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basically the entire western United States.

Another measure is the volume of commerce affected. And by anyone's measure, what we're talking about is billions and billions of dollars. Our own estimate is almost $5 billion. The applicants are here asserting that this Board should be completely unconcerned about the creation of duopoly over this vast area, and they're making two arguments.

The first is that a reduction in the number of competitors from three to two has no effect on rail rates or service quality. And they're making a second argument. They're saying even if it does in general, in this case it doesn't matter here because the competitor being eliminated is the Southern Pacific Railroad.

The first of these arguments is truly astonishing, that there is no market benefit from a third railroad. Applicants in essence are contending that the fundamental laws of economics and common sense, really, don't apply here. Not surprisingly, the record in this case is quite to the contrary.

Cited in the record are numerous economic studies in many industries published in respected journals over the years which confirm that duopolies result in higher prices. Significantly, these studies include extensive empirical work in this industry, the rail industry.

These studies are listed in Dr. Majeur's verified statement, and they're discussed at considerable length in Dr. White's statement submitted on behalf of Kansas City Southern. Commissioner Owen, you mentioned this morning that there had not been a case where the merger to duopoly has resulted in higher rates.

I'd command your attention to Figure 3 in Dr. Majeur's verified statement. That's where he took the remark that Mr. Roach made this morning about rates falling in the wake of the MKT merger. What Dr. Majeur did was look at not whether rates fell in absolute terms, but whether the rates affected by that merger fell relative to the fallen rates generally in the rail industry.

And what Dr. Majeur found is that in the markets that were there to two markets that we identified in that case, that the rail rates did not fall as fast as the industry average. That is just as important as a nominal increase. The issue is does competition result in better rates and better service for shippers?

There's a case where it did. Union Pacific also points to the Powder River Basin saying injecting a second rail carrier lowered rates. Of course it lowered rates. The question is, will injecting a third rail carrier in the Powder River Basin also lower rates?

All of these studies repeatedly point to the answer being yes. Competition is not something you turn on and off. It exists with two, and it that's -- it doesn't get any better. It gets better and better and better. Three is better than two. Three is a lot better than two.

VICE CHAIRPERSON SIMMONS: Are you suggesting more railroads into the Powder River Basin?

MR. FINEST: No, we're talking about this merger. All I'm suggesting --

VICE CHAIRPERSON SIMMONS: I'm asking you.

I know what we're talking about.

MR. FINEST: No, I'm not advocating anything different for the Powder River Basin. The only position we're interested in preserving here is preserving the existing competition that is eliminated by this transaction. The state of competition in the Powder River Basin is where it is today, and we're not trying to improve that.

CHAIRPERSON MORGAN: But let me ask you about the Majeur studies. Is that how you pronounce his name?

MR. FINEST: Sure, yes.

CHAIRPERSON MORGAN: As I understand that study, it comes up with a figure of $800 million in total harm from this proposed merger. Is that --

MR. FINEST: That's right.

CHAIRPERSON MORGAN: And as I also understand it, out of that $800, roughly $270 million relates to two to one points.

MR. FINEST: Subject to checking the figures, but it's in the statement.

CHAIRPERSON MORGAN: Now, I also

understand that in determining that number, the assumption was that the BN Santa Fe trackage rights proposal would provide no competition at all. Is that -- that the BN Santa Fe would provide no competition at all. Is that accurate?

MR. FINEST: It's both an accurate assumption and an accurate fact. Trackage rights -- or at least for the two to one. Yeah, on the two to one, the assumption is what happens when you go from two to one. And that is giving nothing additional for the trackage rights. The more effect of the trackage rights --

CHAIRPERSON MORGAN: But I guess what I'm saying is that the BN's presence would have no effect. In other words, when you arrived at that number, you made an assumption that there would be no competition from BN Santa Fe presence. I'm just trying to understand. Is that correct? Is that a correct assumption in the study?

MR. FINEST: Well, yes, it is. But remember that the result of the BN Santa Fe trackage rights agreement is an increase in current rates maybe by more than the 10%. The study is not really examining the question of what happens when you replace a competitor with a higher --

CHAIRPERSON MORGAN: No, I understand that. I'm just trying to build into the assumptions here so that I understand what your assumptions are in arriving at the numbers.

MR. FINEST: Yeah, the math was just to multiply what is the expected price increase from going to two to one multiplied by the volume of commerce. That's all.

CHAIRPERSON MORGAN: Now, the other piece of the $800 million relates to the three to two points.

MR. FINEST: Correct.

CHAIRPERSON MORGAN: And in that, you assume rate increases in that traffic as shown in the study. You don't assume it, you arrive at a conclusion.

MR. FINEST: Correct.

CHAIRPERSON MORGAN: Now, that traffic -- a lot of that traffic is the intermodal automotive traffic, which is competitive. And so, I just would ask you, of the total amount of three to two traffic that you have looked at and the amount of harm that you have arrived at, how much of that is the intermodal automotive truck competitive traffic?

MR. FINEST: Well, I'm not able to break it down for you exactly. I know that it is contained in the tables. I can get that figure for you, and I'd be happy to provide it.

CHAIRPERSON MORGAN: I guess what I'm getting at is that in the three to two markets where you have indicated harm, to what extent do you account for the commodities where we know there is some competitive force out there already?

MR. FINEST: Well, to answer the question that you're asking, I would refer you to Table 4 in Dr. Majeur's verified statement. And you would have to figure out the percentages, but the intermodal and other traffic that he calculated is listed there. What I want to emphasize --

CHAIRPERSON MORGAN: So out of the $530 million -- I'm writing my numbers -- on the three to two points that you have concluded would represent the harm to those shippers, there is a portion of that that relates to intermodal and automotive and other more competitive traffic so that that number of $530 may indeed include shippers who are in a competitive environment and shippers who may not be?

MR. FINEST: No, no, that's -- that is wrong. If this traffic was included in this table, it is --

CHAIRPERSON MORGAN: Which I think it was. I think it was --

MR. FINEST: Some of it.

