Hut. I will present argument today for Consolidated Rail Corporation. With me today at counsel table is Constance Abrams, a general counsel with Con Rail.

Con Rail opposes the merger unless it is conditioned on the required divestiture of specifically identified lines and assets in the eastern portion of the SP system, what we at Con Rail call SP East.

I will, Commission Owen, specifically identify the lines to which I refer later in my argument.

Like others before me this afternoon, I am going to try to set aside in large part my prepared remarks and address the principle questions that as I listened to earlier colloquy seemed to me to emerge.

First, why the BN trackage rights won't work as a remedy here. Second, why divestiture will work and will preserve the benefits of the merger.

Third, Vice Chairman Simmons, I will try to address the question you have put, how the divestiture process would work. Fourth, I want to speak to the question why further regulatory oversight.
will not work.

Let me begin, however --

VICE CHAIRPERSON SIMMONS: You are going to do an awful lot in a short time.

MR. HUT: I'm going to try by telling you why Con Rail is here. The answer is because our customers have said to us and in record numbers, they have said to you, that they will be seriously harmed by the merger as proposed.

An enormous portion of the traffic that originates or terminates in the SP East region goes from or to a point on Con Rail. If service suffers there or if rates go up, or both, Con Rail customers are hurt.

These customers have said to us that the competitive harms in the SP East region are substantial, that they are not outweighed by any benefits produced there, and that they are not remedied by the BN trackage rights deal in any of its incarnations.

Instead, SP East shippers in vast numbers support divestiture, because only divestiture
establishes a property owning carrier with an investment in the lines sufficient to create incentives for business development, for growth, and for further investment.

Con Rail has said that its divestiture proposal would remain on the table as long as our customers support divestiture as the solution to the harms caused by the merger. They do, and the offer remains.

Let me stress, however, that this stage of the proceeding is not about Con Rail or any divestiture carrier. It is about framing a remedy that will work and that will meet the needs of the shipping public.

Turning to the problems with the merger, it creates acknowledged and unacknowledged competitive harms. The two to one points are only a part of the story. Even as to them, applicants preferred remedy, the BN trackage rights doesn’t work. An applicants preferred excuse, the endless tail of SP competitive and financial loads is wrong.

SP is today, it would remain tomorrow, a
vital competitive force in the SP East.

VICE CHAIRPERSON SIMMONS: Without anything?

MR. HUT: Well no one, Vice Chairman, not even SP says that they will go out of business. They are in the SP East region, not a distant third at all, but a strong and vital second. They are through April, as I last look at the data, the only of the class one carriers who have reflected or who have recorded an increase in car load market share.

Contrary to what you heard today, SP has a solid inter-modal business as testified to by Con Rail Railroad professional's testimony in the record, Mr. Bridges, familiar with the inter-modal traffic.

VICE CHAIRPERSON SIMMONS: You are almost a man who stands alone then in your set. But go right ahead.

MR. HUT: I do think that they have, hold out significant promise as the testimony of Professor Hess said, with solid attention to management. They have assets. They have resources to continue to provide competitive service in the SP East.
Let me turn to the matter of the BN trackage rights. First let me address the question of BN's interest in the matter. You have raised that earlier, Vice Chairman Simmons.

The transportation department has pointed out that BN's position in this proceeding is seriously compromised. It has provided a small fraction of the information about its proposed service that the shipping public and the Board have a right to expect. Each new submission raises more questions about BN service than it answers.

It had no involvement in negotiating the latest effort to fix the trackage rights in the form of the CMA agreement. It has been reluctant to quote rates to shippers. As you heard earlier, those it has quoted have not been competitive. Its refusal to commit itself in the face of repeated customer demand speaks volumes.

Now its silence may very well reflect the lack of commitment. It may also, however, reflect BN's understanding of the serious operating problems associated with the trackage rights, to which I would
like now briefly to turn.

The heart of the story on the SP East trackage rights operations is Houston. BN’s former chairman Grinstein acknowledged that BN faces “severe service disability in Houston.” The significance of that is that Houston anchors each principle route that BN would acquire in the SP East system.

You heard Mr. Roach this morning acknowledge the disabilities produced by multiple switching and handling and the assistance given to operations by the ability to pre-block. Both these problems characterize BN’s service at Houston, both produce disability.

They will have multiple handling and switching. They do not have the capacity to pre-block. This results in increased transit time, cost, increased potential for mis-routing, increased safety risks. SP’s Houston service today faces none of these problems which are not addressed or rectified by the CMA agreement.

BN would be further disabled at Houston and elsewhere by insufficiency in switching and
classification yard capacity, as well as insufficient storage and transit capacity, as Mr. Bercovici mentioned earlier in the CMA agreement, as he indicated does not fix these problems.

Once out of Houston and particularly for traffic moving toward St. Louis, BN's operation problems continue. We have specified in detail in our comments, testimony and brief, that each of the routing alternatives available to them comes hobbled by significant operating disabilities. The CMA agreement has not cured any of these problems that were so graphically described earlier by counsel for IP.

Even if all of them could be solved and UP has been unable to do so in numerous tries, BN service would still rely on trackage rights and not ownership. BN would have no investment in the lines, no incentive to invest or develop business. What it will have are substantial transactions costs. Disputes between the parties are inevitable. The communications problems between SP and UP that Mr. Roach described this morning as the well-spring of the concerns in CNW are
perfect examples of these transactions costs.

In sum, the merger can not be approved with the BN trackage rights as the remedy for the competitive harms in the SP East region. That condition will not work.

But let me turn to the question why divestiture will work, why it will preserve the benefits. No one questions the Board’s authority to order divestiture. It was confirmed recently by Congress in the ICC Termination Act. Divestiture readily meets the four part test that the ICC cases establish, the imposition of conditions.

