CHAIRMAN MORGAN: The other number, the 600 million number includes traffic that would be highly competitive and for which there would not be any harm that we would need to address?

MR. REDISCH: That's correct as well. You can really see the focus of this debate by looking at the L.A. to Chicago corridor, which is the largest 3-to-2 traffic flow that the Department of Justice has uncovered. $700 million, multiplied by 10.9 percent; they say there will be $60 million of harm to shippers. You can't find any shippers that believe that.

There was no discussion on the record of harm in that flow. The shippers in California who participate in that flow all favor the merger. The intermodal shippers all favor the merger. The applicants say and we find this quite credible that that flow is currently dominated by the Burlington Northern/Santa Fe.

It is mainly intermodal traffic moving off, much of it, foreign containers coming into the port of L.A. and moving into Chicago. The applicants
say they are going to use their two routes in
different ways. They are going to run intermodal
trains on one route and manifests on another and they
are going to offer more, in effect, competition to the
carrier that is currently on them, dominates that
route, BN.

The people in California seem to buy that.
The shippers using the route seem to buy it. But
Justice, applying very blindly its methodology for
assessing competitive harm, finds that that route
faces a significant potential harm, that on brief they
were proposing that we require applicants to divest
one of their two lines in that route if we didn’t
accept their primary proposal, which is simply to deny
the merger in its entirety.

CHAIRMAN MORGAN: Thank you.

Any other questions on this particular
section?

VICE CHAIRMAN SIMMONS: I’m concerned more
generally with how the Assistant Attorney General
considers approval of this merger rational, underline,
rational? How can you justify it? I’m concerned
about the word "rational".

MR. MACKALL: I can address that a little bit. We have a different statute from the Sherman Antitrust Act. We have a statute --

COMMISSIONER OWEN: You might need to pull the speaker a little closer.

MR. MACKALL: We have a statute that is somewhat pre-merger. Congress has assumed throughout all the time we have had jurisdiction over these rail mergers since 1920 that there are efficiencies that are obtained through rail mergers when carriers put networks together and get more efficient networks, that that is an important benefit.

The Commission's job, the Board's job has always been to balance these efficiency benefits against any competitive harm. That's what the Staff has done here.

I think it comes up with a very different result than if you just look at one issue, and that's competition.

VICE CHAIRMAN SIMMONS: I agree with you a hundred percent, considering the BN/Santa Fe
agreement and the CMA agreement; it just puzzled me
how that word could be used.

COMMISSIONER OWEN: One other thing before
we move on is the word "collusion." Do we have a
history of any problems in collusion as far as most of
the Staff can remember?

Someone has been around quite a long time.

MR. REDISCH: I will jump into that. We
have given this a lot of thought and discussion
amongst ourselves.

In particular --

CHAIRMAN MORGAN: You colluded amongst
yourselves?

MR. REDISCH: Yes.

(Laughter.)

MR. REDISCH: Quietly and in back rooms.

You can tell how successful we have been
by the surprise at our ongoing deliberations. We have
actually kept this pretty much to ourselves, I am
pleased to say, our discussions.

CHAIRMAN MORGAN: That is definitely
collusion.
MR. REDISCH: Yes.

We have looked at the Southeast where two railroads, CSX and Norfolk Southern, offer two railroads as the only two railroads operating over a wide territory. We have said to ourselves, is there sufficient competitive pressure to push those railroads to efficient operations? And the answer is yes, indeed, there is.

Their costs have gone down each year through productivity gains. Competition has forced them to seek that out. Then we asked, is there sufficient competitive pressure to compel them to pass on to their shippers a significant amount of those productivity gains?

The answer again is yes, indeed; that competition in the Southeast has been a win-win situation for the Norfolk Southern, the CSX, and their competition. Since the Staggers Act, the two railroads effectively compete. A more narrow instance, of course, is the two railroads that have very vigorously offered competition out of the Powder River Basin, the Burlington Northern and the Union
At oral argument, I thought that there was one party that seemed confused. He kept saying well, but we went from a one to two, shouldn't rates go down? That might explain it the first year, but rates have gone down every year for 10 years.

Rates -- everyone is talking about how coal rates out of Powder River Basin, just from 1988 to 1992 or 1993, the study seems to show they were down by 30 percent.

So you do get vigorous competition from two railroads operating within fairly large markets.

COMMISSIONER OWEN: The conclusion would be that Justice probably had no reason to raise that issue inasmuch as they had no history of it and there is no proof?

MR. REDISCH: Justice can think of examples in other industries where two firms or three firms or four firms have reached alliances. I can think of those as well. But they couldn’t really offer examples where that has occurred in railroads; and the applicants have offered, as Jack Ventura
explained, a series of cogent explanations as to why
railroading with its networking economies, its hidden
contracts, with a whole slew of structural impediments
to collusion.

COMMISSIONER OWEN: I just wanted that
cleared up.

Thank you.

CHAIRMAN MORGAN: Thank you.

Why don't we move on to you, Mr. Markoff,
and your presentation? Then we will ask more
questions.

MR. MARKOFF: Chairman Morgan, Vice
Chairman Simmons, Commissioner Owen, good morning.

We have prepared a series of 35
recommendations with respect to the various matters at
issue in the UP/SP merger proceeding.

(1) We recommend that the Board approve
the UP/SP merger. We believe that the merger, subject
to certain conditions, will yield tremendous public
benefits in the form of service improvements,
efficiencies, and cost savings; it will revitalize SP;
and it will strengthen competition throughout the
(2) We recommend that the Board impose as a condition the terms of the BN/Santa Fe agreement, by which we mean the agreement dated September 25, 1995 as modified by the supplemental agreement dated November 18, 1995, and as further modified by the second supplemental agreement dated June 27, 1996.

This recommendation reflects our view that, for many shippers throughout the West, the various rights provided for in the BN/Santa Fe agreement will ameliorate the competitive harms that would be generated by an unconditioned merger. We further recommend that the Board clarify that the BN/Santa Fe agreement includes or will include all of the clarifications and amendments described in applicants' rebuttal filing dated April 29th, and also the West Lake Charles extension referenced in applicants' brief dated June 3rd.

