know that BN Santa Fe has a strong presence out to the west and has, in fact, replicated SP's market share for traffic moving to the west. We're talking about traffic moving to the northeast, and your obligation here is to narrowly tailor a condition.

If you lift the restriction on Tex Mex, you have narrowly tailored -- you have a narrowly tailored remedy there, which provides the level of competition that existed prior to the merger. Because BN Santa Fe is not providing that level of competition.

Yes, one way to do it would be to somehow look at BNSF and try to figure it out. Another way to do it is lift the restriction. It's not a problem. It's all -- it's a paper barrier. We've heard a lot about paper barriers. Let's lift the paper barrier. It doesn't provide any new access to any shippers. Tex Mex already has access to HBT and PTRA shippers.

You lift the restriction, those shippers now have their pre-merger level of competition

replicated because Tex Mex can take that traffic to the northeast and hand it off to the northeastern gateways. That's restoring competition, not adding competition.

Now, let me address briefly the infrastructure issue. We have $120 million of infrastructure investment in this case that we are willing to make. Now, we actually agree with your comment that you have a very complex -- Vice Chairman Owen, you have a very complex terminal area down there.

But, you know, when you have a very complex terminal area, the solution is not to turn it over to one railroad to let them control everything when you have three railroads down in the area. When you have a complex situation out at Dulles Airport when you have service problems, capacity problems, you don't turn over the dispatching and the infrastructure improvements to Delta. No, you want to set up a system that allows the three railroads that operate in that area to invest equally, to make joint decisions.

Do you know what we call that in the rail

industry? A terminal railroad. There used to be terminal railroads existing down there -- the HBT and the PTRA. They dissolved the terminal railroad. They dissolved the HBT, which is a case that is still pending in this Board by the way.

And we also know that by restoring the PTRA and the HBT, then you give all three railroads a stake, and all three railroads can invest. Take a look at the example of the Kansas City Terminal Railroad up in Kansas City. That has four or five railroads in the Kansas City terminal. They all jointly invest. That's what we're suggesting. Let the PTRA, which is controlled by all of us now because Tex Mex is going to be on the Board, jointly invest.

And briefly on the dispatching, let me touch on the dispatching issue, Chairman Morgan. The reason we haven't gone to the Spring Center is because they haven't let us participate in the management. What they've said is, "You can bring in your dispatching. We'll give you this cubicle, and then all of your dispatchers can pick together." But the supervisor -- the supervisor of that is only selected

by BN and UP.

If you want them in the Spring Center, then Tex Mex has to have a right to say who the management is.

And I'd like to -- sorry I went over my time, but I had to answer your questions, and turn it over to Mr. Thomas.

CHAIRPERSON MORGAN: But you do agree that in the Spring Center the director of the center has the authority to resolve disputes.

MR. MULLINS: Yes.

CHAIRPERSON MORGAN: He is the neutral --

MR. MULLINS: Yes. But, well, he's not neutral now. He is only joint. And if you don't allow him to be truly neutral by giving Tex Mex a say in who the director is, then you don't have a neutral director. You have a joint director picked by UP and BN. So it's not a solution just to say, "Tex Mex, move your dispatching to the Spring Center." That does nothing. That turns over Tex Mex's dispatching to UP and BN management.

Let's have a neutral manager there, and

that's what our PTRA plan does. PTRA, which will be controlled by everybody, allows there to be a neutral manager selected by everybody.

CHAIRPERSON MORGAN: Let me just also -- on one other point, because we were talking about two to one and three to two. There also are these one to one shippers.

MR. MULLINS: Right.

CHAIRPERSON MORGAN: And under the consensus plan, these shippers would go from being served by one to three.

MR. MULLINS: The one to one --

CHAIRPERSON MORGAN: How does that work in terms of our legal authority?

MR. MULLINS: I'm glad you brought that up. Under the consensus plan, the only new shippers who gain additional access are a result of the expansion of the neutral switching district. The plan calls for the merger of the HBT and the PTRA, basically restoring what existed prior to the merger. Now, that's adding no open access, no open access when you're just putting HBT and PTRA back together.