CHAIRPERSON MORGAN: -- in the traffic.

MR. FINEST: Some intermodal traffic is included. Some is not. The intermodal traffic that does face effective truck competition is not included. And it was a cut off basically hauls of 500 miles. Now, the average intermodal haul for traffic affected in the three to two markets is over 1,900 miles.

Now, I know there's some debate about at what length of haul does intermodal traffic stop being truck competitive and become rail captive. I've heard different figures. But if you look at the average length of haul, we are talking about a lot of traffic that is moving very long distances. Most of it is LA-Chicago.

That is not truck competitive traffic. That's rail captive traffic. It's included in the table. It should be there. The harm counts.

CHAIRPERSON MORGAN: And then the 500 miles, as I understand that assumption, is that beyond 500 miles, trucks are not competitive with rail. Is that --

MR. FINEST: That was the assumption of this study.

CHAIRPERSON MORGAN: -- the assumption.

MR. FINEST: You know, I know the record has some different estimates about where that cut off is. The point I want you to focus on is for the traffic that we included, we are talking about average hauls that are quite long, about which, for most of it, there really is no serious dispute about whether it's really rail captive or not.

For the length of hauls we're talking

about here, rail is significantly more efficient.

COMMISSIONER OWEN: There is competition, is there not, on that route there?

MR. FINEST: On LA to --

COMMISSIONER OWEN: LA to Chicago?

MR. FINEST: Currently there's three, that's right.

COMMISSIONER OWEN: Right. And so if there ends up being two, the competition is still keen. SP is not a competing factor in that right now, is it?

MR. FINEST: Well, --

COMMISSIONER OWEN: It's mostly intermodal, is it not?

MR. FINEST: Excuse me?

COMMISSIONER OWEN: Mostly intermodal going from Long Beach, Los Angeles ports to Chicago?

MR. FINEST: I don't have the exact traffic break down. I know there's a lot of intermodal traffic there.

COMMISSIONER OWEN: Yeah.

MR. FINEST: Southern Pacific carries --

the way to tell whether Southern Pacific is an effective competitor on that route is not to listen to what the applicants are saying to describe their service. The way to look at it is to look at their market share.

COMMISSIONER OWEN: What we're trying to do is look at it, and I'm asking you for the facts and figures. You're making --

MR. FINEST: 26%. 26% of the traffic in three to two markets Southern Pacific carries. That's our figure. Now that means -- and that's not an inflated figure. That's 26% of the time SP gets the business when shippers have a choice. When a shipper is trying to figure out should I use BN, should I use UP, or should I use Southern Pacific, 26% of the time the shipper decides my preference is Southern Pacific.

Now, you know, I've heard it's suggested this morning that Southern Pacific is a trivial or fringe competitor. What I want this Board to focus on is their market share. Their market share is, by our calculations, truly the third. They don't have a -- you know, a pro rate share.

But this is -- we are not dealing with a competitor who is a fringe firm. So that's the number to focus on.

VICE CHAIRPERSON SIMMONS: Well, you say that Southern Pacific is not as financially weak as the applicants say. Is that what you're saying really?

MR. FINEST: Well, I'm not going to characterize what the applicants have said, but I can say --

VICE CHAIRPERSON SIMMONS: Well, that's what you said in the briefs.

MR. FINEST: -- that Southern Pacific has -- is certainly a lot stronger today than it's been in the past. And in the last five years, it's increased its car loads, it's increased its net revenue miles.

VICE CHAIRPERSON SIMMONS: Well, how in the world do you think they can survive if you've got two large railroads putting in over a billion dollars per year? Where is that money coming from to make them a viable competitor?

MR. FINEST: I want to emphasize how

important it is not to look at the investments, but to look at the market shares, to look at what --

VICE CHAIRPERSON SIMMONS: That might be important for you. I want to know from you what you think about it.

MR. FINEST: About whether SP can compete against BN?

VICE CHAIRPERSON SIMMONS: Also, and that competition Burlington Northern and the Union Pacific are putting together over a billion dollars a year, and Southern Pacific's not going to do this. So what's going to happen to them?

MR. FINEST: Well, first of all, we're not sure what the Southern Pacific's going to do.

VICE CHAIRPERSON SIMMONS: What do you mean?

MR. FINEST: I say we're not sure what the Southern Pacific's going to do.

VICE CHAIRPERSON SIMMONS: Well, are you going to get some more real estate for them to sell?

MR. FINEST: They certainly have a lot of real estate right now, and --

VICE CHAIRPERSON SIMMONS: What are you going to do when it runs out?

MR. FINEST: Right now, they are -- they have positive operating income. That's a key fact. They are making money on operations.

VICE CHAIRPERSON SIMMONS: So you tell me it's going to be like that in the future, is that correct?

MR. FINEST: Well, the future is the question. But there is nothing that indicates that Southern Pacific has a bleak future at all. There are --

VICE CHAIRPERSON SIMMONS: I cannot understand how the Department of Justice can come to this conclusion.

MR. FINEST: Well, there's two things -- two pieces of evidence that I'd like you to consider on this issue, Vice Chairman Simmons. The first is the recent financial history of the Southern Pacific.

VICE CHAIRPERSON SIMMONS: Yes.

MR. FINEST: Look at their balance sheet and their income statement. And the --

VICE CHAIRPERSON SIMMONS: Are you buying or selling?

MR. FINEST: Pardon me?

VICE CHAIRPERSON SIMMONS: Are you buying or selling?

(Laughter.)

MR. FINEST: I'm commenting. But there are lots of people who have expressed an interest in buying, and that's the second piece of evidence I want you to consider. These are valuable --

VICE CHAIRPERSON SIMMONS: Eyeing the total railroad or pieces of it?

MR. FINEST: Pieces of it.

VICE CHAIRPERSON SIMMONS: Okay.

MR. FINEST: There are valuable assets of the Southern Pacific that other carriers are interested in buying. That shows us two important things. One, that it is indeed very possible to compete against the Burlington Northern. People are lining up, paying money for the opportunity to do it.