(3) We recommend that the Board impose as a condition the terms of the CMA agreement. Many of the pro-competitive provisions of the CMA agreement require amendments to the BN/Santa Fe agreement, and
are reflected in the second supplemental agreement dated June 27th; other such provisions do not require amendments to the BN/Santa Fe agreement.

Applicants have not asked that approval of the merger be made subject to the CMA agreement, but, because the CMA agreement is largely tied to the BN/Santa Fe agreement and its provisions are necessary to ameliorate competitive harm, we recommend that the Board impose the CMA agreement in its own right.

(4) The CMA agreement provides that the BN/Santa Fe agreement will be amended to grant BN/Santa Fe the right to serve any new facilities located post-merger on any SP-owned line over which BN/Santa Fe receives trackage rights in the BN/Santa Fe agreement.

The CMA agreement further provides, however, that the term "new facilities" does not include expansions of or additions to existing facilities or load-outs or transload facilities. We recommend that the Board modify this provision in two respects: first, by requiring that BN/Santa Fe be granted the right to serve new facilities on both
SP-owned and UP-owned track over which BN/Santa Fe will receive trackage rights; second, by requiring that the term "new facilities" shall include transload facilities, including those owned or operated by BN/Santa Fe. These modifications will help to assure that the BN/Santa Fe trackage rights will indeed allow BN/Santa Fe to replicate the competition that would otherwise be lost when SP is absorbed into UP.

The CMA agreement provides a post-merger procedure by which a shipper can raise a claim that the merger deprived it of a build-out/build-in option. We recommend that the Board modify this procedure in two ways: First, by making this procedure applicable to all shippers; second, by removing the time limit to which this procedure is subject. These modifications will allow BN/Santa Fe to replicate the competitive options now provided by the independent operations of UP and SP.

We further recommend that the Board clarify that a shipper invoking this procedure need not demonstrate economic feasibility; the only test of feasibility is whether the line is actually
constructed. And we further recommend that the Board provide that any technical disputes with respect to the implementation of this build-out/build-in remedy may be resolved either by arbitration or by the Board.

(6) The CMA agreement provides that, immediately upon consummation of the merger, applicants must modify any contracts with shippers at 2-to-1 points in Texas and Louisiana to allow BN/Santa Fe access to at least 50 percent of the volume. We recommend that the Board modify this provision by extending it to all 2-to-1 points incorporated within the BN/Santa Fe agreement, not just 2-to-1 points in Texas and Louisiana. The extension of this provision to all 2-to-1 points will help ensure that BN/Santa Fe has immediate access to a traffic base sufficient to support effective track rights operations.

(7) With respect to storage-in-transit facilities, the CMA agreement provides: First, that BN/Santa Fe shall have equal access to Dayton Yard for storage-in-transit of traffic handled by BN/Santa Fe under the BN/Santa Fe agreement; and second, that applicants shall work with BN/Santa Fe to locate

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additional storage-in-transit facilities on the trackage rights lines as necessary.

Various parties have criticized these provisions as inadequate, and we think that these provisions can and should be strengthened. We therefore recommend that the Board order that the BN/Santa Fe agreement be modified to require that in addition, BN/Santa Fe shall have access to all SP Gulf Coast storage-in-transit facilities on economic terms no less favorable than the terms of UP/SP's access, for storage-in-transit of traffic handled by BN/Santa Fe under the BN/Santa Fe agreement.

(8) We recommend that the Board condition approval of the merger by establishing oversight for five years to examine whether the conditions imposed by the Board have effectively addressed the competitive issues they were intended to address. The oversight condition we envision will include an explicit statement by the Board that it is retaining jurisdiction to impose additional remedial conditions if and to the extent it determines that the conditions already imposed have not effectively addressed the
competitive harms caused by the merger.

Applicants have consented to oversight to confirm that the BN/Santa Fe agreement has effectively addressed competitive issues; but we think that any such oversight should properly consider whether all conditions imposed by the Board have effectively addressed competitive issues.

(9) Various parties have expressed concerns that BN/Santa Fe will not provide the vigorous competition that is the premise of the BN/Santa Fe agreement. We recommend that the Board address these concerns in two ways: First, by making clear that the Board expects that BN/Santa Fe will compete vigorously for the traffic opened up to it by the BN/Santa Fe agreement; second, by imposing upon BN/Santa Fe a common carrier obligation with respect to the traffic opened up to it by the BN/Santa Fe agreement. We further recommend that the Board make clear that the competition provided by BN/Santa Fe will be one of the key matters that will be considered in the oversight proceeding. And we further recommend that the Board require that BN/Santa Fe submit a
progress report and an operating plan on October 1st of this year, and further progress reports on a quarterly basis thereafter.

(10) Various parties have expressed concerns that BN/Santa Fe may not immediately commence the trackage rights operations made possible by the BN/Santa Fe agreement. We recommend that the Board address these concerns in two ways: first, by acknowledging that, to some extent, immediate commencement of trackage rights operations may not be physically possible; but second, by making clear that the Board expects that, as soon as reasonably practicable, BN/Santa Fe will commence trackage rights operations in the key corridors opened up by the BN/Santa Fe agreement. The key corridors we have in mind are the Houston-New Orleans corridor, the Houston-Memphis corridor, and the Central corridor. We further recommend that the Board make clear that a failure to conduct trackage rights operations in these corridors could result in termination of BN/Santa Fe’s trackage rights and substitution of another carrier or in divestiture.
(11) We recommend that the Board impose as a condition the terms of the Utah Railway agreement. This recommendation reflects our view that, for certain coal shippers, the rights provided for in the Utah Railway agreement will ameliorate the competitive harms that would be generated by an unconditioned merger.

(12) We recommend that the Board condition approval of the merger by granting Tex Mex the trackage rights sought in its Sub-No. 13 responsive application; these trackage rights would run over UP/SP lines from Robstown and Corpus Christi to Houston, and on to a connection with KCS at Beaumont. We further recommend that the Board grant the terminal trackage rights in Houston sought by Tex Mex in its Sub-No. 14 terminal trackage rights application. These recommendations reflect our belief that such trackage rights are required to ensure the continuation of an effective competitive alternative at Laredo and to ensure the continued provision of essential services to shippers located on Tex Mex.

