

Public Benefits

Public Interest from 2000 version of the Code of Federal Regulation¹

49 CFR 1180.1(b)(1) (2000): "(1) Section 11324 directs the Board to approve consolidations which are consistent with the **public interest**. In examining a proposed transaction, the Board must consider, at a minimum: (i) The effect on the adequacy of transportation to the public; (ii) The effect of including, or failing to include, other rail carriers in the area involved in the proposed transaction; (iii) The total fixed charges that would result; (iv) The interest of affected carrier employees; and (v) The effect on competition among rail carriers in the affected region." Emphasis added.

1180(c): "(c) **Public interest considerations**. In determining whether a transaction is in the public interest, the Board performs a balancing test. It weighs the potential benefits to applicants and the public against the potential harm to the public. The Board will consider whether the benefits claimed by applicants could be realized by means other than the proposed consolidation that would result in less potential harm to the public.

(1) Potential benefits. Both the consolidated carrier and the public can benefit from a consolidation if the result is a financially sound competitor better able to provide adequate service on demand. This beneficial result can occur if the consolidated carrier is able to realize operating efficiencies and increased marketing opportunities. Since consolidations can lead to a reduction in redundant facilities and thereby to an increase in traffic density on underused lines, operating efficiencies may be realized. Furthermore, consolidations are the only feasible way for rail carriers to enter many new markets other than by contractual arrangement, such as for joint use of rail facilities or run-through trains. In some markets where there is sufficient existing rail capacity the construction of new rail line is prohibitively expensive and does not represent a feasible means of entry into the market. (2) Potential harm. [rest of text is omitted]." Emphasis added.

Public Interest from 2020 version of the Code of Federal Regulation²

49 CFR 1180.1(b) (2020): "Consolidation criteria. The Board's consideration of the merger or control of at least two Class I railroads is governed by the **public interest** criteria prescribed in 49 U.S.C. 11324 and the rail transportation policy set forth in 49 U.S.C. 10101. **In determining the public interest**, the Board must consider the various goals of effective competition, carrier safety and efficiency, adequate service for shippers, environmental safeguards, and fair working conditions for employees. The Board must ensure that any approved transaction would promote a competitive, efficient, and reliable national rail system." Emphasis added.

1180.1(c): "**Public interest considerations**. The Board believes that mergers serve the public interest only when substantial and demonstrable gains in important public benefits—such as improved service and safety, enhanced competition, and greater economic efficiency—outweigh any anticompetitive effects, potential service disruptions, or other merger-related harms. Although further consolidation of the few remaining Class I carriers could result in efficiency gains and improved service, the Board believes additional consolidation in the industry is also likely to result in a number of anticompetitive effects, such as loss of geographic competition, that are increasingly difficult to remedy directly or proportionately. Additional consolidations could also result in service disruptions during the system integration period. Accordingly, to assure a balance in favor of the public interest, merger applications should include provisions for enhanced competition, and, where both carriers are financially sound, the Board is prepared to use its conditioning authority as necessary under 49

¹ Code of Federal Regulations Title 49 at part 1180, subpart A (2000). Available at <https://www.govinfo.gov/content/pkg/CFR-2000-title49-vol6/pdf/CFR-2000-title49-vol6-part1180-id615.pdf>

² Code of Federal Regulations Title 49 at part 1180, subpart A (2020). Available at <https://www.govinfo.gov/content/pkg/CFR-2020-title49-vol6/pdf/CFR-2020-title49-vol6-part1180-id615.pdf>; Also, see eCFR (Electronic Code of Federal Regulations), available at <https://www.ecfr.gov/current/title-49/subtitle-B/chapter-X/subchapter-B/part-1180>

U.S.C. 11324(c) to preserve and/or enhance competition. In addition, when evaluating the public interest, the Board will consider whether the benefits claimed by applicants could be realized by means other than the proposed consolidation. The Board believes that other private-sector initiatives, such as joint marketing agreements and interline partnerships, can produce many of the efficiencies of a merger while risking less potential harm to the public.” Emphasis added.

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Figure 1: Summary of Public Benefits and Purchase Price (Excluding Assumed Debt) for Prior Transactions and the Applicants

Line	Description	Annual Public Benefits ¹ (millions)	Purchase Price ² (millions)	Annual Public Benefits per dollar of Purchase Price ³
1	Union Pacific and Southern Pacific	\$627.4	\$4,100	\$0.1530
2	CSX and Conrail	\$505.9	\$4,200	\$0.1205
3	Norfolk Southern and Conrail	\$492.3	\$5,800	\$0.0849
4	Canadian National and Illinois Central	\$137.4	\$2,400	\$0.0573
5	Average			\$0.1039
<u>CP-KCS Transaction:</u>				
6	Normal Year Indexed to 2025 and CP Disclosure on Dec. 8, 2021 (Estimated	\$194.6	\$27,200	\$0.0072
7	Normal Year Not Indexed to 2025 and Application Derived Estimated Purchase Price	\$172.8	\$28,333	\$0.0061
8	Highest CP-KCS Transaction Amount Relative to the Average of Large Transactions (Line 6 divided by Line 5)			6.9%

Notes and Sources:

- Public benefits are cost savings and cost reductions, and does not include incremental net revenue from diverted traffic.
- Purchase price excludes assumed debt.
- Given that the transactions occur at different points in time, the amounts for public benefits and purchase price are not comparable. The level of public benefits relative to the purchase price uses amounts that are contemporaneous to the transaction so the ratios of the different transaction are comparable.

