



Surface Transportation Board
Washington, D.C. 20423-0001

ENTERED
Office of Proceedings
October 25, 2021
Part of
Public Record

MEMORANDUM

TO: Cynthia T. Brown, Chief, Section of Administration, Office of Proceedings

FROM: Martin J. Oberman, Chairman

RE: Ex Parte Communications Related to Docket Nos. FD 36500 & FD 36514

DATE: October 25, 2021

On October 18, 2021, I received a letter from Steve P. Gorsline, General Manager of Sunflower State Industrial Railway, expressing views on rail mergers and attaching several news articles related to the notices by Canadian Pacific Railway Limited (Canadian Pacific) and Canadian National Railway Company (Canadian National) of their respective intents to purchase Kansas City Southern and its railroad affiliates (KCS). I have enclosed a copy of the letter with this memorandum. Because Canadian Pacific filed a notice of intent to file an application to acquire KCS on March 23, 2021, in Docket No. FD 36500, and because Canadian National filed a notice of intent to file an application to acquire KCS on April 20, 2021 in Docket No. 36514,¹ this communication is a prohibited ex parte communication pursuant to the Board's decision in Petition of Fieldston Co., Inc. to Establish Procedures Regarding Ex Parte Communication in Railroad Merger Proceedings, Docket No. EP 619 (STB served Jan. 8, 1997). Please place this memo and the enclosed material in the public docket of Docket Nos. FD 36500 and FD 36514.

¹ Canadian National filed a request to withdraw that notice of intent on September 16, 2021. That request was granted by the Board on October 20, 2021, after receipt of Mr. Gorsline's letter.



THE SUNFLOWER STATE INDUSTRIAL RAILWAY, LLC
Post Office Box 245 - Colony, KS 66015-0245



Honorable Martin Oberman
Surface Transportation Bd
395 E Street SW
Washington, DC 20423



Re: TRAINS Magazine article (Sept 2021)

The MISSION of the US Surface Transportation Board:
"The Surface Transportation Board is an independent federal agency that's charged with economic regulation of various modes of surface transportation, primarily freight rail. The STB exercises statutory authority & resolves disputes in support of an efficient, competitive, and economically viable surface transportation network that meets the needs of its users".

Good morning Chairman Oberman:

I SHARE your concerns over service & questioning rationale for mergers. As I push on to restore the abandoned Santa Fe RR route between Ottawa, Kansas & Humboldt, Kansas I point out the HUGE negative that comes from letting the Mega railroads abandon rail lines. In 1991, the ICC let the Santa Fe RR abandon this 60 mile line. Santa Fe cited "little traffic". Well of Course: They raised traffis ABOVE truck rate & chased away every last customer. They did this to sell off a UNDER PERFORMING route so 'the 'sleeker / slimmer' Santa Fe RR would make a nice merger partner. And it worked. Along came Burlington Northern Railway - to merge both railways.

So who won? Stockholders! Who lost? Here's my list (thus far):
a candy manufacturing plant, an automotive parts manufacturer,
5 fertilizer plants, 10 grain elevators, 7 lumber yards, 3 cement
plants and grain alcohol production facility.

And yet... the Santa Fe RR was able to convince the ICC that LITTLE traffic existed so it got it's abandonment wish. But 'look' at 'how' the Santa Fe RR was able to abandon service: raise its tarrifs to exceed truck charges, drive away traffic... Petition for the KCT RR (a.k.a "A&K RR Salvage Co) to come in & buy the Ottawa-Iola line for \$10.00 and then let the KCT RR (one year later) do it's dirty abandonment work. And now, 30 years later: I am in an uphill fight to get lenders to put money behind a plan restore rail service. The 'difficulty' is: IF Santa Fe RR couldn't make it work: how can a new Class III line do it? (They can't see the 'corruption' in this).

It might make sense - to suggest Class I railways that want to abandon their obligations - can do so But they have to put money into a Trust Fund so New owners like - The Sunflower State Industrial Railway, LLC can get the money it needs to do

what the Class I carrier decided it no longer wanted to do. Far fetched? Not at all. This way, stockholders & their get rich plans - get to take a stake (for better or worse) when their Class I line wants to pull the plug & run away scot free. Some of these greedy mergers & abandonments "might get a 2nd look": IF they couldn't just cash in & leave shippers on the hook. Yes when shipping costs MORE - Consumer's (not stock holders) Pay MORE. It's time to factor in WHO loses when a merger connects Point A in Canada with Point B in Mexico (ie, the KCS Ry) & shippers in the middle lose service as this slows getting from A to B "in a hurry". Bigger &/or Faster... (ie, Mergers) isn't always better.