We further recommend that these trackage

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rights be restricted to traffic having a prior or subsequent movement on the Laredo-Robstown-Corpus Christi line, that Tex Mex and applicants be permitted to negotiate the terms and conditions of these trackage rights, and that Tex Mex be permitted to operate via these trackage rights immediately following consummation of the merger.

(13) With respect to traffic moving from
and to Lake Charles, West Lake Charles, and West Lake,
Section 4(b) of the second supplemental agreement
dated June 27 provides as follows: that BN/Santa Fe shall have the right to handle traffic of shippers open to all of UP, SP, and KCS at Lake Charles and West Lake, and also traffic of shippers open to SP and KCS at West Lake Charles; provided, however, that such rights shall be limited to traffic from, to, and via New Orleans, and from and to points in Mexico via the border crossings at Eagle Pass, Laredo, and Brownsville. We recommend that the Board expand BN/Santa Fe's single line access to this traffic by removing the proviso; the principal effect of this recommendation will be to allow BN/Santa Fe to handle
traffic moving to Houston and to other points on BN/Santa Fe. We further recommend that the Board expand BN/Santa Fe's joint line access to this traffic by allowing BN/Santa Fe to interchange this traffic at Shreveport and Texarkana with KCS; the principal effect of this recommendation will be to substitute a post-merger KCS-BN/Santa Fe joint-line routing via Texarkana and Shreveport for the pre-merger KCS-UP joint-line routing via Texarkana.

(14) With respect to Texas Utilities Electric, we recommend that the Board condition the merger by requiring that BN/Santa Fe be allowed to interchange TUE's coal trains with KCS at Texarkana and Shreveport. Without this condition, all but one of TUE's Powder River Basin routings would involve UP/SP, and the one that would not be excessively circuitous.

(15) With respect to Dow at Freeport, we recommend that the Board preserve Dow's existing SP build-out option by providing that trackage rights will be granted to a carrier to be named by Dow, subject to Board approval, over UP's line from Texas.
City to Houston and over UP’s or SP’s line from Houston to connections with KCS and BN/Santa Fe at Beaumont, with the right to connect to the build-out line in the vicinity of Texas City in order to serve Dow and any other shippers located on the build-out line. Although this condition preserves an SP AP build-out option, the trackage rights will run over the UP line from Texas City to Houston because the SP line is being abandoned.

(16) With respect to the Capital Metropolitan Transportation Authority, we recommend that the Board condition the merger by providing Giddings-Llano shippers a Class I connection at Giddings. The potential competition that exists today rests upon an SP connection at Giddings; and this potential competition can be preserved by providing that the operator of the Giddings-Llano line is to be regarded as a 2-to-1 short line for purposes of Section 81 of the BN/Santa Fe agreement, the so-called "omnibus" provision. We further recommend that the Board note that applicants will be held to their representation that they will allow BN/Santa Fe to...
establish a connection at Elgin, if and when operations are reactivated over the Smoot-Elgin segment. We further recommend, however, that the Board note that CMTA has a right to a single connection with BN/Santa Fe, either at Elgin or at Giddings, but not to two such connections, and that CMTA will therefore be required to choose between Elgin and Giddings, unless the parties agree otherwise.

(17) With respect to Entergy Services and its affiliates, we recommend that the Board condition approval of the merger by requiring that the BN/Santa Fe agreement be amended to permit BN/Santa Fe to serve the White Bluff plant via a build-out line between White Bluff and Pine Bluff, if and when that line is constructed. This recommendation is designed to preserve the build-out status quo at White Bluff.

(18) With respect to the City Public Service Board of San Antonio, we recommend that the Board impose a condition allowing BN/Santa Fe to serve Elmendorf Station via CPSB's existing trackage rights agreement with SP. This recommendation is designed to
preserve the pre-merger status quo respecting the CPSB trackage rights.

(19) With respect to Union Carbide Corporation, we recommend that the Board condition the merger by granting BN/Santa Fe trackage rights over SP’s Victoria-Lavaca line between the UP main line and a point near Kamey. This recommendation is designed to preserve the build-out status quo at the Seahrit Plant.

(20) Applicants have made numerous representations to the effect that certain points will be covered, certain services will be provided, and so on. By way of example, applicants have represented, with respect to the City Public Service Board of San Antonio, that the BN/Santa Fe agreement will be amended to clarify that Elmendorf is a covered point. That is one particular representation; there are many others. We recommend that the Board condition approval of the merger by requiring applicants to adhere to the various representations they have made. We would note, of course, that to the extent these recommendations are reflected in the second
1. supplemental agreement dated June 27, nothing further needs to be done.

2. (21) We recommend that the Board determine that the terms of the UP/SP Merger Agreement with respect to the purchase of the SPR common stock are fair both to the stockholders of UPC and also to the stockholders of SPR.

3. (22) We recommend that the Board note that the securities request contained in the lead docket, respecting approval or exemption of securities issuances to finance UP/SP common control, terminated by force of law effective January 1, 1996.

4. (23) We recommend that the Board exempt, in the Sub-No. 1 docket, the trackage rights provided for in the BN/Santa Fe agreement and included in the Sub-No. 1 notice filed November 30, 1995. These trackage rights are vital to the competitive service that BN/Santa Fe will provide, and we believe that the trackage rights class exemption can be invoked with respect to trackage rights provided for in a settlement agreement.

5. (24) We recommend that the Board direct

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applicants and BN/Santa Fe to file, no later than
seven calendar days prior to the effective date of the
decision approving the merger, an additional class
exemption notice covering the trackage rights that
will be added to the BN/Santa Fe agreement in
accordance with the amendments required by the CMA
agreement. These trackage rights are also vital to
the competitive service that BN/Santa Fe will provide,
but were not included in the Sub-No. 1 notice filed
November 30.