Second, it means that these assets are valuable and they won't be shut down. It means that these assets will be -- remain in operation. They'll have employees running them. These assets are not like a plant that closes down. These rail assets are not leaving the industry. The only question is, who is going to operate them?

VICE CHAIRPERSON SIMMONS: Listen, if you don't continue to buy equipment and keep your tracks up all the time, you're doomed for failure. And that costs money. Where is the money coming from? That's what I want to know.

MR. FINEST: Southern Pacific has a couple of options. One, they can walk away from this deal and decide that they are once again interested in investing in their own future through real estate or loans. They have available credit to them. Two, they can make a second deal with any of the railroads that are also interested in buying their assets.

They can make another deal with the Union Pacific that doesn't raise these kinds of problems. We've talked about the I-5 corridor and what the benefits that might come from that transaction are. SP and UP could go out and make that deal tomorrow, and this Board would probably not have a problem with that. I certainly don't think I would.

VICE CHAIRPERSON SIMMONS: You're advocating it then, is that correct?

MR. FINEST: I think the part of this deal that doesn't involve the anti-competitive effects are fine. Now, we've seen a lot of mergers in this industry, and most of them we have not opposed. Most of them have created great benefits.

VICE CHAIRPERSON SIMMONS: I think we've seen a few more railroad mergers than you have though.

MR. FINEST: I've been around a while, but I'm sure that's true.

COMMISSIONER OWEN: I've been around longer than you have.

MR. FINEST: But the point here is that the -- most of the railroad mergers are not anti-competitive like this. We have not opposed most of them. Or where we have, they've been, you know, narrow points where basically end to end transactions have minor competitive problems for the most part. Our analysis and this -- well, at least your predecessor -- our analysis dovetailed pretty nicely.

I mean, there's always differences around the margin. But wherever we thought a merger was beyond the pale and shouldn't be approved at all, your predecessor agreed.

CHAIRPERSON MORGAN: Let me follow up on a question that he had, and that relates to SP.

MR. FINEST: Yes?

CHAIRPERSON MORGAN: If this merger were not approved, as I believe your position is, it is possible that SP would then be sold in pieces. Yes, there are options, but that is clearly one of them -- could occur.

MR. FINEST: If the current owners think that's going to make them the most money, that's what they'll do.

CHAIRPERSON MORGAN: Now, obviously right now SP -- we can have a lot of discussion about what its financial condition is, but clearly SP is struggling in the market right now and is having trouble competing in certain markets. If SP were sold in pieces, wouldn't you have the same problem as SP is having right now?

MR. FINEST: Well, when someone makes an offer for part of a firm, they're usually saying I can make better use of those assets than you can. That's why I can pay you enough money to get them. So, you know, if somebody like Con-Rail bought part of Southern Pacific -- you know, you heard Mr. Roach this morning.

His big concern is he was going to lose a lot of traffic if Con-Rail bought it because Con-Rail would create single line service from the Cotton Belt area all the way to the northeast. I mean, that's the same benefit he's claiming for his railroad and yet, you know, he's here telling you that's terrible.

What I'm suggesting is if somebody wants to make a more attractive bid for these assets or the whole company -- it hasn't been marketed. We don't know what's going to happen. If Southern Pacific's current owners decide that they really want to get out of the business, they're going to take the best deal they're offered.

Right now, the best deal they've been

offered is the most anti-competitive purchaser available. No wonder that's their first choice. I'm sure Union Pacific is willing to pay them a lot more money for their assets than a pro-competitive purchaser, but that ought not concern you folks. The rule for you is to protect the public interest.

Don't let these assets disappear. Don't let them be purchased by the -- virtually the only purchaser in the entire country that can create a problem like this. They could sell the entire company to virtually anyone else without creating these problems, without creating these harms.

What you should do is not accept these invitations to wander into this quagmire of partial approval and regulatory oversight and future divestitures and five proceedings in the future that Mr. Roach talked about. Just tell them no. They understand what they can and can't do.

Make them go and make their next best deal.

VICE CHAIRPERSON SIMMONS: Is that what the Department of Justice does?

MR. FINEST: You bet, you bet. That's what we do, and then we -- what normally happens is parties come back, we have a consent decree, there's a divestiture. They get the rest of their deal through. Happens very quickly, and no one complains about the process. That is, I think, an excellent model for this Board. Just tell them no.

Make them come back with a deal that's acceptable. There are plenty of deals that are acceptable.

CHAIRPERSON MORGAN: Well, you mentioned that there might be another person out there that would step up to the plate and be willing to purchase SP.

MR. FINEST: Sure.

CHAIRPERSON MORGAN: But that clearly hasn't happened other than the transaction that we have before us. And of course, the marketplace --

MR. FINEST: And it won't happen.

CHAIRPERSON MORGAN: The marketplace, of course, generates this kind of transaction, and that's good because we want the marketplace to act in a positive way. And so, we allow transactions to come forward, but I just would say that it's not that easy. We don't have four or five on the record applications for purchase of the total SP.

MR. FINEST: With all due respect, Chairman Morgan, I think you're trying to find a -- you're trying to broker a deal here. What you should be focusing on is your statutory --

CHAIRPERSON MORGAN: I don't think I'm trying to broker a deal. What I'm trying to understand is taking your position and trying to understand where it leaves us. We are responsible for transportation.

MR. FINEST: Correct.

CHAIRPERSON MORGAN: And I need to be responsible and so do my Board members when making a decision and figuring out where it will lead us. If we do X, it will mean Y. If we do Y, it will mean Z. That's all I'm asking. And I'm trying to understand taking your position and working it through the system.

MR. FINEST: Okay, I understand. And I

think all I'm suggesting that -- you know, the record here is clear. When you write an opinion, the problems with this transaction can be made crystal clear. And you know, the applicants already know where the biggest problems are. And then you just deny the application.

They can take that information and they can restructure an acceptable proposal. You don't get involved in divestitures. You don't get involved in regulatory oversight. You don't get -- you don't become a rate regulating body for all of the rates west of the Mississippi River. And that would be consistent with what the Staggers Act wants this Board to do.