Respectfully,

A handwritten signature in cursive script, appearing to read "Steve".

Steve P. Gorsline, General Manager
Sunflower State Industrial Ry, LLC

__ enclosures



FOR RELEASE

03/23/2021 (Tuesday) [PDF Version]

No. 21-13

Contact:

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202-245-1760

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The Surface Transportation Board has received a "notice of intent" regarding a proposed transaction that would place Canadian Pacific Railway Company and the Kansas City Southern Railway Company, both of which are Class I railroads, under common control. Under the Board's statutes and regulations, this proposed transaction would be classified as "Major" and would be the first major transaction to seek Board approval in more than two decades.

The Board is also reviewing the proposed acquisition of rail carriers owned by Pan Am Systems, and Pan Am Railways, a Class II railroad, by CSX Transportation, Inc., a Class I railroad. The STB expects to publish a notice in the Federal Register on Thursday determining whether this proposed transaction will be classified as "significant" or "minor."

Railroad transactions can have broad implications for the shape of the nation's transportation system going forward. The STB has exclusive authority to review these proposed transactions and to determine whether to issue requisite approvals. The agency intends to scrutinize the transactions carefully and diligently, in keeping with the applicable statutory and regulatory frameworks. Additionally, the agency is committed to moving forward expeditiously, while ensuring meaningful opportunities for public participation and stakeholder comment.

The freight railroad system is a crucial component of our Nation's infrastructure. It is both a key engine of economic growth and essential to maintaining our national security. It is important for us to make sure that the U.S. maintains a robust, efficient, competitive, and economically viable surface transportation network that meets the needs of its users. Over the course of the 25 years since its creation, the Surface Transportation Board has faced substantial railroad merger transactions, and I am fully confident in my fellow Board members and our staff to adjudicate these matters and reach the appropriate outcome on the merits.

###

NEWS

Canadian Pacific sweetens bid to purchase KCS

New offer is increase of \$2 billion, but still falls short of Canadian National's deal

CANADIAN PACIFIC HAS SWEETENED its offer for Kansas City Southern in the hopes that regulatory uncertainty would unravel Canadian National's merger agreement with KCS.

CP on Aug. 10 boosted its bid by \$2 billion, which values KCS at \$300 per share. That's \$25 per share higher than CP's previous offer but still \$25 below the offer the KCS board accepted from CN in May.

CEO Keith Creel said CP was making the offer in advance of an Aug. 19 KCS shareholder vote where the railroad's investors are being asked to approve the merger with CN. "The regulatory uncertainty of the proposed CN merger has placed KCS stockholders in the unfortunate position of having to vote on the proposed CN merger ... all the while not having any level of certainty with respect to whether the STB will approve CN's use of a voting trust," Creel wrote in a letter to KCS CEO Pat Ottensmeyer.

The Surface Transportation Board says it will rule by Aug. 31 on CN's request to place KCS into a voting trust while their



Kansas City Southern's Bossier City Local passes through Shreveport, La., on Jan. 8, 2020. Canadian Pacific has made a renewed bid to purchase KCS. William H. Davis Jr.

merger is under regulatory review. The CN-KCS merger is being judged under the board's more stringent 2001 merger rules.

The board in May approved CP's request to put KCS into a voting trust and would judge a CP-KCS merger under its older and less onerous merger review rules.

The voting trust issue is a key hurdle: KCS shareholders would receive their cash and CN stock only after KCS is placed into a trust.

"We are excited to provide KCS stock-

holders a significantly more attractive alternative to this situation: this opportunity to turn down the CN merger proposal and once again pursue a combination of CP and KCS — a more certain transaction which offers compelling short-term and long-term value that is actually achievable already has the benefit of STB approval use a voting trust and is, in our view, the only viable Class I merger," Creel wrote.

CN's response was a statement calling the new CP bid "another inferior offer." KCS said its board of directors would consider the new offer in accordance of the terms of its deal with CN.

The regulatory climate may have changed since CN and KCS announced their deal. STB Chairman Martin J. Oberman has questioned railroads' need to merge, and a Biden Administration executive order seeks to reduce the dominance of large corporations — including railroads.