(25) We recommend that the Board direct
applicants and Utah Railway to file, no later than
seven calendar days prior to the effective date of the
decision approving the merger, a class exemption
notice covering the trackage rights provided for in
the Utah Railway settlement agreement. These trackage
rights are vital to the competitive service that Utah
Railway will provide.

(26) We recommend that the Board exempt,
in the Sub-No. 2 docket, the line sales provided for
in the BN/Santa Fe agreement. These line sales are an
important part of the arrangements provided for in the
BN/Santa Fe agreement.

(27) We recommend that the Board exempt, in the Sub-Nos. 3, 4, 5, 6 and 7 dockets, the common control by applicants of The Alton and Southern Railway Company, the Central California Traction Company, the Ogden Union Railway and Depot Company, the Portland Terminal Railroad Company and the Portland Traction Company.

(28) We recommend that the Board exempt, in the Sub-No. 8 docket, common control of UP and the two motor carriers controlled by SP, and common control of SP and the one motor carrier controlled by UP.

(29) We recommend that the Board grant in the Sub-No. 9 docket the application filed by applicants and BN/Santa Fe for an order permitting BN/Santa Fe to use two segments of KCS track in Shreveport and one segment of KCS track in Beaumont. The order has been sought under section 11103, which allows the Board to require terminal facilities owned by one railroad to be used by another if the use is practicable and in the public interest, and will not
substantially impair the ability of the owning carrier
to handle its own traffic. The segments involved in
the Sub-No. 9 docket are essential to the planned
BN/Santa Fe operations in the Houston-to-Memphis and
Houston-to-New-Orleans corridors.

(30) With respect to the proposed
abandonments and discontinuances of the two segments
of the Tennessee Pass Line, we recommend that the
Board deny the abandonments but grant the
discontinuances. We are recommending denial of the
Tennessee Pass abandonments because there is some risk
that Tennessee Pass traffic cannot be rerouted
successfully via Moffat Tunnel. We are, however,
recommending approval of the Tennessee Pass
discontinuances because local traffic on the Tennessee
Pass Line is minimal. Our recommendations will allow
a commonly controlled UP/SP an opportunity to
demonstrate that Tennessee Pass traffic can be
rerouted successfully; but our recommendations will
also preserve the Tennessee Pass corridor until such
time as that demonstration has been made.

(31) We recommend that the Board approve
all other abandonment and discontinuance requests made by applicants. The 15 lines subject to this recommendation are presently used primarily, in a few instances exclusively, for overhead traffic, and the evidence demonstrates, with respect to each such line, that this overhead traffic can be rerouted by a post-merger UP/SP. The local traffic generated by these 15 lines is minimal; in a few instances, it is nonexistent, and these lines simply cannot be sustained by the limited amounts of local traffic they generate.

(32) We recommend that the Board impose the standard labor protection conditions: for the merger, the line sales, and the terminal railroad control transactions, New York Dock; for the trackage rights, Norfolk and Western; and for the abandonments and discontinuances, Oregon Short Line.

(33) With one exception, we recommend at this time that the Board impose the various mitigation measures recommended in the Post-environmental Assessment that was served on June 24, 1996. The one exception relates to the Tennessee Pass line: if the
Board adopts our recommendation to deny the abandonment but to approve the discontinuance, the mitigation measures recommended in the post-EA will have to be adjusted accordingly.

(34) We recommend that the Board find that the UP/SP merger, subject to the recommended environmental mitigation measures, will not significantly affect the human environment, and we further recommend that the Board find that an environmental impact statement is not required.

(35) Finally, we recommend that the Board deny all requests for conditions except those we have specifically indicated should be granted in whole or in part.

We would be glad to take any questions.

CHAIRMAN MORGAN: Thank you. We all get training here in how to read fast.

You have run through many conditions. The key to many of these conditions is to try, as I understand it, to preserve the competition that exists to-day at points that become 2-to-1 points post-merger?

MR. MARKOFF: Yes.
CHAIRMAN MORGAN: Obviously the staff, in coming up with these conditions, looked at the CMA agreement and felt it was not adequate.

Could you summarize where you found the CMA agreement to be inadequate?

MS. FARR: I would like to have Lou Mackall speak to that.

MR. MACKALL: One of the problems with the CMA agreement was that the traffic rights under it only covered what have been designated as 2-to-1 points. There are other shippers at 1-to-1 points that also enjoy the fact that they have a second carrier near them, although the second carrier does not serve them directly.

We addressed those problems, as CMA does, by expanding build-in and build-out options, by expanding transloading options and new facility options, that kind of thing that are in the CMA agreement.

But the problem with the CMA agreement is that it did not cover, for the most part, people that weren't members or had restrictions on who could take
advantage of these options.

So we basically broadened the type of things that are in CMA to cover all the shippers that are affected by the merger.

CHAIRMAN MORGAN: So if a shipper today had a build-out option, it would have one post-merger?

MR. MACKALL: We tried to replicate the impact of direct competition that happened in the Florida merger.

CHAIRMAN MORGAN: Now the plastics industry, of course, had several issues they were concerned about. You have indicated a condition related to storage in transit facilities which I know is of importance to the plastics and petrochemical industries.

Are we amending a provision that is already in one of the other agreements?

MR. MARKOFF: There is a provision in the CMA agreement regarding storage and transit facilities, and we are recommending that provision be expanded.

CHAIRMAN MORGAN: So that as I heard you
when you read it, all shippers would have -- would be able to work with BN/Santa Fe in getting access to all of the current SP storage and transit facilities; is that correct?

MR. MARKOFF: Yes.

CHAIRMAN MORGAN: Now, you also discussed an arbitration process that is under the CMA agreement that would continue as a condition here.

Do you have any concerns about how that arbitration process is going to work?

MR. MARKOFF: The arbitration, under arbitration, or before the Board, only for technical questions that come up, because the basic question that applicants have been talking about is feasibility. We made it quite clear that there is no test of feasibility. The line gets built; it is feasible. If it doesn't get built, it is not feasible, there is nothing to dispute.

CHAIRMAN MORGAN: In other words, under the CMA agreement, there was a requirement for feasibility.

MR. MARKOFF: There was no specific
requirement for feasibility, but the applicants made
clear they were under the impression that that was
implicit in the CMA agreement. We are making clear
no.