No one disputes that the merger creates competitive harms in the SP East region, or that divestiture will remedy those harms, or that it is operationally feasible.

Significantly, as the Justice Department points out, none of the railroads that has expressed interest in becoming the divestiture carrier would pose competitive concerns.

Importantly, SP East divestiture will also preserve the benefits claimed for the merger. Why?
It will do so because as applicants themselves acknowledge, these benefits, route shortening, increased single line service, capital savings, and targeted capital investment, are almost entirely in the western portion of the post merger network.

Those claimed in the SP East region by contrast, are either not benefits. There are substantial questions about the benefits of directional running, or the purposes served by some of these can be achieved in other ways.

That aspect that benefits are achievable in other ways is, Chairman Morgan, a principle focus under the regulations that govern these proceedings in Section 11.80.1.

Earlier Staggers Act cases, I should note, and there have been references to benefits produced by those, were overwhelmingly end to end mergers. This Board has not since the SF/SFP merger faced one with parallel aspects that this one has.

It is for these reasons that the divestiture fixes the harms while preserving the benefits that divestiture in SP East commands such
widespread shipper support. The shipper associations, from individuals, and indeed, from governmental entities such as the transportation department, the Texas Railroad Commission, and state attorneys general in the region.

Let me now address the third and fourth questions I wanted to get to. How would divestiture work and the problems with oversight.

Divestiture can be accomplished easily and expeditiously. It is a market produced structural remedy that will cure the harms once and for all. It involves far less need for continuing regulatory involvement than the proposed trackage rights deal.

VICE CHAIRPERSON SIMMONS: You sound like you are from the Department of Justice.

(Laughter.)

MR. HUT: Well, we agree --

VICE CHAIRPERSON SIMMONS: Go right ahead.

MR. HUT: -- in significant part. A concern that you must have about the regulatory oversight proposed for the trackage rights is the risk that BN and UP during the period of that oversight
would have substantial question about making investments in lines that could turn out to be as both counsel indicated this morning, there after candidates to divestiture. They said well if it doesn't work, you can divest later. How is that going to produce the necessary investment and the necessary hard competition from the --

CHAIRPERSON MORGAN: Well, we have heard this morning I think from the applicants that they would be willing to run that risk.

MR. HUT: They may say that now, but are they going to put their money where their mouth is?

CHAIRPERSON MORGAN: Well, if they don't know exactly where divestiture might occur, they'd have to put their money a lot of places.

MR. HUT: Or not. And that's --

CHAIRPERSON MORGAN: Then they'd probably have to do a lot of non-divesting throughout their system.

MR. HUT: That seems to be a major concern.

CHAIRPERSON MORGAN: Which I would hope
they would not do.

MR. HUT: If their concern was the SP East region where the competitive problems, I submit to you, Chairman Morgan, are most acute, that is where they may not do their investing as against the day that this Board would order divestiture.

The kind of regulatory oversight --

VICE CHAIRPERSON SIMMONS: Pardon me. You have to keep in mind that under your divestiture proposal, that there are those that say if you were the successful buyer of SP East, you'd be getting a huge windfall. Do you disagree or not?

MR. HUT: No. I do disagree. We think that we could provide a first-rate competitive service to shippers in the area, to introduce single line service for substantial numbers of shippers elsewhere in the country. But with the proposal, the question whether Con Rail now would become the divestiture carrier, it's not before you now.

VICE CHAIRPERSON SIMMONS: If you were successful, I think there would be a lot of points where you wouldn't even have any competition.
MR. HUT: We have, Vice Chairman Simmons, pledged and promised in testimony that were Con Rail to become the divestiture carrier, and that’s not a question I submit before you now, that we would maintain open gateways, on non-discriminatory terms, our merger would be or that acquisition, excuse me, that connection, that divestiture, would be entirely end to end. Con Rail is prepared as to the testimony indicates and as the public record indicates, to expend a very substantial amount of money, a substantial 10 figure offer.

CHAIRPERSON MORGAN: You just a minute ago said that divestiture is not really an issue here, but it really is, which leads me to my next question. That is, obviously you have an interest in divestiture and in acquiring SP East or your version of SP East. But there is no responsive application before us from you on this.

MR. HUT: That is correct, Chairman Morgan.

CHAIRPERSON MORGAN: So if divestiture is an issue in this case, and clearly it is because you
and others have made it an issue, and you are
interested, then why is there nothing before us?

MR. HUT: First of all, I think that there
is a good deal before you. Let me tell you why we did
not submit a responsive application.

We did not do so because we thought that
this phase of the proceeding ought to be about the
shape of the remedy, not about the identity of any
specific --

CHAIRPERSON MORGAN: But again, in this
day of trying to get as much done as efficiently as
possible, which I think is certainly what this Board
is about, and what Government these days hopefully is
about so that we can get decisions more quickly for
the business community, it would seem that all of
these issues should be before us fully at the same
time.

MR. HUT: I think that the issues can come
before you in very short order. The way we would
envision divestiture operating is in large part the
way Ms. Jones suggested.

First, that the merger could not be
consummated without investiture. Second, that as promptly as possible upon the rendition of any decision approving the merger conditional on divestiture, UP would be required to make known how it intends to conduct the operation, the divestiture process.

Third, that interested divestiture carriers, and there are many who have expressed interest, with substantial value being offered, would make competitive auction type proposals to forge a market-driven response.

That process, which would culminate in negotiation and the development of a definitive agreement, could be accomplished very very promptly in a matter of weeks, and would then be submitted to this Board, which given the expedition with which the proceedings have been conducted to date, I have no doubt, although it would be your judgement, could accomplish the necessary proceedings with greater expedition, because the issues would be --

CHAIRPERSON MORGAN: That assumes of course that one person prevails in negotiations with
If that is not the case, then I would not expect it to go quickly. I would expect that it would be another proceeding with differing views on divestiture, how much, who, and so forth.