CP and KCS reached a \$29 billion deal in March, but CN swooped in with a \$3 billion offer. CP's latest offer is worth \$3 billion. — Bill Stephens

CN, KCS eye route upgrade

'Springfield Speedway' a key to linking railroads

THE BIG PRIZE in a Canadian National-Kansas City Southern merger is connecting Canada, the U.S., and Mexico. But the combined CN-KCS route to Kansas City would receive the largest single merger-related investment to tie the networks together.

CN would spend \$250 million to create the Springfield Speedway, a new single-line route linking Kansas City with Detroit and Eastern Canada via the Illinois capital. The funding would beef up CN's 112-mile former Illinois Central Gilman Subdivision from Gilman, Ill., to Springfield and KCS's 288-mile former Gateway Western line from Springfield to Kansas City. CN's Gilman Sub is a 60-mph route with islands of centralized traffic control, while the KCS line is 40-mph dark territory with a saw-tooth profile and short passing sidings.

The upgrade rationale: connecting Kansas City to Eastern Canada and its ports for intermodal traffic and linking carload origins on CN with KCS destinations.

By upgrading the line through Gilman, CN CEO JJ Ruest says, "Kansas City would be directly connected to the port of

Montreal, the port of Halifax, and potentially the port of Quebec City and be connected with the East Coast trade not only for imports but also for exports."

Intermodal analyst Larry Gross says it's a stretch for Kansas City to be served by Canadian ports. U.S. ports are significantly closer. But he says lower costs at Canadian Atlantic ports could favor a CN routing for imports from Southeast Asia.

CN says that finding "match-back" loads for containers that otherwise would return to Asia or Europe empty boosts the competitiveness of its intermodal business and its port partners. The Kansas City area would provide exports of fertilizers, cereal grains, and other grain products.

"Kansas City is a smaller Chicago, I call it. All the Class I railways get there ... except for CSX. It's a great hub for business, especially in the grain world out there. But it's a great east-west connector as well as a north-south connector," says Doug MacDonald, CN senior vice president of special projects. "CN sees a lot of traffic going through there." — Bill Stephens

NEWS BRIEFS

Wabtec plans to market next battery-electric



WABTEC says it will sell its next generation of battery-electric locomotives, which will reduce fuel use and emissions of a locomotive consist by 30%. Tests of its first PLXdrive locomotive on **BNSF RAILWAY** in California brought fuel savings of 17%. *Taken: David L. Lippert*

The **SURFACE TRANSPORTATION BOARD** rejected the **CSX** application to acquire **PAN AM RAILWAYS** as incomplete, noting particular shortcomings in its analysis of competitive impacts, among other flaws. CSX said it would refile and address the STB's concerns.



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spread support from shippers and ports, which is crucial for gaining regulatory approval in Washington. By early June, more than 1,400 letters backing the merger had been sent to federal regulators.

CN expects the merger to generate \$1 billion in annual synergies, most of it new revenue from traffic growth that will flow from the first single-line service to and from Mexico. CN and KCS say they will cut days off current transit times by eliminating interchange and coordinating operations, including reducing switching by moving cars in larger blocks across their combined system.

To address competition concerns in the one area where the railroads' systems overlap, CN said it will sell the 70-mile KCS line that links New Orleans with Baton Rouge, La. Kansas City Southern's New Orleans Subdivision closely parallels CN's own former Illinois Central line, and the railroads jointly serve nine customers on the route. CN also said it would keep all existing KCS interchange gateways open, including the KCS-CP interchange in Kansas City.

Canadian Pacific — which reached a \$29 billion deal with KCS in March, only to have CN swoop in with a higher offer a month later — said the battle for KCS is



ES44DC No. 2243 leads a northbound CN train past the platform for the Amtrak station in Hammond, La., in June 2013. James Terrebonne

not yet over. CP contends that CN won't be able to proceed under its current KCS merger agreement if the STB declines the voting-trust application. If that were to occur, CP would seek to revive its merger with KCS. To the chagrin of KCS officials, CP also plans to forge ahead with its KCS merger application at the STB.

CP CEO Keith Creel says a CN-KCS

merger will upset the competitive balance of the North American rail network. CP will become the odd man out, at roughly half the size of the 26,500-mile combined CN-KCS network. And that, Creel says, will make CP an acquisition target or force it to seek a merger partner. "We will explore our strategic opportunities," Creel says. — Bill Stephens

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In the September issue

A cog to the top of the West

After a \$100 million rebuild, the **BROADMOOR, MANITOU & Pikes Peak Cog Railroad** is ready to tackle the 14,000-foot mountain, and we've got an inside look at this unique Colorado railroad. Bob Johnston explores the future of the tilting **TALIES**. We'll also look at the newest ways commuters will reach the Big Apple on **LONG ISLAND RAIL ROAD**. And if that's not enough, we'll hear from an expert on **BROKEN RAILS** about what causes them and how to prevent them.