CHAIRMAN MORGAN: Now, the Utah Railway
conditions I see it is an attempt to address some of
the concerns raised by Western Coal shippers. Would
you explain specifically how the Staff feels it will
address their concerns?

MR. MARKOFF: The Utah Railway agreement
grants Utah Railway access to several additional lines
that it does not have access to now. In addition, it
grants Utah Railway trackage rights from Utah Railway
junction east to Grand Junction, Colorado.

It is going to provide for shippers
located east and midwest and some shippers west of
Salt Lake City. It will provide them an option they
don’t have now with coal out of the Uinta Basin
originated by the railway and either at Provo or Grand
Junction. There will be a routing competitive with
the UP/SP rate.

CHAIRMAN MORGAN: There was some concern
in the record about whether this type of competitive alternative would indeed work. Maintaining what the coal shippers view as the source of geographic competition as between the Powder River Basin and the Colorado-Utah coal, does the Staff feel that this addresses that concern specifically?

MS. FARR: I would like to have Michael Redisch address that.

MR. REDISCH: The short answer is yes, it does. I will give you a slightly extended answer.

There are two different types of coal in the west, at least, bituminous and subbituminous. I learned a lot about coal production by reading through the record in this proceeding.

The subbituminous coal is mined exclusively in the Padwrorthy Basin through very efficient mining methods. I’ve not been there. I’ve seen the pictures. Huge gashes in the earth, $4 or $5 per ton at the mine now for the coal.

The Uinta Basin coal, which is accessed by the Southern Pacific in Colorado and the Utah Railway in Utah, is a higher Btu content coal. That would
make it slightly more desirable by utilities, but it is also more difficult and more costly to mine. It costs as much as $15 to mine, to produce, and sell at a profit.

So these coals tend not to compete directly for those utilities that have constructed plants and boilers that have the opportunity to burn Powder River Basin coal; that is the coal of choice.

You do see a lot of utilities who can’t burn all Powder River Basin coal because even though it is a low sulfur coal and will help them comply with the Clean Air Act under Phase I and by the year 2000 under Phase II their boiler capacity is such that there is a process called derating that takes place if they burn all Powder River Basin coal. They tend to blend those coals. There is quite a bit on the record of utilities that have purchased some Powder River Basin coal and some coal originated by the Southern Pacific out of the Uinta Basin in Colorado.

But in general, those have not been competitive. They have been complementary. The major competitor of the Uinta Basin coal is, in fact, the
low sulfur, high Btu coal produced in the Appalachian
region and elsewhere and sold to Midwestern utilities.
That, in fact, is exactly where the Utah Railway hopes
to sell its coal as it hopes to extend its routes east
under this agreement.

We did look at the relative market shares
out west. SP is not a significant presence for coal.
It originates about 8 percent of all coal. Burlington
Northern is about 57 percent, UP about 30 percent.

What we have determined is that with the
exception of a few shippers who might be situated
close enough to the Uinta Basin to make the shorter
rail haul overcome the much higher mine price, there
is very, very limited competition between these two
coals. They are, in fact, distinct. The Union
Pacific’s competitor for coal, as we all know, is the
Burlington Northern out of the Powder River Basin.

SP has a franchise. It has pursued it
vigorously. It has entered into backhaul arrangements
and offered very competitive rates heading east by
offering one of its local shippers in Utah, Geneva
Steel, very attractive rates for steel products, steel
inputs moving west and coal moving east.

There is a limit to that because there is a limit to how much of those backhauls Geneva Steel will take; but we looked at the record. We decided that UP will not suppress Uinta Basin coal. Why would it? It is a good business. It is complementary to its own business.

We are suggesting a monitoring condition so if UP chooses to suppress that coal, that we would see it quite clearly. The protestants here are not alleging that there’s going to be much of a price effect, as I see it. They are really alleging that UP simply suppress all the fine efforts Southern Pacific made in marketing that Utah coal and Colorado coal. We will see if that is so.

The Montana rail link, which bases its responsive application largely on coal, suggested in a brief that even though existing utilities may be locked in to boiler requirements and the types of coal that they can burn, that there would be significant ex ante competition between Uinta Basin and Powder River Basin coal while the utility is in the planning and
Our assessment is that utilities at this stage, before they site a plant, before they choose a coal source, before they choose a railroad, before they have chosen a coal mine, need not be worried about any mergers between the Union Pacific and the Southern Pacific cutting off their opportunities to purchase coal. They will be able to purchase Powder River Basin coal, they will be able to purchase Utah coal, they will be able to purchase coal from any of the Midwestern producers.

So we did not see merit in that ex ante argument pursued on brief by Montana Rail Link. That's the long answer.

CHAIRMAN MORGAN: Very thorough. Thank you.

Let me ask about grain in NAFTA and Texas. The Tex-Mex condition, to what extent does that reflect and respond to the concerns raised about competition as it relates to NAFTA movements, grain, and also Texas?

MS. FARR: This question, I too would like
to have Michael Redisch respond to.

MR. REDISCH: How kind.

(Laughter.)

CHAIRMAN MORGAN: You're doing fine.

MR. REDISCH: Thank you, Chairman Morgan.

VICE CHAIRMAN SIMMONS: You get a cigar when you are over.

MR. REDISCH: I'm looking forward to that, sir.

CHAIRMAN MORGAN: A lot of months have gone into this.

MR. REDISCH: For all of us.

I would like to take this opportunity to mention, going back to coal, we have found one potential anti-competitive effect that we raised concern about with Staff. It was not a pricing effect. It was not a Uinta Basin versus Powder River. It was our concern over the Tennessee Pass Line. We have defined anti-competitive effects of the merger as higher prices or poorer service that producers might face as a result of this merger.

It did concern us that the applicants'
plan to shift traffic to a more efficient tunnel routing might degrade service and lead to backups on that route. This would actually hit coal shippers in the pocketbook. They are the ones who own the coal cars.

If those coal cars are strung out over greater time periods on the Moffat Tunnel line, then you need to own a lot more cars to meet whatever delivery schedule you are going to need for your utilities. We were concerned about that. We didn’t listen to what the applicants had to say.