MR. HUT: That is conceivable, but one person would prevail with UP in the sense I think that UP would select a single divestiture carrier with which it would negotiate --

CHAIRPERSON MORGAN: And then if there is opposition to that selection, then we get into round two and further proceedings. Is that possible?

MR. HUT: It's possible if there were a serious opposition. But the nature of most of the proposals on the table, not all, but certainly many, suggest that the opposition would be certainly far less than you have --

CHAIRPERSON MORGAN: Well I can envision a situation in which one railroad would end up being the selected one, and another railroad would not be favorably disposed to that selection. That could present us with another controversial proceeding.
MR. HUT: It could, but the controversy I think would be far less broad in its scope and could be resolved far more quickly than this one, which after all, has been only seven months from the filing of --

CHAIRPERSON MORGAN: Well, you recall when the sale of Con Rail was at issue, that certainly was not an easy issue to deal with because there were a lot of differing views, even within the railroad community about how that should turn out. So I'm not sure about that.

MR. HUT: That is so. You cannot eliminate all together the possibility of disputes with these complex transactions that have difficult operational and other issues. But this Board in this proceeding has demonstrated that it knows how to move matters along with extraordinary and commendable expedition.

I want to turn, if I can, and my red light has been on for some time, so if the board would bear with me, to one further component of my presentation. That is, the content of the divestiture we are
requesting.

In framing a divestiture remedy, the Board would begin with the lines that virtually all parties, and there are many, who endorse SP East divestiture advocate, Houston-New Orleans, Houston-Memphis-St. Louis. Those routes are identified by the heavy blue line on the map that we submitted with our brief that is reproduced to my left, to the Board's right. I believe you have a presentation before you on an 8-1/2 by 11.

Beyond that, there's further widespread agreement that SP East also comprises the Houston-Brownsville route, which applicants acknowledge is a two to one corridor.

The Houston-Eagle Pass route and the St. Louis-Chicago route. Again, the map to my left with its broad multi-colored bands tells that story. It is over these routes that SP's traffic moves today. These routes should all be divested.

Finally, numerous shippers along with ConRail, also urge the divestiture of the route to El Paso in order to assure competition at Mexican
gateways. As the Justice Department has suggested, the Board should include routes like this one that are necessary to realize fully the pro-competitive commercial and operating benefits of a divestiture remedy.

COMMISSIONER OWEN: In as much as we are talking about divestiture here, can you identify how many class one railroads compete with Con Rail in its territory?

MR. HUT: Two.

COMMISSIONER OWEN: Territory -- Con Rail also requests that the applicants be ordered to sell to Con Rail the eastern lines of Southern Pacific in support of divestiture. Con Rail speaks of resulting efficiencies from single line operations, faster transit times, lower operating costs, and pure freight car handling. Does it not follow that similar efficiencies would result if either Norfolk Southern or CSX gained access to Northeast markets, now served exclusively by Con Rail?

I think that when we come to the Christmas tree here, we should start taking a look at what we're
going for and see if it goes in the opposite direction.

MR. HUT: Well, Commissioner Owen, it seems to me that different standards apply. What we’re talking about here is a merger that is proposed, is a merger that reduces rail competition from two to one, and not to a pre-existing condition.

I should add also that Con Rail at this stage is not asked the Board to require divestiture specifically to it, but rather to require divestiture, we believe that for some of the reasons you have identified and others, that the proposal that we could put on the table and present to UP would be in the best interests of shippers, the public, UP shareholders, and that it would commit itself for acceptance in presentation back to you for approval.

CHAIRPERSON MORGAN: But there are several different SP East divestiture proposals. There’s yours, there’s KCS’s which is a little different, there’s the Justice Department’s proposal. There are a variety of proposals out there, correct?

MR. HUT: The Justice Department, as I
understand it, actually suggests, turned down in its entirety.

CHAIRPERSON MORGAN: Right. But if you were to do a divestiture.

MR. HUT: Yes. There are a variety of proposals. As I say, there is virtual anonymity as reflected there in the heavy blue line. The multi-colored bands down to Brownsville, Chicago, and out to Eagle Pass do reflect the overwhelming number of parties recommending SP East divestiture and to endorse divestiture of those lines.

VICE CHAIRPERSON SIMMONS: You cite shipper support for Con Rail's proposal. Are any of these shippers located on SP's effected lines, to your knowledge?

MR. HUT: I believe so, Vice Chairman Simmons. We had support from Dow, PPG, Corning, Huntsman --

VICE CHAIRPERSON SIMMONS: They have expressed support of you being the Con Rail support then?

MR. HUT: They have expressed support for
Con Rail. There are numerous others in the record, and support for divestiture.

VICE CHAIRPERSON SIMMONS: Well I know they support divestiture. I am trying to find out who is supporting Con Rail.

MR. HUT: At least those that I have mentioned. Others, Chrysler, Citgo Petroleum, Liondell.

VICE CHAIRPERSON SIMMONS: Okay.

CHAIRPERSON MORGAN: Just to make it clear in terms of your divestiture proposal. I understand the consensus proposal, which is the heavy navy line over there. But yours is El Paso, Eagle Pass, Brownsville, Houston, and on up to Chicago. Is that the --

MR. HUT: That's right. Everything on the chart.

CHAIRPERSON MORGAN: That's how many miles total? Do you know?

MR. HUT: Approximately 1,200.

COMMISSIONER OWEN: You didn't ask to go all the way to Port of Los Angeles, Long Beach.
If Con Rail acquires South Pacific Eastern lines, those shipping to the northeast will have a choice of Union Pacific and then Con Rail, or Con Rail direct. Doesn’t it follow that Con Rail will refuse to set competitive joint rates with Union Pacific in order to force all of the traffic onto Con Rail lines?