CHAIRPERSON MORGAN: Of course, the opposite view is that that kind of process would further delay what the marketplace seems to be dictating. And that is, of course, as you and I both know, something that we struggle with, which is to not interfere with what seems to be a legitimate marketplace response to whatever is out there.

So that --

MR. FINEST: When you're thinking about that point, here's what I want you to think about. That the most anti-competitive deal will always be proposed first because it's the most profitable. So when you say the marketplace is, you know, serving up this transaction to this Board, that's to be expected.

I mean, that's how we get the transactions that are the problem transactions. We almost always find that when we order a divestiture, the selling price of the divested assets represents more of a competitive price for those assets. It represents the value of those assets in a competitive market, not in a monopoly or duopoly market.

The purchaser here, UP, is always willing to pay a sum that represents the discounted value of a future stream of super competitive prices. That is why you should not assume that this is a market response. It's a market response that restrains competition. That is the point you should focus on. You should be looking for the transaction that will not create competitive problems, and there are a lot of them out there.

And there are a lot of transactions out there that will create many, many great efficiencies. SP could do an end to end deal with a number of carriers. Those are very efficiency enhancing, and it's -- you know, it's the kind of deal that Mr. Roach fears precisely for that reason.

He doesn't want to see that happen. His railroad doesn't want to see that happen. They want to merge with a competitor. Everybody wants to merge with a competitor. Your job is to tell them no. You can't merge with a competitor unless the efficiencies are so great that the transaction on balance is worth taking the competitive hit.

That is not the case here. The competitive hit from this transaction is the largest ever proposed. A horizontal merger of this nature -- it's inconceivable to me that somebody would propose this under the anti-trust laws. And it's not because they're afraid of the Department of Justice. It's because they're afraid of a federal district judge applying the law.

That is the same concern that this

industry should have about this Board, that they can't pull something like that on this Board because you are concerned about the competitive implications. That's the role that I think this Board should take. It's what Congress expects you to take in forming the STB. And it's what the authors of the Staggers Act had in mind.

They want competition. And the way you preserve competition is two things. Deregulate where you can and enforce competition rules where you must. That is what should be done with this application.

COMMISSIONER OWEN: I'm fascinated by your knowledge of the transportation industry, Mr. Finest. I'm also fascinated by one of your policies at the Justice Department that you always deny the first deal that comes into the door as one of your statements earlier.

MR. FINEST: Excuse me?

COMMISSIONER OWEN: And so -- and one of the other things, what you're talking about here is fragmenting an industry here or potential merger or rail line as SP. And I get a little concerned about that, because when you fragment a rail line like the SP and sell it off part and parcel to a multiplicity of different entities, then what you do is you have interchanges, switching and different things like this transloading or whatever.

So you drive the shipping cost up. So a through system seems like it would be better, whomever bought it. I don't know. And I'm not certain. I don't know the dollar value of whether this is a good deal or not. It must be, or these people wouldn't be putting up the money they're doing -- I mean, they're putting up.

One of the things I'd like to address though is one of your witnesses, Dr. Kicherson, was a witness in the Burlington Northern/Santa Fe merger, I believe. He disagreed with the projected savings that would result from that merger, and Justice was very emphatic in that also. But in fact, the savings originally projected by the applicants seem to have been understated.

Why then should we believe this same witness with regard to the projected savings in this case? Now, you're saying all of these things here, and it's based on some of his figures here. And I'm also -- I'm sure, and also Ms. Zimmer and also Dr. Majeur, is it?

MR. FINEST: Majeur.

COMMISSIONER OWEN: He pronounces it right. He just can't spell.

COMMISSIONER OWEN: Okay. But on that -- so we had about a billion four swing there. I think he was estimating an economic loss of maybe $700 million, and the proponents were estimating a benefit of maybe $700 million plus or something in that neighborhood.

And then, if I just go on -- and I won't belabor the point here because I think you've illustrated it fairly well there -- another of your principal witnesses, Dr. Majeur -- has Dr. Majeur been witness in other railroad merger cases, and how long ago did he -- Dr. Majeur complete his education, and what is the extent of his private sector experience, especially in a relevant case such as this?

I just thought it would be of interest to us because someone that states that trackage rights are not relevant at all in their presentation, I seriously question that. And trackage rights have been around for quite some time and an awful lot of railroads use them reciprocally and so forth.

And so I was just saying we've had two cases here of two individuals who have been pretty well misstated. And so, -- and if it went that way with Burlington Northern and Santa Fe, then why we should be so excited about what you're doing now.

MR. FINEST: Well, I think there's a big difference between the Burlington Northern/Santa Fe --

COMMISSIONER OWEN: Maybe, but not in the people that prepare the figures. That's what I'm getting at. See, there might be differences in the two applications as such, but not in the people that prepare the figures is what I'm getting at -- in the studies.

MR. FINEST: The -- regardless of if the Burlington Northern/Santa Fe efficiencies were overstated, it really didn't matter that much because the competitive problems were relatively narrow and easily fixed.

COMMISSIONER OWEN: A few hundred million dollars, it doesn't matter?

MR. FINEST: It didn't matter to approval or not approval. That's the point.

COMMISSIONER OWEN: Okay.

MR. FINEST: If there's not much harm, it doesn't matter that, you know, there's not much -- not as much benefit.

COMMISSIONER OWEN: I'm a businessman and I run apartments and manage them. And I just can't figure out why $100 million dollars doesn't matter. It's -- I'm not accustomed to Washington yet, I guess.

(Laughter.)

MR. FINEST: My only point is the -- when you're saying that the efficiencies are over stated, it -- you know, in our view, the Burlington Northern/Santa Fe merger had significant efficiencies. It did. It was largely end to end. Our concerns with it were quite limited. They were focused on a number of very discreet markets. We certainly didn't oppose the transaction outright.