Yes, there were 25 trains a day running through that line by the Denver-Rio Grande 20 years ago. They were a different type of train. So we have recommended as part of our coal assessment the -- that the Board deny the abandonment application for that line and only permit the discontinuance. I’m glad I had an opportunity to jump in there.

CHAIRMAN MORGAN: Grain?

MR. REDISCH: Yes. Tex-Mex, Mexico, wonderful area. NAFTA working well. We want to maintain that.
The key border crossing is Laredo. It gets 55 percent of U.S.-Mexican movements. It is currently served by the Union Pacific directly and by the Tex-Mex which is a hundred-plus year old small U.S. carrier that connects with both the Union Pacific and the Southern Pacific at Corpus Christi, runs about 150 or so miles.

It is Tex-Mex that has essentially preserved a second competitive option for the major gateway for U.S.-Mexican trade.

There is some concern after the merger it will have an opportunity to use the Burlington Northern/Santa Fe under the settlement agreement, but the Tex-Mex has offered its responsive application not as a replacement for the Burlington Northern but as an addition to it.

Tex-Mex has suggested a different routing than the Burlington Northern route, one that would follow a less congested Southern Pacific routing into Houston and on to a connection with the Kansas City Southern Railway at Beaumont.

Our assessment is that Tex-Mex has some
reason for concern. Almost 10 percent its traffic today is originated on the Southern Pacific, exclusively at points served by SP. That traffic is likely to flow toward the more efficient single line routing SP will gain when it merges into UP toward Laredo. Another large block of Tex-Mex's traffic is originated by the Burlington Northern/Santa Fe; less today than about a year-and-a-half ago because BN has been essentially embargoing all grain traffic moving on the SP.

So the Tex-Mex's traffic has declined markedly, although BN has explained that this has nothing at all to do with the Tex-Mex and everything to do with the poor service offered by SP. It keeps losing BN grain cars on its way back and forth between Houston and Corpus Christi.

But there is still a risk that the new trackage rights that will replace BN's hauling rights to Eagle Pass will provide a new efficient routing for it, and that rather than operating at a 31,000 mile funnel offers BN shippers an opportunity to use Laredo, it will instead offer a lot of those shippers
a single line routing into Eagle Pass.

So as a safety feature, we would recommend that the Board grant the Tex Mex its responsive application as the Tex Mex has explained. If it is wrong and the applicants' assessment is correct, then few shippers will use this new arrangement and most shippers will use the Burlington Northern settlement agreement routing into Corpus Christi.

Our feeling, and one that was provided by a large number of shippers on the record, most of them grain, but some other commodities as well, was that economical access to important international trade routes should not be jeopardized. The Tex Mex responsive application not only met with significant shippers' support, grain shippers in the Midwest, from Volkswagen of America, but also from the Texas parties, from the Railroad Commission of Texas.

We are also recommending that the Tex Mex not be given unrestricted access to use these trackage rights but that they only be used in conjunction with traffic that moves on to or off of the Tex Mex.

Tex Mex has said such limitation would not
undermine the purpose for which the rights are sought, and it would not significantly affect Tex Mex's ability to provide essential services to customers local to its lines. We have taken it at its word. These would be additional competition, what I might call pro-competitive tinkering that Tex Mex has asked for but they concede does not require it to meet the goals of their responsive application, which is to provide an alternative competitive routing for the grain and other commodity movements that are expected to flow south when NAFTA trade with Mexico expands.

Thank you.

CHAIRMAN MORGAN: Let me turn to some of the environmental issues.

We heard some testimony at the oral argument regarding both Laredo and Wichita. Ms. Kaiser, if you could just summarize for us the suggestions in both of those areas and the progress in the discussions that have been going on?

MS. KAISER: I would be glad to do that.

CHAIRMAN MORGAN: Pull the mike close to you.
MS. KAISER: We first want to emphasize --

VICE CHAIRMAN SIMMONS: A little louder.

MS. KAISER: My family tells me I am awfully loud, so this is a new experience.

CHAIRMAN MORGAN: I have the same problem.

(Laughter.)

MS. KAISER: We first want to emphasize we have recommended an independent mitigation study for both Reno and Wichita. When we say independent, we mean independent. This study would be conducted under the auspices of the Board. The Section on Environmental Analysis would select an independent contractor who would work under the sole supervision and direction to ensure there was an independent analysis. This independent environmental analysis would look to the effects associated with the additional traffic that would result from the proposed merger.

After this independent mitigation study was completed, we would present it to the Board for its review with these recommendations, so you all would have an opportunity to look at the study very
closely and then have an opportunity to issue a
decision which would impose conditions that would
embrace the mitigation you determined appropriate was
recommended in the study.

I would like to take a minute to tell you
a little bit about what we envision the study would
do. Again, I want to emphasize the study would focus
on the environmental effects associated with the
proposed merger. In conducting the study, we would
certainly solicit comments from the public, community,
Federal, state, and local agencies affected.

Also, the study would look to shared
costs. There is no single cost agent here. There
have been multiple contributing parties. We would
look at ways to share the costs if there are effects
that need to be remedied with the mitigation.

One example I would like to point out to
you --

CHAIRMAN MORGAN: I think the mike is not
working very well.

I want to make sure everybody has the
benefit of your work.
MS. KAISER: Is this better now?

Again, we want to emphasize this independent study would look at different vehicles for shared costs. For example, in the City of Reno, the best visual example I can give you is this conference table. You have here a situation where, when we first walked in, the table was clear, so to speak. If you envision the rail line going through the center of the table, that would be the start.

But you see here our papers and how they built. Well, on both sides you have this type of situation where you have business development, you have casinos, tourists, et cetera.

And in looking to these two independent studies, we have identified Reno and Wichita because they are so unique in this overall merger.

For example, with Reno, there is the 24-hour test vehicular traffic, proximity of casinos to the right of way has created the right of way to fine tune mitigation.

So as a result of this study, we will look further to refine very specific mitigation that meets...
the unique circumstances of these two communities and we will -- during this time, we will not implement the desired increase in projected traffic as a result of the merger.