MR. HUT: Not at all.

COMMISSIONER OWEN: Oh.

MR. HUT: We have promised the contrary. We have promised in sworn testimony through the testimony of principle Con Rail officers, to keep open gateways, non-discriminatory terms of interchange. We think that efficient joint line service is something that we want to encourage, not discourage.

COMMISSIONER OWEN: Who would enforce that then?

MR. HUT: Any aggrieved party could lodge complaints in an appropriate way.

VICE CHAIRPERSON SIMMONS: If you were successful --

MR. HUT: This Board.

VICE CHAIRPERSON SIMMONS: If you were
successful in your quest of this SP East, do you have
the economic wherewithal to handle the traffic?

MR. HUT: Absolutely.

VICE CHAIRPERSON SIMMONS: Where is it?

Do you have the equipment and everything to do it
right now, presently?

MR. HUT: Part of the proposal, Vice
Chairman Simmons, contemplates the required
divestiture of locomotives and rolling stock
sufficient to be able to permit Con Rail to provide
competitive service from day one.

VICE CHAIRPERSON SIMMONS: From who, SP?

From SP?

MR. HUT: From SP.

VICE CHAIRPERSON SIMMONS: I find that
hard to believe.

CHAIRPERSON MORGAN: Getting back to
trackage rights for a minute. Obviously on Con Rail,
in your system, you probably have trackage rights to
other places as well as individuals have trackage
rights on your system. Your position here seems to
indicate that trackage rights here would not work.
However, clearly they must work in your markets and you use them effectively. How do you square those two positions?

MR. HUT: Our position here, Chairman Morgan, is that the trackage rights will not work because of the serious operating problems that characterize these trackage rights.

We do not suggest that trackage rights cannot work, although we do note that I think any railroad would prefer to offer service as an owning carrier, just as any shipper would rather have service from an owner carrier. But in some circumstances, of course trackage rights do work and have worked.

Earlier this morning it was suggested to you that Con Rail operates over trackage rights for some 16 percent of its system. Those trackage rights, however, are quite different from the ones that are before you. Some two-thirds of those are freight exclusive routes over Amtrak and other passenger agencies. The other one-third is for overhead traffic only. So these are not rights that are developed to facilitate local service to specifically affected...
shippers who would otherwise suffer a reduction in
competition.

COMMISSIONER OWEN: Why is Con Rail, who
reports to be revenue inadequate, so anxious to spend
2 billion dollars to acquire the Southern Pacific
Eastern lines?

MR. HUT: Well revenue adequacy is
probably not the test. Otherwise, there would be a
number who would flunk it.

We believe that we can offer a first rate
quality service to the shipping public in the public
interest. We look forward to the day that we can
demonstrate that to the UP and to this Board, and that
we can of course in doing so, earn an appropriate
return on the assets invested in that operation.

CHAIRPERSON MORGAN: Thank you very much.

MR. HUT: Thank you, Madam Chairman.

CHAIRPERSON MORGAN: Next, we will hear
from William Mullins and James Rill, on behalf of
Kansas City Southern Railway Company.

MR. MULLINS: Chairman Morgan, before you
start the clock, I would like to make a procedural
First, let me state for the record that my name is William Mullins. I am with the law firm of Troutman Sanders. Our firm represents the Kansas City Southern Railway Company.

Second, I have given Secretary Williams, I see that they have passed those out. I appreciate that. Those are handouts of the visuals that we'll be using.

Third, we've been allocated 10 minutes. I plan on speaking for eight of those 10 minutes, and reserving the remaining two minutes for our co-counsel, Mr. James Rill, former assistant attorney general for anti-trust in the Bush Administration.

Accordingly, I would like that you notify me when my two minutes are left. At that point, I would like to stop, take any questions that you may have, and then turn it over to Mr. Rill. Thank you.

Chairman Morgan, Vice Chairman Simmons, Commissioner Owen, as many of you know, I spent six and a half years at the ICC. In that capacity, I sat right where all my former colleagues are sitting right now, right behind the commissioners. I advised three
different commissioners on various merger proceedings. I advised them on the Denver Rio Grande’s purchase of the SP, the KD case and the Wisconsin Central merger case. I was involved in all of those.

I was proud of what the commission and the staff did in those cases. I thought those were good mergers. They were in the public interest. I think history has proven that correct.

However, the proposed UP-SP merger is not like those mergers. This is not an end to end merger like every other post-Staggers Act merger. This is not a four to three merger like the KD case, or for that matter, the BNSF case. This is not a consolidation of the regional railroads like in the Wisconsin Central case.

The proposed transaction is significantly different from all of those previously approved mergers. This merger will result in the largest consolidation of parallel track in history. Everyone talks about the parallel nature of this merger. I believe this first graph graphically illustrates that with the colored lines representing the parallel areas
where UP and SP compete. That is unlike any other previous merger.

This Commission has previously stated that the burden of proof in a parallel merger is a heavy burden, and can only be met with substantial evidence. KCS submits that applicants have not met this burden.

The burden is on the applicants to prove the transaction is in the public interest, not on the opponents to prove otherwise.

I also want to tell you that this merger is the most anti-competitive merger ever proposed. As Exhibit no. 2 shows, this merger has seven times the anti-competitive effect of the BNSF merger and twice the anti-competitive effect of the Santa Fe Southern Pacific merger, which the Commission flatly denied.

VICE CHAIRPERSON SIMMONS: Are you telling me that if KCS finds the successful acquire, that there wouldn’t be any parallel lines?

MR. MULLINS: That is basically correct, Commissioner Simmons.