We certainly didn't, you know, appeal from the ICC's decision. You know, we had some disputes or certainly some concerns about the trackage rights compensation structure in that case, and they're the same kinds of concerns we have now. And now we have a lot of company because there's more people who are affected by it.

In that case, you know, we were kind of by ourselves. But what we -- the question is not who's saying it. The question is, is what they're saying true? And the problem with these trackage rights is that they really don't restore the current level of competition. They're just not nearly as good as owning your own track.

You know, you're always the visiting team.

CHAIRPERSON MORGAN: We did approve those in the most recent merger, and I -- we don't have any evidence that they are not working in that. And this was a significant number of miles in that case as well.

MR. FINEST: Well, I think you -- what you ought to look at is what has happened to prices on the trackage rights. I know there's only anecdotal evidence in the record, but even on the trackage rights in this case, as I understand it, Burlington Northern has been out and not exactly bidding aggressively for their prospective service on the trackage rights at issue here.

And in the BN/Santa Fe case, I have heard anecdotal -- strictly anecdotal complaints about, you know, the level of competition over trackage rights. I think you should be very concerned about those things. These applicants are asking you to take a huge gamble here. And you're being asked to approve trackage rights that are unlike -- really substantively unlike any that have ever been approved.

We are talking here about, you know, dozens, hundreds of shippers, switches, access, local access. These aren't just overhead rights. These are situations here you have to get full cooperation from your landlord. The opportunities -- the opportunities for a landlord to discriminate against a tenant are immense here just because of the high level of service for switching in and out.

You ought to be concerned about that. And to protect against that, to prevent discrimination against the tenant, look at what has been proposed. I want you to look at --

VICE CHAIRPERSON SIMMONS: Your answer is just to say no, and that solves it.

MR. FINEST: I -- that is the way that you solve the most problems, the most -- very quickly. And you'd be faithful to the mandate of Congress in doing what it expected to happen in this industry, not to have anti-competitive mergers take place. This Board's here to make sure that happens. And that's what I think is your best move, absolutely.

CHAIRPERSON MORGAN: Well, I guess -- I don't necessarily see it that simply. But I mean, I think that you have shippers who are for this merger. You have shippers who are against this merger. You have efficiencies in this merger, you have competitive harm in this merger. And our job is to balance all of that and to look at the benefits and to look at the harm, to put a package together, and to figure out how it comes out in the end.

That, to me, is a delicate process. It is not an easy process. We wouldn't be here today with some 400 parties of record and a voluminous documentation on this case if it weren't a little bit more complicated than the obvious. And I respect your position, but there's a lot here that not easily leads to a conclusion, which is why we're here.

MR. FINEST: The one thing I would ask you when you are striking that balance of efficiencies versus the competitive harm, focus very closely on the issue of whether the efficiencies that you're putting on one side of the scale require -- require the competitive harm. And think about the I-5 corridor. There's a big chunk of efficiencies that could be gotten with no competitive harm.

So the test -- and the test that the ICC has set forward is the efficiencies to count have to be merger related. They have to be achievable only by taking the competitive hit. I can't stress it --

CHAIRPERSON MORGAN: I think your -- is it Christensen -- indicated that he assessed the efficiencies in this case at somewhere around $70 million, is that right?

MR. FINEST: That's his lower bound. I mean, he gave --

VICE CHAIRPERSON SIMMONS: He was quite wrong on his assumptions about Burlington Northern/Santa Fe.

MR. FINEST: Pardon me?

VICE CHAIRPERSON SIMMONS: He was quite wrong in his assumptions, if he's your expert on efficiencies as it relates to the Burlington Northern/Santa Fe. He says categorically that mergers just don't result in any efficiencies, especially the mergers of the 1980's.

MR. FINEST: Well, that -- I think that many of the efficiencies of the mergers are overstated. I think most of the efficiency gains have come from deregulation.

VICE CHAIRPERSON SIMMONS: Burlington Northern and Santa Fe is an up to date example. I mean, he said there wouldn't hardly be any. And here they've got over a billion dollars worth of efficiencies. But he's your expert.

MR. FINEST: Yes.

VICE CHAIRPERSON SIMMONS: Okay.

COMMISSIONER OWEN: I have one other --

MR. FINEST: Yes, sir?

COMMISSIONER OWEN: I just wanted to clarify though -- earlier, I think, one of your statements was that the Department of Justice -- I don't know if it necessarily suggested, but it indicated there was real estate assets that -- Southern Pacific can continue to sell real estate in order to meet its financial obligations.

And I guess my question would be, is the position of the Department of Justice that hocking the silverware is the appropriate means to support a lifestyle rather than bringing income in line with the expenditures? Because they've sold $2 billion dollars already.

MR. FINEST: My position is that the owners of property ought to be permitted to do with that property what they want subject to the anti-trust laws.

VICE CHAIRPERSON SIMMONS: Say no.

CHAIRPERSON MORGAN: Just say no.

(Laughter.)

Anything else? Thank you very much, Mr. Finest.

MR. FINEST: Thank you, Madame Chairman.

CHAIRPERSON MORGAN: Now if I could step out of the order just for a minute, I believe that Governor Michael Leavitt is here from Utah -- just flew in, I understand. So if we could just step out of the line and allow the governor to come up and make his presentation.

GOVERNOR LEAVITT: Thank you, Madame Chair and commissioners. There's no such thing as just flying in from Utah.

(Laughter.)

CHAIRPERSON MORGAN: Well, that's not our jurisdiction now, but we won't get into that.

(Laughter.)

GOVERNOR LEAVITT: Whoever said you can't get there from here -- actually, it's of some importance, I suspect, that I let you know that I got up at 4:00 this morning in order to come.

VICE CHAIRPERSON SIMMONS: Thank you.

GOVERNOR LEAVITT: And I came not so much to elicit your thank you, but let you know how important this is to our state.

CHAIRPERSON MORGAN: Well, I was up at that hour, but not -- for other reasons.