So potentially we would maintain an environmental status quo while fine tuning would go on; and again, I want to emphasize that that mitigation study would then be presented to all of you for review and then a decision would be issued with appropriate mitigation conditions for these two locales.

CHAIRMAN MORGAN: Are there discussions ongoing now in these two locations?

MS. KAISER: There are discussions ongoing. This is a very difficult situation because you have many polarized issues. It is not simply one issue. Cost is a very, very big concern here. How is that going to be shared? That is a primary hurdle. We do view this as a shared cost.

VICE CHAIRMAN SIMMONS: Do you feel reasonably assured, then, that this study will allay the fears and possibly solve the safety concerns of
these two communities?

MS. KAISER: We are going to make every effort to do just that. We feel there are certain steps that can be taken such as separating crossings, pedestrian overpasses and underpasses that go to the heart of safety. We are going to look very carefully at that. We are going to work very closely, again, with the communities to make sure they have an input and we present to you a very well-rounded, balanced study.

VICE CHAIRMAN SIMMONS: Very good.

COMMISSIONER OWEN: Along that line of thinking, I think you did mention in your presentation you were looking backward in time to the way you described the conference table there as the building permits and so forth and buildings continuing to encroach upon the lines as the city grows.

I would hope the cities would take a look at that and say that they do have some responsibility and that the environmentalists that you are sending out there to do this appraisal would take into consideration and take a look and remind them of their
responsibility that you have issued some of these building permits in the last 20 years or 50 years that have encroached upon this right of way here and moved into it, and you have impacted this area here so that now that it is restricted in such a sense, that you have no other solution other than sell the casinos and make it into a park.

Who is to bear that cost and that burden?

Local citizenry would probably fight you on that. I wish you well on that.

CHAIRMAN MORGAN: During this 18-month period, what would be the Board's involvement in this process?

MS. KAISER: As I said earlier, the section on environmental analysis would work very closely with the contractor. We would be the sole supervisor and director of control. We would report back to you on the progress of the study as it went along to answer any questions you might have about this study's scope.

Then again, we would work -- I have to emphasize with the community, the city. We would look
at the shared costing option and then come forward with a recommendation to all of you which you can either accept in full or in part based upon the analysis in the study.

CHAIRMAN MORGAN: During that 18-month period, what would be the level of traffic specifically over those lines in that -- during that period?

MS. KAISER: We propose an additional two trains a day on these lines while the study is going on. This would potentially maintain the environmental status quo but not create any shifts that could throw the environment, if you will, out of whack.

CHAIRMAN MORGAN: Because the plan, but for this particular problem, would be to run many more trains than two a day over that track; is that correct?

MS. KAISER: That's correct.

CHAIRMAN MORGAN: Are there any other questions?

COMMISSIONER OWEN: I might have a couple more, if you don't mind, regarding the quarterly
reports of Burlington Northern, I believe, to ensure there is going to be an effective competitor.

I was wondering, what are we looking at? What might go along? A hundred years? I would like reports of any kind.

MS. FARR: We don’t envision the reports to continue indefinitely, just until the time when Santa Fe would implement its trackage rights.

COMMISSIONER OWEN: I will continue to remind you of that every quarter.

One other question. There have been a number of conditions imposed here, environmental constraints. What type of a financial impact would that have been upon the Applicants as to whether or not it would be prohibitive for them to go ahead with this merger?

MR. MACKALL: Overall, most of the conditions have to do with making sure that UP doesn’t have increased monopoly power, competitive power that they didn’t have before.

So, out-of-pocket, there would be very little, with the possible exception of the
environmental conditions, which we don't know exactly how that will come out.

But there might be some fairly significant dollars in that.

COMMISSIONER OWEN: I just wondered about the granting of the Tex Mex trackage rights this morning. When you propose this, what kind of an impact does that have?

MR. REDISCH: Our assessment is that it should have a limited impact, operationally. It is going to propose to move over an SP line which does have room on it for the traffic. It will not impede the settlement agreement.

We are not talking about a lot of interference with the Applicants' existing operations as the Tex Mex has proposed it. So I don't see much in the way of an adverse impact on the Applicants' operation.

COMMISSIONER OWEN: I would like to monitor that. If we go ahead and vote this morning, whatever the vote turns out to be, if it is approved, I would like to monitor that as we go along over the
next year or so to see if there was a significant impact financially. For us sitting here in Washington, D.C. and being the economists and attorneys and so forth in this room, you have done an outstanding job. I commend all of you on that.

Is it real in the real world when you get out in the field? I guess that is my question.

A year from now, I would like to take a look at that.

VICE CHAIRMAN SIMMONS: Commissioner Owen, is that with regard to marketing?

COMMISSIONER OWEN: No.

VICE CHAIRMAN SIMMONS: Okay.

Madam Chairwoman, if we are going back to the monitoring, if this Board should see fit to vote and the recommendations of the Staff are approved and the Wisconsin Central, the ICC-imposed monitoring, an oversight for a five-year period, and we decided that -- to discontinue it after finding no competitive harm after three years. I would like to have somebody's comment as it relates to that, how you might feel about it.
What would be your recommendations? Maybe they would be down the line further.

MR. MACKALL: It is hard to tell what is going to happen. As a staff, we feel very confident the various anti-competitive effects that have been predicted here will not come to pass.

If they do not come to pass and we don't have problems with this, it could be that we might take at some point -- we would be a little less than active in our monitoring. If problems do emerge, then we would be more active. I think we have to play it a little loose right now.

VICE CHAIRMAN SIMMONS: Okay.

MR. KONSCNIK: One thing I would like to add in response to Commissioner Owen's question about monitoring is to see the effects to the Union Pacific on the imposition of some of the conditions. I think, based on our recommendation, we expect that the net effect of many of these conditions will simply be to constrain the pricing by Union Pacific.

So I'm not sure that that would be particularly measurable from our standpoint; but we
think that we will have good, positive effects for the public interest in that the pricing decisions made by the Union Pacific will certainly be affected by the alternative competitive presence that is provided for if you accept our recommended conditions.