VICE CHAIRPERSON SIMMONS: Oh no. You haven’t looked at the map.
MR. MULLINS: We would not have a parallel competitive problem at all, because you would have UP and the SP merged system there. You would have the BNSF system there. You would have the KCS system there, all competing in the same markets. You would have three carriers.

I want to tell you that the parallels of this transaction and the Santa Fe Southern Pacific merger are uncanny. As here, it involves significant parallel effects. The Santa Fe, like the UP, proposed a series of trackage and other rights to remedy those problems. And as in this case, every time the opponents pointed out a problem with that remedy, they would change it.

Finally, there were threats that the SP would go bankrupt, would have to retrench if Santa Fe were not allowed to buy the SP. But despite the threats of walking away from the deal, the changed remedies and Santa Fe's last minute attempt to grant an extensive set of trackage rights, the Santa Fe Southern Pacific merger was denied. It was denied because the anti-competitive effects were simply too
great to be fixed.

But unlike the Santa Fe Southern Pacific merger, however, the Board does not have to deny this merger. While there are significant anti-competitive effects, there are benefits, Chairman Morgan. We'll gladly admit those benefits.

The question for the Board, and I know you are struggling with it. I know the staff and the commissioners are all struggling with it, which is what is the best way to fix those anti-competitive effects and preserve the benefits? That is what the debate is going on right now, the internal debate among the staff.

Applicants have put forth a set of trackage right. They are the most extensive set ever proposed. They have changed this trackage rights over four times.

They first said it fixed all the problems. Then they changed it again. Again last Friday, they put in some new changes without an adequate opportunity to comment on those changes.

Indeed, I'm a little unsure as to what
transaction I am supposed to be submitting evidence on
because it keeps changing throughout this whole
proceeding.

VICE CHAIRPERSON SIMMONS: I suggest you
better catch that with them then.

(Laughter.)

MR. MULLINS: Well, I’m trying. I’m
trying. If you’d give me 30 more days, I’d love to,
Commissioner Simmons.

VICE CHAIRPERSON SIMMONS: You’re not
going to get 30 days.

MR. MULLINS: That’s too bad.

CHAIRPERSON MORGAN: You’re not going to
get 30 more days.

MR. MULLINS: Ten, all right? I’ll take
10.

Nevertheless, is it true that shippers
will be protected by the ever-changing BNSF agreement.
If it were true, then all the shippers and shipper
groups would not be here today.

As they have told you, the trackage rights
proposed will not solve the competitive problems.
Attempts by this Board to fix those competitive problems by further tinkering with those rights will be wholly inadequate.

Even the trackage rights sought by other carriers such as Tex Mex will also fail to resolve the competitive problems of this merger. For instance, Tex Mex proposal to use trackage rights does nothing to resolve the competitive harms in the Houston to St. Louis corridor, or for that matter, NAFTA traffic coming out of Chicago.

Now let me explain to you why divestiture is a better remedy than trackage rights. Applicants say divestiture would reduce service quality, undermine the benefits, eliminate new single line service, re-balkanize the railroad system. These claims are simply untrue.

Applicants propose a 1.3 billion dollar corridor upgrade program to rebuild and reconfigure a merged UP/SP system. The purpose of this upgrade program is to provide new single line service for certain routes that have never before had single line service.
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Applicants propose a 1.3 billion dollar corridor upgrade program to rebuild and re-configure a merged UP/SP system. The purpose of this upgrade program is to provide new single line service for certain routes that have never before had single line service.
But I'd like to direct your attention to
the chart where the blue lines represent the lines
included in the corridor upgrade program, while the
red lines represent the KCS divestiture proposal.

As is clearly shown, none of the lines
included in the KCS divestiture proposal are scheduled
for the corridor upgrade program. Indeed, they can do
their entire 1.3 billion dollar upgrade program with
divestiture.

As a result of this merger, applicants
will be able to provide new single line service over
numerous new routes. But as the chart showed, the
maps in the brief showed, and as the next chart shows,
not any of the single line routes that are put forth
in the applicants proposal, in their brief, none, none
of the single line routes, the new ones that they
identify will be impacted by the KCS divestiture
proposal.

Indeed, I challenge Mr. Roach to come up
with one single line route that will be impacted by
the KCS divestiture proposal. When you asked him that
question later today, he talked about maybe some
problems in the central corridor. But did he tell you
a single line route in the Houston to St. Louis
corridor that would be impacted? No. All he talked
about was the bidirectional problem and the capacity
problem, because they will be able to preserve every
single single-line route with the KSC divestiture
proposal.

Furthermore, divestiture is not an
unreasonable Government intrusion in the market place.
Whereas monitoring by this Board would be.

Monitoring conditions may have worked well
in the Wisconsin Central case, but such a condition in
a transaction of this magnitude is tantamount to a
bureaucratic nightmare.

Furthermore, it would be impossible to
determine at some later date whether certain rate
increases were a result of the merged power of the
UP/SP or a result of general economic conditions.

I believe if you put on a five-year
monitoring condition, you are getting this Board right
back into the pre-Staggers days of government
regulation, where every time there's a little problem,
everybody has to run into the government to ask for a fix. But there is a better way.

Congress made it clear in the Staggers Act, in the Interstate Commerce Determinatio... Act, that the best way to prevent anti-competitive conduct is to foster and preserve competition through structural conditions such as divestiture, and not impose government supervised regulations and oversight conditions.

VICE CHAIRPERSON SIMMONS: You are sounding like the Department of Justice.

MR. MULLINS: The Department of Justice wants denial. We don't want denial. We want divestiture.

VICE CHAIRPERSON SIMMONS: All right.

MR. MULLINS: Unlike applicants terminal trackage rights request to have the Government force KCS to allow BNSF over its tracks, despite private contracts to the contrary, divestiture does not result in the confiscation of private property at rock bottom prices as some have claimed.