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CEO Pat Ottensmeyer says. "Improved service will beget growth."

CN CEO JJ Ruest says the end-to-end merger will boost rail competition, take trucks off the highway, and benefit customers in all three nations. "We are very excited about the future and our combined companies," Ruest says.

The CN-KCS combination faced an immediate challenge: Whether the U.S. Surface Transportation Board will approve Canadian National's request to place KCS into a voting trust while the merger is under regulatory review.

The STB in May rejected CN's initial request to put KCS into a voting trust on procedural grounds, because the railroads had not yet filed their merger agreement. But the board also said it would take a more cautious approach to a voting trust involving a CN-KCS merger, and indicated that it had concerns over the \$19 billion in debt Canadian National would take on to finance the most expensive rail merger ever.

CN and KCS in late May filed their merger agreement and voting-trust application, which are being judged under the STB's untested and tougher 2001 merger rules. The voting trust does two things. First, it allows KCS shareholders to receive

CN train C758 passes an overgrown tractor in Glendora, Miss., on Sept. 1, 2018. A combined CN-KCS network would account for almost 1,200 of the state's 1,644 Class I miles. Bradley Bates

\$325 per share in a combination of cash and CN stock. Second, it allows KCS to operate independently while the merger is under review.

CN and KCS sought to show that the merger is in the public interest and that CN has the financial strength to acquire KCS. The railways argued that their deal is in the public interest because it would create new competition for BNSF Railway and Union Pacific between Texas and Chicago, as well as capture more freight off highways. CN also said it would not be

harmful if it were forced to sell KCS. "Divestiture poses no significant financial risk to CN, as it could sell KCS and easily cover the entire amount of its new debt," the railroads wrote. "Indeed, CP awaits in the wings with a keen interest."

CN had hoped for approval of the voting trust in June, but the STB set a schedule that made a ruling unlikely before late July, while also asking for more details on CN's finances. The railroads expect the STB to approve the merger itself by late 2022. The CN-KCS deal has won wide-



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News

A matter of trust

▲ A Kansas City Southern yard job works the railroad's yard in Monroe, La., on Dec. 13, 2017.
William H. Davis

CANADIAN PACIFIC WAS JILTED
at the altar when Kansas City Southern on May 21 selected Canadian National as its partner in a \$33.6 billion merger to create the first railroad linking Canada, the U.S. and Mexico.

KCS said CN's offer was the best for its shareholders, customers, and employees. "This transaction is directed at growth through improved service, faster transit times, shorter and more consistent routes.

technological innovation, and providing customers with more choices, including new and expanded single-line routes for rail customers that are more competitive with truck, barge, and other rail routes." KCS

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CP is the only KCS suitor that could gain regulatory approval, boost competition, and create a balanced North American rail system, Creel says. CP's lawyers warned, in a letter to the U.S. Surface Transportation Board, that if CN acquires KCS, CP would be the odd man out and forced to set off the final wave of railroad consolidation by seeking a merger partner among the other Class I systems.

CN responded by saying that CP was misleading KCS shareholders and that combining CN with KCS would enrich investors, enhance competition, and clear any regulatory hurdles.

Both railroads won widespread support from shippers, ports, and others for their proposed mergers with KCS. But CN and CP bickered over the extent to which a CN-KCS merger would affect competition.

CP claimed a wide swath of customers in the American Heartland would see their rail options reduced by having both the KCS and former Illinois Central main lines



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Canadian National makes bid for Kansas City Southern

\$33.7 million offer sets off battle with Canadian Pacific over smallest Class I

▲ All three sides of the current merger triangle — Canadian Pacific, Kansas City Southern, and Canadian National — are represented on this southbound CN train approaching Slinger, Wis., in April 2017. Matt Krause

LITTLE KANSAS CITY SOUTHERN — at 6,700 miles by far the smallest Class I railroad — is the pretty girl at the dance. Last summer, a pair of infrastructure funds unsuccessfully sought to take KCS private. That sparked merger talks between Canadian Pacific and KCS, which jelled into their \$29 billion merger deal announced in March. A month later Canadian National responded with a \$33.7 billion unsolicited offer that sought to take away CP's dance partner.