CHAIRMAN MORGAN: Well, I believe that we are now prepared to vote on the Staff's recommendations.

Briefly summarized, they are to approve the merger application with the BN/Santa Fe trackage rights agreement and the CMA agreement as further significantly amended by the Staff recommendations; is that an accurate summary?

MS. FARR: Yes. Also the Utah Railway settlement agreement.

CHAIRMAN MORGAN: I would move, then, to adopt the Staff recommendations.

VICE CHAIRMAN SIMMONS: I second.

SECRETARY WILLIAMS: Commissioner Owen?

COMMISSIONER OWEN: If I could, please, I would like to start off with a little statement on this.
Since 1920, it has been the public policy of this agency to encourage railroad mergers that were in the public interest. Overwhelming evidence was presented that if we approve this merger, there will be substantial operating cost savings, improved rail service, renewed financial strength for Southern Pacific, more effective rail competition.

Nonetheless, this agency is obliged to consider the likelihood of competitive harm. Competitive harm is likely to be substantial in certain important markets. The conditions proposed are intended to ease and often eliminate that harm. There are many publics and many interests, as we heard this morning. We cannot satisfy each. What we have achieved will allow the greatest good to be achieved with the minimum harm.

Therefore, I vote to approve the transaction with the conditions proposed by Staff, and with a few other remarks, because this is a historic moment in my lifetime.

Let me stress to skeptics that this agency will be an alert policeman using its extensive powers
to command immediate remedies as necessary, as you
heard outlined this morning. I have every intention
of walking the beat with a soft voice and a big stick.

I wish to make several additional points.

First, with respect to Amtrak, I remind
the Applicants that the Rail Passenger Service Act of
1970 requires Amtrak trains to have preference over
freight traffic.

Furthermore, I accept the applicants’
assurances given during the oral arguments that UP/SP
will move immediately to correct Amtrak’s service
problems on the Southern Pacific line.

I will continue to watch very closely
every railroad’s handling of Amtrak trains.

With respect to labor, the allied rail
unions asserted during oral argument that there is a
link between a previous STB decision and a recent
fatal train wreck. It is as absurd to blame Board
decisions for human factor accidents as it is to blame
society for the violent behavior of some citizens.

Adults are responsible for their own actions, even
when they belong to unions and are employed by
I am concerned, however, with labor union complaints that merging railroads use implementing agreements to circumvent collective bargaining agreements. The very fact that UP/SP addresses the matter positively in its agreement with the United Transportation Union is evidence that the issue has merit. The purpose of implementing agreements is to permit consummation of a merger, not to achieve other objectives meant for collective bargaining.

Since rail labor and management voluntarily negotiated the Job Protection Agreement of 1936, disputes over implementing agreements have been submitted to binding arbitration. That is still the case. The parties to the dispute choose the arbitrators and it is the parties' responsibility to ensure that the arbitrators have the necessary qualifications and are evenhanded.

STB's role is not to second-guess arbitrators chosen by management and labor.

As the Supreme Court ruled, a review of arbitration decisions is limited to various specific

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circumstances. I see no reason to change what rail-labor agreed to 60 years ago.

Also, I wish to say something with respect to my home state of California. I don't have anything for Oklahoma today, but California.

Nowhere are the benefits of this transaction more apparent than California, which is home to one of every nine Americans. One of every nine Americans of this merger has the support of Governor Pete Wilson, Attorney General Dan Lungren, the Public Utilities Commission, the congressional delegation, the ports that handle almost half of our Nation's waterborne international trade, and almost all rail shippers.

Attorney General Dan Lungren ordered an economic analysis with Southern Pacific. He found SP unable to compete but found the capital investments enough to satisfy the demands of shippers. It is a conclusion joined in by the railroad's largest union, whose members are working under a concessionary contract.

In fact, Southern Pacific's employees are
the best informed about that railroad’s financial problems. They are the best informed because they must live with the below-industry wages, even though California has one of America’s highest costs of living.

This merger will enable Southern Pacific to gain access to the capital resources necessary to upgrade track and other facilities and to renew the locomotive fleet, which is very important and critical. These investments are essential now in the corridor between Seattle and Los Angeles, called the I-5 is to be made competitive with passengers, trucks and if the Alameda corridor and the NAFTA agreement are to benefit the United States.

Finally, there is a group of people I want to congratulate. They are the people making possible for efficient transportation and American competitiveness in the world markets for more secure jobs as we compete in the international market. It is possible only because of investors, your shareholders, those who save more than they earn and invest the difference into companies such as Union Pacific, so it
may purchase locomotives, computers, train employees, and rehabilitate the SP.

UP stockholders repeatedly have been asked to give up portions of their projected savings to share them with shippers, unionized employees and communities. Union Pacific has negotiated in good faith and entered into concessionary agreements. They have gone the extra mile with regard to environmental concerns.

The stockholders and management of Union Pacific, the capitalists, are to be congratulated. Capitalism is about building and creating and always has been, always will be.

I cast my aye vote.

SECRETARY WILLIAMS: Vice-chairman Simmons.

VICE CHAIRMAN SIMMONS: Yes.

SECRETARY WILLIAMS: Chairman Morgan?

CHAIRMAN MORGAN: Before we get to that, do you have a statement?

VICE CHAIRMAN SIMMONS: I passed the Chairman a little yellow note here and asked her to
tolerate me as an admission of my three gray hairs.

My concerns are closer to home. I have been here 13 years.

I am concerned and I congratulate this Staff, starting with mail clerks, messengers, right up through the office directors, to the General Counsel, right up to this Board that we have today.

This is the finest Board with which I have ever served. This is the finest chairman with whom I have ever served. It is remarkable what has been done here. And I didn't want this -- everybody to jump up with what they did get or didn't get to pass this up, to praise these people that are working down in the bowels of our organization for what they have done and those that are sitting in front of me today.

It is a remarkable job, and I guess because maybe I'm expendable, I'm going to say something else. I respectfully -- and I underline respectfully -- urge this Congress and the President to give this Board the people and the necessary economic wherewithal to continue to do the fine job that has been demonstrated here today.