In conclusion, the Board has a clear
choice in remediying the anti-competitive effects of this merger. It can accept the cumbersome ill-defined set of overhead trackage rights which will not preserve the competitive options for shippers. Or the Board can order divestiture of parallel track.

Divestiture is quick and easy, and preserves all competitive options for shippers. It provides a structure for continued competition without additional government intervention or the risk of some future tacit collusion.

Without divestiture, this merger should be denied.

COMMISSIONER GWEN: I was going to ask you at the start of your presentation, Mr. Mullins, to stand a little bit closer to the microphone.

(Laughter.)

MR. MULLINS: You have got to remember that this is my first time on this side of the aisle, you know.

VICE CHAIRPERSON SIMMONS: You have made some vague assertions about collusion in your brief. Do you want to enlarge upon that?
MR. MULLINS: There are two risks of collusion. One is future collusion, tacit collusion.

VICE CHAIRPERSON SIMMONS: But I mean has it already gone on? That's what you --

MR. MULLINS: I believe Mr. Rill would probably be the best person to answer that question, but we certainly believe --

VICE CHAIRPERSON SIMMONS: I have never seen you short of an answer.

MR. MULLINS: We believe that this Board, whatever, if there has been anything, and that by the way is how we proposed it in our brief, if there has been collusion, we don't think this Board should immunize in its 11341 power such conduct.

All we are asking for is a statement by this Board that its power does not immunize any conduct that may have otherwise --

VICE CHAIRPERSON SIMMONS: When you put it in that context, you almost say something has gone on. You leave that illusion that something might have happened.

MR. MULLINS: Well I think the facts are
in the record. We don’t have all the facts because we were denied discovery on some of those facts. But the facts are in the record. You can read the facts and make your own conclusion, Vice Chairman.

CHAIRPERSON MORGAN: You can make your own collusion.

(Laughter.)

CHAIRPERSON MORGAN: It’s late in the day.

COMMISSIONER OWEN: I would like to ask a question. I think it’s a fairly serious one. It was in Sunday’s Washington Post. I question if it was totally misquoted in this particular capacity.

Kansas City Southern’s President Michael Haverty is quoted as saying that the merger decision is going to come down to politics, and that big-time political forces have spent a ton of money on this.

These are very serious, inflammatory charges. Does Mr. Haverty have any evidence that this Board is being influenced by political forces? Have you any evidence that members of this board or staff of this board has accepted any money from the applicants or been influenced in any indirect way?
I think that's a very strong statement. I have been involved in the political process for 30 something years. I take very -- I am extremely disturbed by someone saying that in the news media here.

MR. MULLINS: I think he was not accusing the Board of some sort of political corruption. I don't believe that's what he was --

COMMISSIONER OWEN: Even the staff.

MR. MULLINS: Or the staff, for that matter. Believe me, I know this staff. They are a very professional staff. I worked for them for six and a half years, and they would not do anything like that.

COMMISSIONER OWEN: But you can carry it back to Mr. Haverty for me that I take exception to those remarks very much so.

MR. MULLINS: I think what he was saying, Commission Owen, was that this is a very politicized decision.

COMMISSIONER OWEN: Well this is the nation's capital. Naturally it's political.
MR. MULLINS: I think that’s all he was saying. I don’t believe he was trying to accuse the Board of any sort of political graft or corruption. He just would not say that.

COMMISSIONER OWEN: I think it’s wrong to even allude to that in the papers.

CHAIRPERSON MORGAN: Let me ask you about divestiture. When Con Rail was presenting their testimony, I asked them the same question, which is given your interest in this matter and given your interest in divestiture, and also your argument that we can’t really decide upon the BN Santa Fe trackage rights agreement because we don’t have enough before us to make that decision, why did you not file a responsive application?

MR. MULLINS: Well first, I would ask why didn’t the BNSF not file a responsive application or an operating plan or any of those types of things that you accuse us of not filing.

CHAIRPERSON MORGAN: I am not accusing. I am just asking.

MR. MULLINS: You are asking the question.
I would also say as a matter of pure law, Chairman Morgan, that if you look at the precedence of this ICC going back to 1986, any time somebody has filed a responsive application and there has been more than one party wanting that piece of track or that information, the Board doesn't pick and choose. The Board always goes out and says let the market place decide.

If that is going to be the precedent, which by the way is a precedent that we support and think is a good precedent, then what is my incentive to go through all of the costs and expense of filing a --

CHAIRPERSON MORGAN: Well Montana Rail Link obviously felt --

MR. MULLINS: And they are the only carrier filing in the central corridor. You would have had three or four carriers filing in the Houston to St. Louis corridor.

CHAIRPERSON MORGAN: That leads to my next question which is if there is that much interest in divestiture, then what kind of process are we looking
at and what kind of time table for resolving this matter?

MR. MULLINS: Sure. If you announce on Wednesday, if you come in here and announce Wednesday that you are going to order divestiture of the parallel lines in let's say the Cotton Belt corridor, let's say, UP and SP will, if they decide to go forward with the merger, they will be on the phone the minute that is announced on Wednesday trying to cut a deal with as many parties as they could to try to get divestiture quick and easy, because they want to consummate.

I'll bet you, you could have a divestiture order done -- by the time you announce your decision on Wednesday, you could have divestiture done, completed, another procedure done and over with in less than two or three months after the issuance of your August 12th decision. I'll guarantee it, because you can do that.

CHAIRPERSON MORGAN: If, as I indicated earlier, if one railroad ends up being the person to whom the lines are divested, is that going to make all
the other railroads happy?