GOVERNOR LEAVITT: I would also like you to know that I'm here representing not just myself, but I am here representing as well our legislative leadership, our congressional members unanimously, and also I am here representing what I believe to be a lot of small shippers and a lot of people in the future who at this point haven't even contemplated the fact that they may be wanting to do business in the state of Utah.

We among the delegation and legislative leadership are united in the position that I'll present today, and I'd like you to know that I'm here on their behalf as well.

I suspect that I am probably the only governor that you'll see today, and there's a reason for that. We occupy a very unique position in this whole transaction. We are, I suspect, one of the only states, if not the only state, that this would result in -- with the exception of one small piece of a specialty railroad called Utah Railroad, all of the railroad assets that are in the state would be owned by one company.

If this transaction is not handled properly, it undoubtedly goes without saying that we would suffer as a state immeasurably and that we would suffer permanently. Our state's economy in the future, I think, is directly tied to the handling of this transaction. The state of Utah is the state of incorporation for the Union Pacific Railroad.

We have enjoyed a long, fruitful and amiable relationship with them and continue to do so. Southern Pacific as well has been a corporate citizen in our state, and they have represented a vigorous competitor in our market.

VICE CHAIRPERSON SIMMONS: How about the Utah Railway?

GOVERNOR LEAVITT: The Utah Railway is as well a respected a citizen and taxpayer.

CHAIRPERSON MORGAN: Taxpayer first.

GOVERNOR LEAVITT: And they as well are -- play a significant niche role in one industry. There's on my desk -- or on my credenza, there is a little memento. Every year we celebrate in our state the anniversary of the driving of the golden spike, which I will remind you took place in Utah where the transcontinental railroad actually was finally united.

Some irony, I suspect, with the Union Pacific and a predecessor railroad, the Central Pacific, met at that time. Let me go directly to the bottom line for us. I've had some sense of the feeling you expressed with the complexity of all of this, the fact that there are benefits and there are potential disadvantages and trying to weigh all those.

We've been going through them for months. Here's how we come out. Utah supports the merger if it is conditioned in a way that will protect us from the prospect of our unique problem. If we were not able to condition the merger in a way that would protect us, it is not a transaction we could support for the reasons that I've already outlined.

In the perspective of decades, as I suggest, this may be one of the most important things economically that occurs in our state. First let me acknowledge the pluses that we see on this transaction. It's clear that there are some efficiencies and that there are cost savings, and that we would benefit from that.

And for that reason, I know we have enthusiasm. It's also clear to us that there is some question as to the viability of Southern Pacific financially on a going forward basis. We accept the merger as benefitting our state because of those reasons.

Now, I would like to just make this point, that we come today really looking -- having stated our support, we come today looking for help from you. If there was ever a circumstance that the role of this Board was designed to protect, it would be a circumstance such as this.

COMMISSIONER OWEN: Does it have anything to do with state's rights?

GOVERNOR LEAVITT: A subject for a

different day. Our purpose is -- years ago, we had four railroads. It went to three and to two; and with the exception of the Utah Railroad, which plays that unique niche, we will be to one owner. And so we think that there are some things we need to do in order to make this workable and so we can get the benefits that you alluded to and protect ourselves from the necessary down size.

Let me review with you the three things that we would like to request that you condition the approval of this merger. The first one is the price of the trackage rights. Currently the trackage rights agreement calls for them to be three mills. UP indicates in our extensive discussions with them that they believe that covers their allocated costs in total.

Before I entered into public service three years ago, I was in business myself. I think I understand allocated costs. It's pretty clear to me from my discussions with them that if we were to reduce that to two and a half mills, that it would not in any way adversely affect the benefits of this merger to them.

And it would accomplish something that is vitally important to us, and that is to create -- and it's the bottom line for us -- is to just create a competitive environment where a competitor can in fact be successful. That's the first point, reducing the trackage rights to 2.5 mills.

The second would be to -- we believe that because you would be now dealing in an environment with essentially one owner that there is a higher duty owed by that company, and that we believe that the shippers need to have some fall back surrogate for competition, something that would emulate competition in the -- if it did not occur the way it is planned.

Now we -- some of our thoughts would be that perhaps the railroad ought to pay for an audit that would by -- on an annual basis -- that would under similar products in similar distances allow a comparison with other markets where there was viable competition.

And if, in fact, there was some -- if in fact comparing similar markets -- rather, similar products, similar distances, disparity and they were going up faster -- I'm talking now about percentage of increase going into the future. We recognize there are all kinds of reasons that you can differences.

But if you take similar products, similar distances from one market to the other and compare the increases, we think that that would then have the ability for either the state and/or the shippers to be able to go back and get a refund based on the fact that it's going up faster.

That would give us a surrogate or some sort of -- some way of emulating the competitive forces that would normally hold it down, allow us to have the benefits of the merger, but at the same time give us some protection if the competitive environment that is believed to be out there isn't.

Now, if you wouldn't mind, I'd like to pause and tell you why that's of real concern to us and why we think both of those elements are important. We believe at 2.5 mills that there will be a competitive market. However, there's lots of things that go into whether someone comes to a market to compete.

A week or so ago, I ended up at a dinner with my colleagues in the west with representatives of the Burlington Northern and Santa Fe. And we had quite a discussion that I think was instructive. They said we're looking forward to coming to your state to do business. I said well, great, where have you been? Four months ago, you said you'd come out and find out if in fact there was a market.

I know of one competitive proposal in four months that had been made. Well, we've got a lot of the things going. We're trying to work through our other merger. I said that's fine, but my competitive future is at stake as a state. I need to know if you're going to be a viable competitor. I don't doubt that they're very capable.

Well, we started talking about the question of whether or not there ought to be a financial stake. Well, we're concerned about having a financial stake because we've got $2 billion dollars we've got to invest somewhere else. Well, you know, I spent a long time in business, and I know that a lot of times you put your efforts where your investments are.

And so there's got to be some way -- and in fact, I spent the first years of my professional career living on commission. And I know what competition looks like.

VICE CHAIRPERSON SIMMONS: Your Honor, what kind of business were you in?