Where does the open access come in? The open access comes in when you expand the geographic limits of the neutral switching entity, which the plan does. The plan does expand the geographic entities to take in the Bayport loop. Some of those shippers down there were one to one shippers.

We believe those one to one shippers did suffer a merger-related competitive harm. But, again, that is only a portion of the consensus plan. When you basically merge HBT and PTRA back together, there is no open access. There is no shipper getting a new carrier. They're just having their level of competition restored.

Have I sufficiently explained that?

CHAIRPERSON MORGAN: I think so.

VICE CHAIRMAN OWEN: You have rose-colored glasses a little bit different than mine.

MR. MULLINS: Thank you.

CHAIRPERSON MORGAN: Mr. Thomas?

MR. THOMAS: Chair Morgan, Vice Chairman Owen, let me begin by mentioning that The Society of the Plastics Industry that I have represents not only

all of the major resin producers in this country producing 90 billion pounds of resin, most of which is down -- coming through the Houston market, but some 20,000 processors -- product manufacturers if you will -- throughout this country that depend on those resins, depend on fair pricing, depend on a reasonable level of service. We are the most dependent industry in this country on rail service -- the most dependent.

I've sat here today and I've listened throughout these proceedings, and I think we all know that, referencing back to one of the comments you made, there really is only one key issue here. One issue, and that issue is competition.

The UP clearly, through the statements that were made here, does not believe in competition. I don't think in my some 30 years here in Washington I have ever heard any statements so anti-competitive, to sit here and listen to the argument that we ought to have the freedom to unilaterally raise our prices because of what you referred to, and quite correctly referred to, as an absolute stranglehold on a market in Houston, with the idea that somehow magically this

is going to result in their benevolent investment in infrastructure.

I wonder if they talked to Dow about how Dow improves and meets competition and operates more effectively in what -- I believe in the free enterprise system -- in order to have the profits needed to make their investments.

And you talk about a competitive industry. I'd ask you to visit with some of our companies, and I think you'll see one of the most competitive industries in the world.

UP's absolute control over the Houston market, almost total control, has been demonstrated because when its service was at its very worst there was no alternative. We didn't have anywhere to go. I don't know whether they lowered their rates or not. You know, if I had been in their situation offering service that had gone from four days to 40 and 50 days, I guess maybe I would have tried to throw somebody a bone, too, in that unbelievable situation.

But I'll tell you one thing, it didn't matter because if our companies had had a viable

alternative, had had some real competition, they wouldn't have let UP in the height of this crisis continue to have their business.

You know, UP really wants it both ways. On the one hand, they step up here and argue they shouldn't have any competition and make this outlandish statement that, oh, well, the reason is because, you know, it might make us competitive with our rates and we won't have the money to invest in any infrastructure. And then they turn right around and hold up the BN as providing effective competition.

You've heard it -- that BN has not provided any effective competition. We haven't seen any real competition.

I'm just going to end by -- because there is only this one issue -- by saying that I truly believe that this Board has a public responsibility. You have a responsibility to operate in the public interest, and our industry and I do not believe that maintaining a virtual monopoly in the Houston marketplace is in the public interest.

I don't believe a -- and I don't believe

it will accomplish what you want to accomplish and what we want to see accomplished, which is no more of this kind of crisis. We don't want any more of that. Our industry can't take it. We've been hit too hard. The State of Texas has been hit too hard.

You're sitting here today -- I would hope we are here today to find a way to make sure this doesn't happen again. So ask yourselves, what is it that produces effective price competition? What is it that produces effective service? What is it that would bring in some alternatives to help in developing infrastructure?

The only thing that will do it is for you to take an aggressive action today and to adopt the consensus plan that we've proposed that will bring some real competition into this arena, into the Houston market.

And I would say, Vice Chairman Owen, you've asked -- and I think rightly so -- on every occasion I've been here, "Well, what about a private solution?" What about a private solution? We tried to sit down with the UP. We've tried to bring the

parties together.