MR. MULLINS: I doubt if it will make them happy, but that's what the market place is all about. The market will decide what carrier gets to be divested. You'll have a quick and easy, maybe two month proceeding in here where they will have their say. Everybody can have their say. This board can make a ruling on that.

But we're not talking six months. We're talking two or three months. You've got to remember, there's a whole 45 days in there between your announcement on Wednesday and the time you issue your decision where all the negotiating and all of that can be taking place.

I would also argue that divestiture is no lengthier in terms of details than trying to implement the merger itself. I mean this merger with UP and SP was going to take months, if not a year to implement. So how is that any different than trying to go through that process of implementing that than trying to do a two-month divestiture process while that process is going on. Thank you very much.
CHAIRPERSON MORGAN: Thank you.

MR. RILL: Chairman Morgan, and members of the Board, Vice Chairman Simmons, let me save you just one comment. You are going to say I sound like the Department of Justice, and I'm going to say guilty.

The principle message that I'd like to bring to the Board today is that the competition policy assessment that's been presented by the Department of Justice and remarkably I think with the basic logical fundamental concurrence of the Department of Agriculture and the Department of Transportation, is very much in the traditional mainstream of competition policy enforcement that has governed our market place in this country for at least the last 20 years.

I say that with deference to the special statutory mandate of this board with the deference to the expertise of this board and particular industries. But there is nothing in the statute and nothing in your predecessor's statutes that detracts from the fundamental notion that competition policy is an intricate essential element of the public interest.
Competition policy with respect to mergers is embraced in the 1992 merger guidelines that were issued. I had the privilege of being assistant attorney general for anti-trust when they were issued in the last year of the Bush Administration in 1992. They actually were a fine tuning, we like to think an improvement, on the merger guidelines that were issued in 1982 as Assistant Attorney General Bingaman said in the Reagan Administration.

Under each of the five prongs of the analysis of those merger guidelines which are generally applicable. They should be applicable in every industry. This merger would be considered to be bad, would be wrong, would be anti-competitive.

It creates undue concentration from three to two, to duopoly, even I would suggest to monopoly. The intricate inter-relationships created under this merger and the ability of the firms to have legitimate knowledge of each other’s businesses as conducive to non-collusive coordination which would constitute harm to consumers, to shippers. Entry barriers I think as the Board has acknowledged throughout the day are very...
high, very difficult. Efficiencies are achievable through other routes. We do not deny, as Mr. Mullins said, efficiencies exist in this merger. But they certainly do not outweigh the anti-competitive forces that would be set at large were this merger to be approved as proposed.

Finally, there's been much discussion about whether the Southern Pacific would go forward, what would happen to the Southern Pacific. I only recall to you Mr. Roach's opening statement. This is not a failing company case. This is not a failing company case.

So under each of the five prongs of the merger guideline analysis, which should be generally applicable to competition assessments in all industry, this merger goes down. DOJ with DOT and USDA applied the merger guidelines analysis, applied mainstream competition analysis carefully, I submit correctly. They got it right. You should disapprove this merger, at least order the divestitures suggested by the Kansas City Southern.

VICE CHAIRPERSON SIMMONS: Are you
concerned that the rates will go up as competition subsides?

MR. RILL: Normally when competition subsides, prices go up, yes.

VICE CHAIRPERSON SIMMONS: Ms. Bingaman didn’t answer my question about two railroads that are in the Powder River Basin.

MR. RILL: I wonder, was that from one to two or from three to two?

VICE CHAIRPERSON SIMMONS: It doesn’t matter what it is, there are two there.

MR. RILL: Well there are two there, but what was the pre-condition?

VICE CHAIRPERSON SIMMONS: And the rates have gone down.

MR. RILL: My understanding is the pre-condition was actually improved by the presence of two railroads, which is my understanding, it was a contributing factor to the rate decline.

VICE CHAIRPERSON SIMMONS: You are going to say that the presence of the UP is responsible for the rates decline?
MR. RILL: I would say that two is better than one. Three is better than two.

VICE CHAIRPERSON SIMMONS: I see. So four is better than three?

MR. RILL: Not necessarily. You would have to look at it in a given market context and figure out what the scale economies and the cost functions are. There is not a magic number except that in this analysis, in the economic studies I've seen supporting this analysis, under mainstream application of competition policy, three is better than two in this case.

It's not a magic number that can be generally applied across the board, but it is a functional element of appropriate competition policy analysis.

COMMISSIONER OWEN: That is an odd statement to make in a way, that three is better than two, because when you take Montana Rail Link or some of the short lines, one is better than three because there's not enough traffic.

MR. RILL: Well I said in a particular
factual context, and in this particular factual context, we don’t want to over-generalize. I agree with the Board we don’t want to over-generalize. In certain cases not here proposed, scale economies are such that one may be all that the market can handle. That’s certainly not even being argued in this case. There are admitted anti-competitive concerns here.

COMMISSIONER OWEN: I concur.

CHAIRPERSON MORGAN: I think that on the record, the question really is with respect to three to two, first off, whether that is indeed a situation of harm that needs to be addressed. Obviously the Justice Department and you all have taken one position on that. The Department of Transportation feels that the evidence is inconclusive as it relates to the three to two. It does not cause us to automatically conclude that three to two is an issue.

Two to one I think is where there’s more agreement that there’s an issue there that needs to be addressed. The question is, how much and how.

MR. RILL: Well certainly two to one is an
issue that would need to be addressed. We think the
parties proposals for addressing it is wholly
inadequate.

I think on mainstream merger analysis,
generally speaking, and I will generalize now, that
where scale economies will permit and market
conditions are such, three is better than two.

Then one has to go beyond that analysis
and look at the underlying facts in the case, and
determine whether or not that generality applies to
this particular situation.

The fact of the matter is, our area of
principle concern and the one that was addressed
primarily by Mr. Mullins and in our brief, the line
from St. Louis to Houston really is two to one.