GOVERNOR LEAVITT: I was in the insurance business. Not the railroad business, but the insurance business. We owned a group of agencies all over the west. The point is that we need to have some way of emulating competition if it doesn't materialize for reasons that are unconnected to the rates.

Now we think that it will, and we think that there are good, solid benefits to be defended, and we support the merger. But we need to have these conditions in order to create the balance that, Madame Chair, that you spoke of.

Now the third condition is that we believe that the five years oversight that the -- is now being proposed by this commission is inadequate and that it would be valuable to have that extended to some period beyond that, say 15 years, where you would have the ability to -- if necessary, to deal with this.

Let me just summarize. All we really want here is a fair, competitive market. And because we're dealing with a unique situation, we think this calls for a unique solution. In summary, we think that being able to reduce from three to 2.5 mills is an important part of it. Secondly, some mechanism to emulate competition if it does not -- again, all we want is a fairly competitive market.

And third, we think that lengthening the oversight period would be of value and importance. This is a unique situation in our state. And we support the merger, but only if we can find a way to take care of that uniqueness and protect us. And we think at that point we will have achieved the balance, Madame Chair, that you spoke of.

I'd be happy to respond to any questions that you have.

CHAIRPERSON MORGAN: Now, the three conditions, the second and the third sound somewhat similar. In other words, the second is basically coming up with some mechanism to ensure competition over the long term.

GOVERNOR LEAVITT: To emulate the benefits of it. In other words, if we can't have it in our jurisdiction, let's take another area where it does exist and use that as a surrogate for us. And then if there is in fact a problem in ours, it would be reflected there and our shippers would receive the benefit of that oversight.

CHAIRPERSON MORGAN: And then the oversight would be our oversight to ensure --

GOVERNOR LEAVITT: I suspect that could be true for part of the time or for all of the time. It seems -- personally, I think this -- in fact, I ought to clear this up. This condition's going to last for a long time. It's very possible it could be in effect 20, 30, 40 years from now. So we need to have whatever part it is that's emulating competition go on forever.

Now, whether or not you need to maintain jurisdiction over that is probably a different subject. It may be that the jurisdiction of your -- or the limit of -- there may be a need for a limit -- it may be possible to limit the length of time in which you have jurisdiction but have that part of the agreement go forward.

VICE CHAIRPERSON SIMMONS: Does the Utah Railway agreement allay some of your concerns?

GOVERNOR LEAVITT: Again, I'm pleased that the Utah Railway --

VICE CHAIRPERSON SIMMONS: The Burlington Northern --

GOVERNOR LEAVITT: -- has reached an agreement, because I think in that one industry, in that one area, --

VICE CHAIRPERSON SIMMONS: I didn't expect you to be out against them.

GOVERNOR LEAVITT: Good. They're taxpayers you remember.

VICE CHAIRPERSON SIMMONS: Yes.

COMMISSIONER OWEN: In your second point there, competition valuation or emulate benefits, does that mean to say then that Utah will assist all of us folks out in Orange County and the people in California where you've stole all of our business?

(Laughter.)

GOVERNOR LEAVITT: I tell Governor Wilson we need the California economy to improve for two reasons. The first is that we depend highly on the spin off economy that you get. And besides that, we haven't got room for everybody in Utah.

(Laughter.)

COMMISSIONER OWEN: During the winter seasons everybody in Park City -- but shouldn't the price paid for trackage rights equal the cost of damage similar to heavy trucks causing pavement damage and all of this? And Burlington Northern/Santa Fe should pay equal to whatever -- I don't know if 2.5 mills or whatever trackage right price there per ton mile or whatever -- I have no idea whether that's fair or not.

GOVERNOR LEAVITT: Well, it appears to us to be the right number where first of all they can compete. And frankly, because you got -- this is a large deal and a large merger. It benefits a lot of people. And we've got this one unique position, and we've got to find some way to assure that we're creating competition.

And we don't think that it in any way creates a disadvantage for Union Pacific. They can -- I think they could charge that. According to the people we're talking to and our economists, they think they can do that and move forward. I know they maintain it's three, but I think they could do it 2 1/2. And it would help create the sense of competition.

There is a need for a higher duty here when you've got one company owning all of the assets. And as I suggested earlier, if there was ever a time when the nature of the duties of this Board come to bear, this is it. We need you to help us through this. We need the -- we think the merger is an extraordinarily good opportunity for a lot of people, but we need to condition this in a way that takes care of this unique problem.

COMMISSIONER OWEN: Have you sat down to negotiate with Union Pacific?

GOVERNOR LEAVITT: I have spent a lot of time with Union Pacific. They are good corporate citizens. I know them well. It's become -- whether you'd call our discussions negotiations, I don't know; but we've come to this conclusion. Whether they agree with it, I'm not 100% sure either. But that's our position.

COMMISSIONER OWEN: My basic philosophy is that you try to do everything in the private sector that you possibly can when --

GOVERNOR LEAVITT: That is in fact mine, Commissioner, and I think we're presenting here a means of emulating private sector competition that will give us the capacity to emulate it if we don't have it. We're not asking for a regulatory scheme here. What we're asking for is an emulation or a surrogate for competition that may not -- I say may not.

Everybody believes BN's going to come in and be a vicious competitor, and I hope you are. But if they don't, we've got to have a fall back position.

COMMISSIONER OWEN: Appreciate it.

CHAIRPERSON MORGAN: Anything else?

VICE CHAIRPERSON SIMMONS: No.

CHAIRPERSON MORGAN: Well, thank you very much for coming. I know this is of great interest to you, so I appreciate you being here to --

GOVERNOR LEAVITT: It is of significant interest. Thank you very much for receiving me.

CHAIRPERSON MORGAN: -- help us with this important decision.

GOVERNOR LEAVITT: Good, thank you.

CHAIRPERSON MORGAN: I hope it takes you a little shorter time to get back home than it did to get here.

GOVERNOR LEAVITT: Well, the fact that our time together did not last long may mean I get home tonight. Thank you.