Why all the interest in KCS? The railroad's north-south main line stretches from Kansas City, Mo., deep into Mexico. Its cross-border traffic has doubled since 2012 and shows no signs of slowing down as intermodal, automotive, and refined prod-

ucts traffic all continue to grow. The pandemic laid bare an overreliance on manufacturing in Asia, and railroaders expect some of that production to shift to low-cost Mexico as part of a phenomenon known as near-shoring. Toss in the updated NAFTA agreement called USMCA, and you've got the potential for more growth by creating the first railroad to link Canada, the U.S., and Mexico.

"Overall, we are the better bid, the better partner, the better railway, and the best solution for KCS and for the North American economy," CN CEO JJ Ruest says. CN says combining with KCS would create \$1 billion in synergies, divert truck traffic to rail, and create shorter, faster stack-cleared routes from Mexico to Chicago, Detroit,

and Eastern Canada.

Adds Ruest: "What's really missing in North America at this point is really a true north-south transcontinental railroad."

That, of course, is precisely what CP is hoping to create with KCS, too. CP CEO Keith Creel was not surprised rival CN, his former employer, jumped into the fray. CN's offer — which comes in 21% higher than CP's — was "eye-opening," Creel says. But Creel said there was no reason to sweeten his railroad's bid for KCS because CN's dueling offer was so anti-competitive that it would never make it out of the starting gate. CP's deal with KCS was iron-clad, Creel insists, and CN's was so fraught with regulatory risk that it was "unattainable," a "fantasy," and "fool's gold."

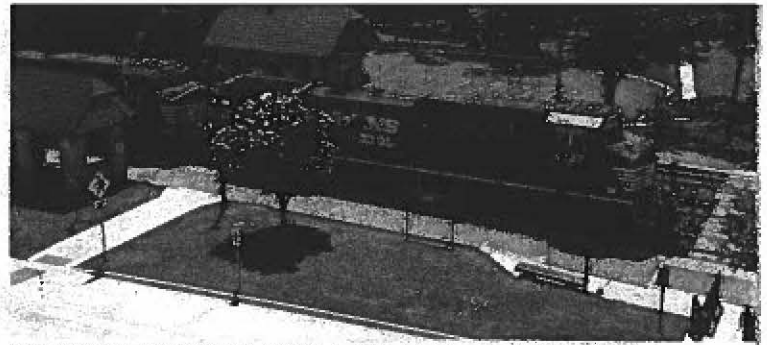
decrease in the level of the workforce over the last few years, I think something like 25%," Oberman says. Concerned those cuts have left Class I railroads unable to confront a crisis, he wrote all seven Class I CEOs about their ability to address freight demand, including crew and locomotive availability.

The publicly traded U.S. Class I roads have adopted Precision Scheduled Railroad operating models, cutting costs to reduce operating ratios and boost profitability.

From February 2017, the month before CSX Transportation adopted PSR, through December 2020, U.S. Class I rail employment fell 21% overall, but by an average of 26% at CSX, Norfolk Southern, and Union Pacific, according to STB data.

"We're seeing, I believe, some impact from that on the service side. Missed switches, crew shortages," Oberman says. "A lot of this stems from furloughs and quarantines from COVID, but I think it's also related to the fact that the whole workforce has been greatly reduced over the last few years, I think largely in response to pressures from Wall Street. And I am beginning to get concerned that this could start impacting capital expenditures as well."

CSX, NS, and UP have scaled back capital budgets the past few years. That's partly a result of winding down spending on posi-



A Norfolk Southern AC44C6M leads a BNSF train at Hinsdale, Ill., on June 13, 2021. STB chair Martin Oberman has questioned whether railroads have enough crews and locomotives.

tive train control implementation as well as halting the purchase of new locomotives as the railroads run fewer but longer trains.

The STB chairman also questioned the rationale for mergers, as well as the substantial premiums Canadian Pacific and Canadian National were willing to pay to acquire Kansas City Southern.

"I am all for promoting much more competition in the freight world, particularly among railroads and particularly with railroads getting more freight off the highways and onto the rails," Oberman says.

"But consolidating railroads even more than they have been, I don't see the argument about why that would help them get more freight off the highways."

What's needed, Oberman says, is more rail competition, not less.