VICE CHAIRPERSON SIMMONS: Well the one
reason I continue to talk about the Powder River
Basin, that happens to be the energy source for the
future for a long time for this country. That was why
when only the Burlington Northern was there, I was
very instrumental in being sure that the CNNW was in.

But I am here to tell you that I am
gratified that those rates have continued to decline. Now I realize there are many other factors in that, because you have two railroads in the east primarily, large ones.

MR. RILL: I haven’t studied the eastern railroad lines. Vice Chairman Simmons, I think if you moved from one to two, if you were instrumental in moving a competitive context from one to two, you should take great pride in that. I’m not surprised, without knowing what the other factors are, that rates did in fact go down.

VICE CHAIRPERSON SIMMONS: And the rates have gone down in the east.

MR. RILL: So I think you should be very careful that we don’t go two to one here.

VICE CHAIRPERSON SIMMONS: Well, I don’t think anybody is going to go from two to one.

MR. RILL: Well, that’s a question of --

VICE CHAIRPERSON SIMMONS: Have you got plans?

MR. RILL: We have no plans, but that’s a question of what is the viable competitive
alternative. At best, or the best solution is the one proposed for divestiture.

I would if I may, Madam Chairman, just like to come back to Vice Chairman Simmon’s question on collusion, because there is no charge of collusion being made by Kansas City Southern here today or elsewhere.

There is a question of examining certain events where discovery was blocked, and the very fact that one can not conduct discovery makes it obvious that one can not make a charge other than what may be based on full discovery. But that is not what’s here today. We are not suggesting that collusion has occurred for purposes of this or for any other purpose at this point.

Nor are we suggesting that anybody is going to get together in a smoke-filled room afterwards. We don’t have to. Because the fact is, that the functionality of this merger brings into close coordination, by virtue of trackage rights and other factors, obviously the relationships of Union Pacific and Burlington Northern.
No one is suggesting that that coordination in and of itself is an anti-trust violation. However, in the context of a merger, where two dominant firms meet each other daily, discuss trackage rights, discuss operating conditions, it is hornbook competition law that without any illegal act whatever, they can simply observe the rate setting, the service, the practices of one another that would make what we call duopoly or oligopoly coordination a lot easier than if that relationship didn’t exist.

That also is in the merger guidelines, but it’s basic economic theory. I can say as assistant attorney general, when I was in office, we were very concerned with those kinds of structural and relationships.

VICE CHAIRPERSON SIMMONS: Well I am concerned about it also. That is why I brought it up.

MR. RILL: I appreciate that, Vice Chairman Simmons. I hope that my remarks clarified that there are no charges of illegal conduct being made, but there is a grave concern over the structural conditions that would flow if this merger would
proceed as it's been proposed.

VICE CHAIRPERSON SIMMONS: I have no other comments.

MR. RILL: Thank you very much, Madam Chairman and members of the board.

CHAIRPERSON MORGAN: Thank you.

VICE CHAIRPERSON SIMMONS: That was a long two minutes.

MR. RILL: Good questions though.

CHAIRPERSON MORGAN: Next we will hear from Mark Sidman, representing Montana Rail Link Inc.

MR. SIDMAN: Madam Chairman, board members, my name is Mark Sidman. I appear before the Board today on behalf of Montana Rail Link. Seated to my left is the President of Montana Rail Link, William Brodsky.

MRL filed a responsive application in these proceedings in which it proposed that a newly formed entity called Acquisition Company acquire one of the two central corridor routes that would be owned by the combined UP/SP. The rail lines and rights covered by the responsive application are indicated on
the map before you.

There are three issues that I will address today. One, to preserve competition in the central corridor, the Board should approve MRL’s responsive application rather than ordering UP/SP to auction off one of its lines in that corridor.

Two, central corridor shippers strongly support the divestiture of a central corridor route to MRL.

Three, the United States Department of Transportation’s criticisms of the MRL proposal are unfounded and should be rejected by the Board.

You have heard numerous shippers and shipper groups argue today that BNSF operating as a trackage rights tenant will not provide effective competition in the central corridor. MRL agrees with those conclusions. Preservation of rail competition in the central corridor can be accomplished only if the shippers in that market are served as they are today by two owner operators.

In order to preserve the competitive status quo, the Board must impose a condition that
results in a divestiture by UP/SP of a central corridor route.

You can do this in two ways. Either the Board could approve the MRL responsive application or the Board could direct UP/SP to sell off a line to the highest bidder.

There are several reasons why the public interest will be best served by approving responsive application. First, an auction condition will put UP/SP once again in the position of trying to cobble together a transaction that passes Board scrutiny.

The Commission recognized in SF/SP that sending off a party to address the anti-competitive aspects of its own merger application is inherently suspect. The Commission in that case doubted that the applicants would place public benefits above private ones. There is no reason to believe that UP and SP would do so in this case.

The second reason for rejecting an auction condition is that it necessarily would involve a full blown second stage to these proceedings. A sale to an unidentified party that has not filed the responsive
application would delay consummation of the merger pending Board and public scrutiny of the proposed transaction.

MRL’s responsive application on the other hand, could be approved now, thereby allowing the public benefits of the merger to be realized immediately.

A third reason why the Board should approve MRL’s responsive application rather than imposing an auction condition is the existence of the settlement agreements between applicants and Illinois Central and Wisconsin Central. In the event of a divestiture order, these agreements presumably will result in one of those two carriers negotiating to acquire central corridor route. But the few criticisms that have been leveled at the MRL proposal, principally the loss of some single line service and operational issues in the Kansas City terminal, even if valid, would apply equally to Illinois Central and Wisconsin Central. Neither of those companies has a presence in Kansas City. Neither operates in California.