CHAIRPERSON MORGAN: Okay, if we could return then to our regular schedule. We next will hear from Michael Dunn from the Department of Agriculture. The Secretary would have wanted to be here, but Michael Dunn will be replacing him today. Michael, you have five minutes.

MR. DUNN: Thank you, Madame Chairman. I'm Michael Dunn. I'm Assistant Secretary for Marketing Regulatory Programs for the Department of Agriculture. I have accompanying me here today Lon Hontemia, who is the Administrator of Ag. Marketing Service; and Paul Clepner, who is from the Marketing Transportation Division of Ag. Marketing Service.

And I'd like to thank you for the opportunity to allow us on behalf of the Secretary of Agriculture to put in our response to the proposed merger between Union Pacific and Southern Pacific. Because of the Agricultural Adjustment Act of 1938, the Ag. Marketing Act of 1946, the Secretary of Agriculture is charged with initiating and participating with the Surface Transportation Board in proceedings involving rates, changes, tariffs, practices and services.

We filed comments in these proceedings on three previous occasions to raise our concerns about the potential impact of the merger and ultimately to oppose the merger as presently structured. In our earlier comments, we highlighted the importance of competitive rail service for agricultural producers, shippers, and the entire rural economy and concerns about the long run effects of the continuing consolidation and concentration in the rail industry.

I might add we've just had a study on concentration. And outside committee, advisory committee, and the Secretary of Agriculture -- they felt so highly about the loss of competition in the rail service that they had a special spin off report in that concentration report to the Secretary.

It was just given to us on the 6th of June. And on March 29th, finally we suggested that there was a need for a third major railroad to operate in the important corridor connecting the grain producing regions in the lower plains with ports along the Gulf of Mexico. In our April 29th filing, the Department concurred and supported the Department of Justice conclusions that rail competition in many western markets would be substantially reduced if the proposed merger were approved.

The merger would leave only two major railroads operating in the western United States. It would reduce competition in the central corridor between Kansas City and the west coast. Again, we ask the Surface Transportation Board to consider the need for a third major railroad to operate in the east -- in the important major corridors.

USDA's concerns have been addressed -- have not been addressed. And as a result, Secretary of Agriculture Dan Glickman stated USDA's opposition then to this merger in his comments that were filed June 3rd of 1996. Today I reiterate USDA's opposition to the UP/SP merger as presently proposed. We believe this could seriously disrupt the competition balance that exists in transportation.

The merger would adversely affect agriculture producers, shippers, rural communities in many parts of the midwest, southwest, and west. We believe the merger could seriously restrict exports of agriculture products to key foreign markets and hinder the successful implementation of a new 1996 Farm Bill.

If approved, the merger would leave only two Class 1 railroads operating in much of the western United States. In many areas, the railroads would drop from two to only one. And in these areas, rail is often the only economically feasible alternative for shipping bulk agriculture commodities like grains and oil seeds.

Tracking rights alone will not inherently limit the availability to preserve competition. By their nature, trackage rights place the non-owning carrier at operational and economic disadvantage to the owning carrier. These disadvantages would result in restricted competition over much of the region where the UP and SP presently operate.

VICE CHAIRPERSON SIMMONS: Pardon me, sir. Did your department oppose the Burlington Northern/Santa Fe?

MR. DUNN: Did we --

VICE CHAIRPERSON SIMMONS: Oppose the merger?

MR. DUNN: We did not.

VICE CHAIRPERSON SIMMONS: Why?

MR. DUNN: We expressed our concern over that particular merger. We did not oppose it at time. But I must say, Mr. Commissioner, since that merger took place, we have had unprecedented problems in the upper midwest of the availability of rail cars to many of the producers.

VICE CHAIRPERSON SIMMONS: So you're telling me the possible merger of the Southern Pacific and the UP give you real concerns as opposed to the Burlington Northern/Santa Fe?

MR. DUNN: It gives us continuous concerns. The Economic Research Service did a study in June of 1989, James McDonald -- his part of the summary's conclusion was the presence of a competing railroad also has a noticeable affect on rail rates. Competition is weakest and rail rates rise well above incremental cost in regions, generally the western parts of the Great Plains that have only one or two railroads and are far from navigatible rivers.

So that is why we have additional concerns over this one.

VICE CHAIRPERSON SIMMONS: Well, I have an abiding interest in the hauling of grain. I'm sure the Secretary's made you aware of that. And I'm not aware that Southern Pacific hauls a lot of grain. I can't see what your real problem is.

MR. DUNN: Southern Pacific hauls about 16% of the grain -- or 14% of the grain in the area. But it does provide the availability of competition.

VICE CHAIRPERSON SIMMONS: Just a small haul though for grain?

MR. DUNN: Well, if I'm the producer out there and they're the one that's hauling it for me, they're the biggest game in town.

VICE CHAIRPERSON SIMMONS: Okay.

MR. DUNN: Independent studies cited in this proceeding indicate that rail shippers in markets served by three railroad pay lower rates to rates in those markets served by only two railroads. Increasing rail rates for agriculture products would result -- from this merger would be borne most heavily by farmers through lower commodity prices and higher cost of agricultural end cuts.

Higher rates would also place affected agriculture shippers in rural communities in economic disadvantage to those in other areas where transportation alternatives exist. If allowed, it could adversely affect U.S. exports of agriculture commodities. Reduction in rail competition could limit the ability of the U.S. agriculture to reap the benefits of trade liberalization.

Under NAFTA, Mexico is expected to be an important growth market, especially for grains and oil seeds produced in the midwest and plain states. Affordable rail rates and access to service are critical. The merger could also adversely affect the implementation of the 1996 Farm Bill.

This new farm bill gives farmers the flexibility to respond to market signals. Farmers will not be able to take full advantage of that flexibility if increased shipping costs and lack of access to important foreign markets reduce their net returns. The UP has made attempts to alleviate some of the concerns of shippers in the Gulf Coast region.

However, USDA's principal concerns regarding increased competitiveness has not been resolved. The merger as structured makes no provisions for line divestitures that are necessary to preserve competitive transportation options for many