We've tried to work out a private solution, and what we've heard time and time again is, "Oh, we'll take care of it. We'll fix it. Service is improving. The light is out there at the end of the tunnel." I haven't seen it, and I believe what will actually turn that light on is some real competition, and that's why we're here today asking for the adoption of this consensus plan.

We need some aggressive action on the part of this Board to solve this problem, so that we don't have this kind of crisis again in the future.

I'd be glad to respond to any questions. Maureen Healy is here, our Director of Transportation, and our legal counsel is here, Marty Bercovici.

CHAIRPERSON MORGAN: Well, I think your statement was very clear. I think you want more competition. That's essentially the summary of your remarks. I think we've probably asked all of the questions, in one way or another today, that need to be asked. I have a closing remark or two.

But before we leave this panel, Vice

Chairman, if you have anything else to ask this panel.

VICE CHAIRMAN OWEN: I wasn't going to say anything, but after your remarks there, I just want you to know that I have tried to cope with this problem for four and a half years since I've been here, a little over four years, of the railroads and the single traffic and the competition, market prominence, open access, all of these issues -- rates, bottlenecks, and everything else. And it still escapes me. It's a real difficult problem.

And yet, when I see this group come in here today, somehow we're reaching for things off the Christmas tree again, without really putting together a compatible, connective type of solution to it, long-lasting. And when I look at your local port there, and your Railroad Commission, I see -- still, I continue to see piecemeal solutions to the problems.

And if we try to adopt those --

MR. THOMAS: Well, when you --

VICE CHAIRMAN OWEN: -- and transfer those to other parts of the nation --

MR. THOMAS: When you look at --

VICE CHAIRMAN OWEN: -- you create great chaos in the industry as a whole.

MR. THOMAS: When you look at me, Vice Chairman Owen, you're looking at someone here representing shippers.

VICE CHAIRMAN OWEN: Right.

MR. THOMAS: We don't represent a railroad. We don't have any desire to get anything off a Christmas tree except one thing. We want the restoration of a reasonable level of service in the Houston market. This is the heart of our business -- the Houston market.

VICE CHAIRMAN OWEN: I know.

MR. THOMAS: It doesn't exist there today. So we're here asking for a restoration of a reasonable level of service, so that we, as an industry, can continue to compete effectively and operate in the public interest by delivering our downstream customers, and the ultimate consumer, products at a fair price.

So I thank you again for the time today.

VICE CHAIRMAN OWEN: Thank you.

CHAIRPERSON MORGAN: Thank you.

Let me thank everyone for being here. It was a productive hearing. I want to thank the staff. You know, as I've said before, when we put one of these things together it requires a lot of staff to work on it and get it implemented in the right way. So I want to thank each and every staff member of the Board who was around and who has helped us.

There is one other person, though, that I want to thank, and that is Gus. This is probably the last public hearing that he and I will be together at, I hope.

(Laughter.)

And let me just say that, you know, sometimes in this town we forget to say thanks, we forget to support our friends, and we forget to look at the positive contributions that people have made, and I just want to say to you, Gus, thank you. Thank you for your friendship, for your support, and for your many positive contributions.

The Board and the transportation community could not have done it without you. I could not have

done it without you. And we are forever indebted to you for your service.

We had a recent gathering here at the Board in which we honored Gus, and at that time I read the following quote, which Gus has heard but perhaps the rest of you have not, and it goes like this: "Real generosity toward the future consists in giving all to what is in the present."

Gus, you have given much to the future by being here with us in the present, and I don't believe anyone will forget that. I certainly won't. And I hope you will call on me every now and again and give me a little common sense and a little good advice because it ain't going to get any easier.

With that, I would just like to give you an ovation.

(Applause.)

VICE CHAIRMAN OWEN: Thank you. Thank you. No speeches.

(Laughter.)

CHAIRPERSON MORGAN: We have begun today with what is important, and we have ended today with

what is important, with all due respect to Houston.

Everyone will hear from us very shortly on this decision. With that, I think we can adjourn. We've done a hearing in less than four hours; I think that's a record. And we will be off to get the job done.

Thank you all very much.

(Whereupon, at 1:45 p.m., the proceedings in the foregoing matter went off the record.)