"The thing that's impressed me most since I've come to the board is the lack of competition for most shippers in most parts of the country," Oberman says. Many are located on a single rail line with no opportunity for service from a distant second railroad, he explains. — Bill Stephens

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STB chief voices service concerns

Chairman of regulatory body questions Wall Street influence, need for mergers

▲ A Canadian National train of wind turbine blades rattles across the diamond at Wellsboro, Ind., on June 11, 2021. Two photos. **THREAT:** David Lassen

THE CHAIRMAN of the Surface Transportation Board is concerned pressure from Wall Street is undermining railroad service and has questioned the need for major rail mergers.

"Our mandate as an agency

... is to ensure and protect a strong national rail network. That's why we exist. And everything we do should be aimed at that outcome," STB Chairman Martin Oberman told an investor webcast in late May.

The influence of Wall Street — including the push for ever-lower operating ratios and aggressive share buyback programs — conflicts with the board's mandate, he says. "There's been a huge

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Matt Rose's warning comes true

Railroads become a target for regulators



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The railroad industry's chickens have come home to roost. Before he retired in 2019, BNSF Railway Executive Chairman Matt Rose warned that the other Class I railroads were inviting regulatory risk by adopting Precision Scheduled Railroading, reducing service, and demarketing some types of traffic in pursuit of higher profits. "We have this common-carrier obligation to provide freight service to all customers in all markets," Rose told an industry conference in January 2019. "And what we're doing in PSR is we're redefining what we're willing to accept in the freight railroad industry on certain lanes.



Former BNSF Chairman Matt Rose

And I really do believe we're going to get in a lot of trouble by doing that. "When you start redefining markets," Rose added, "I think then the federal policy makers will look at this, and quite frankly, they will not be happy with us." Well, guess what: New Surface Transportation Board Chairman Martin J. Oberman is not happy with railroads. He questions whether the Class I systems are shirking their common-carrier obligations due to pressure from Wall Street. "I have wondered ... whether the combination of the reductions in workforce, the interruptions in service, the demarketing all implicate the common-carrier obligation that railroads have and have had really since the beginning of the railroad industry," Oberman told the Midwest Association of Rail Shippers in July. "And it's something that I continue to focus my attention on."

Oberman said he fully supports the White House's call for increased competition in the rail industry. The Biden administration's July 9 executive order, which aims to limit the dominance of large corporations across the economy, dovetails with efforts already under way at the STB. "There are just many, many parts of the country ... where there's just not real effective competition among rail carriers," Oberman says.

The STB chief says his agency will take a look at hot-button issues like reciprocal switching, lifting exemptions on the regulation of certain commodities, and ways to more easily settle rate disputes. Reciprocal switching, which allows sole-served shippers to seek access to another nearby railroad via interchange, has been on the board's back burner since

2016. U.S. railroads vigorously oppose the reciprocal switching, calling it forced access. But Oberman wants action. "I have talked about it a lot. And it's not just talk," he says. "The concept of more competition ... is something very high on my list of concerns, and I hope we will be able to move forward in some fashion in that area."

We don't know what shape regulatory reform may take. The devil is always in the details. But it's clear that Oberman is likely to get the ball rolling — and that the Class I railroads won't like it much.

"I am frequently reminded by my friends in the railroad industry that we should butt out and the market should regulate rates



STB Chairman Martin J. Oberman

and service. And I agree. I think the market should regulate rates and service," Oberman says. "But ... for that to happen there has to be a market. And so to me, it is far better if we have more competition in the shipping and freight industry so we don't have to get involved."

Yet just nine days later Oberman asked all of the Class I railroads to provide information about congestion at their international intermodal terminals, where containers were stacking up faster than shippers could receive them due to pandemic-related factors largely beyond the railroads' control. The rub? Intermodal isn't even among the commodities the STB regulates.

It's unclear whether the Big Is Bad mood in Washington may affect the proposed Canadian National-Kansas City Southern merger, the first between Class I systems in two decades. CN and KCS have broad shipper support for their deal, and that's important. But obviously talk of reducing railroads' market dominance does not help a merger's prospects of winning regulatory approval.

The STB has become more activist in the past couple of years and has increased its scrutiny of all sorts of transactions, from CSX Transportation's proposed acquisition of New England regional Pan Am Railways to Canadian National's sale of former Wisconsin Central branches to shortline operator Watco.

If railroads have been downplaying the threat of onerous regulations — and ignoring Rose's prescient warning — then Oberman's comments should serve as a wake-up call. There's a new sheriff in town. **I**

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OF CONCERNS."
- MARTIN J.
OBERMAN,
STB**



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