Figure 2: Summary of Total Benefits and Purchase Price (Excluding Assumed Debt) for Prior Transactions and the Applicants

Line	Description	Annual Total Benefits ¹ (millions)	Purchase Price ² (millions)	Annual Total Benefits per dollar of Purchase Price ³	Payback Period Based on Purchase Price divided by Annual Total Benefits ⁴
1	Union Pacific and Southern Pacific	\$750.6	\$4,100	\$0.1831	5.5
2	CSX and Conrail	\$651.8	\$4,200	\$0.1552	6.4
3	Norfolk Southern and Conrail	\$791.8	\$5,800	\$0.1365	7.3
4	Canadian National and Illinois Central	\$216.2	\$2,400	\$0.0901	11.1
5	Average			\$0.1412	7.6
	<u>CP-KCS Transaction:</u>				
6	Normal Year Indexed to 2025 and CP Disclosure on Dec. 8, 2021 (Estimated	\$1,000.4	\$27,200	\$0.0368	27.2
7	Normal Year Not Indexed to 2025 and Application Derived Estimated Purchase Price	\$888.4	\$28,333	\$0.0314	31.9
8	CP-KCS Transaction Amount Relative to the Average of Large Transactions (Line 6 divided by Line 5)			26% ⁵	3.6 ⁶

Notes and Sources:

- 1 Total benefits are the sum of the incremental net revenue as private benefits and the public benefits.
- 2 Purchase price excludes assumed debt.
- 3 Given that the transactions occur at different points in time, the amounts for public benefits and purchase price are not comparable. The level of public benefits relative to the purchase price uses amounts that are contemporaneous to the transaction so the ratios of the different transaction are comparable.
- 4 Purchase price excludes assumed debt divided by the total benefits.
- 5 The 26 percent amount is computed as Line 8 divided by the average on Line 5. $\$0.0368/\$0.1412 = 0.26$ or 26%.
- 6 The 3.6 amount is computed as Line 8 divided by the average on Line 5. $27.2/7.6=3.6$

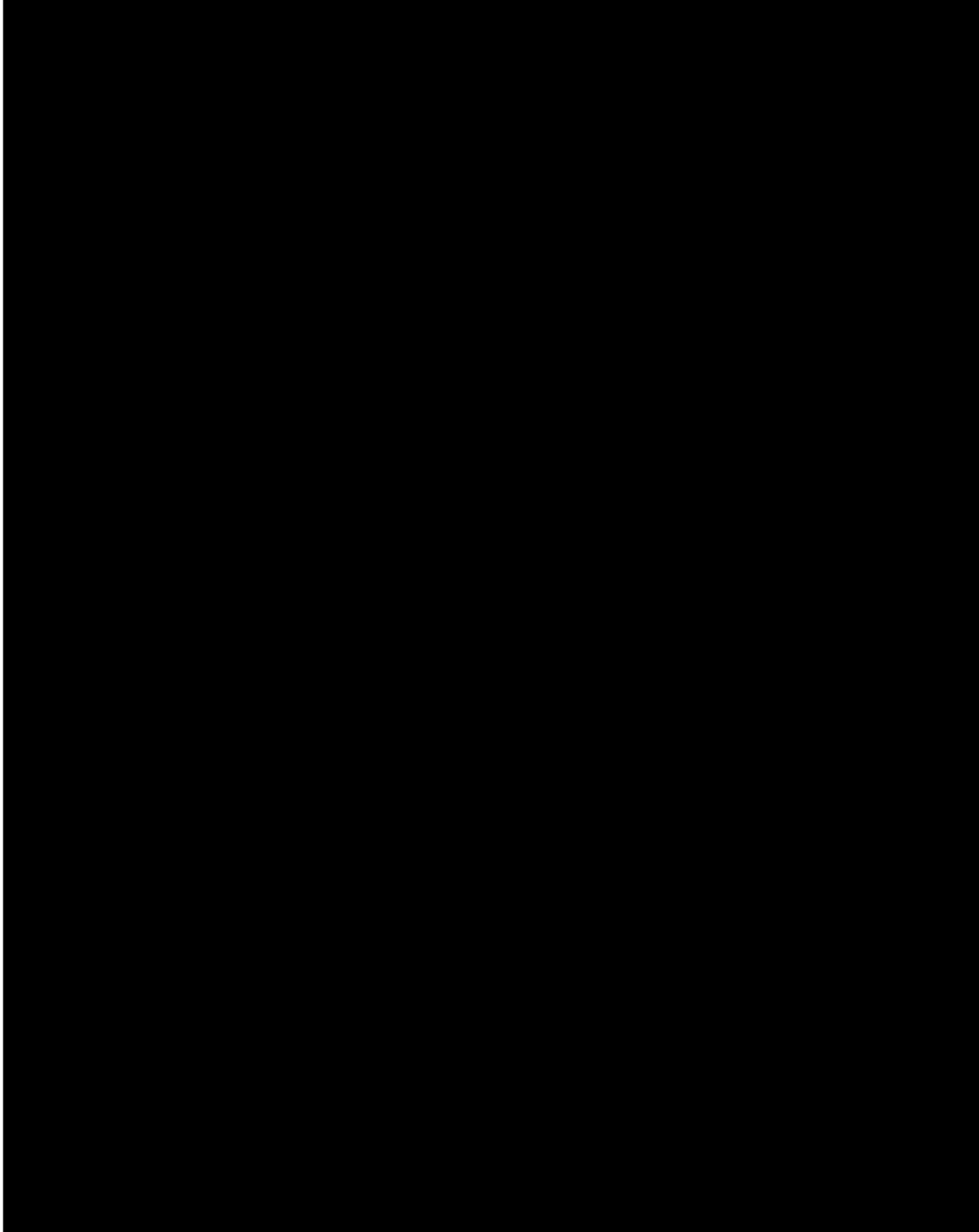
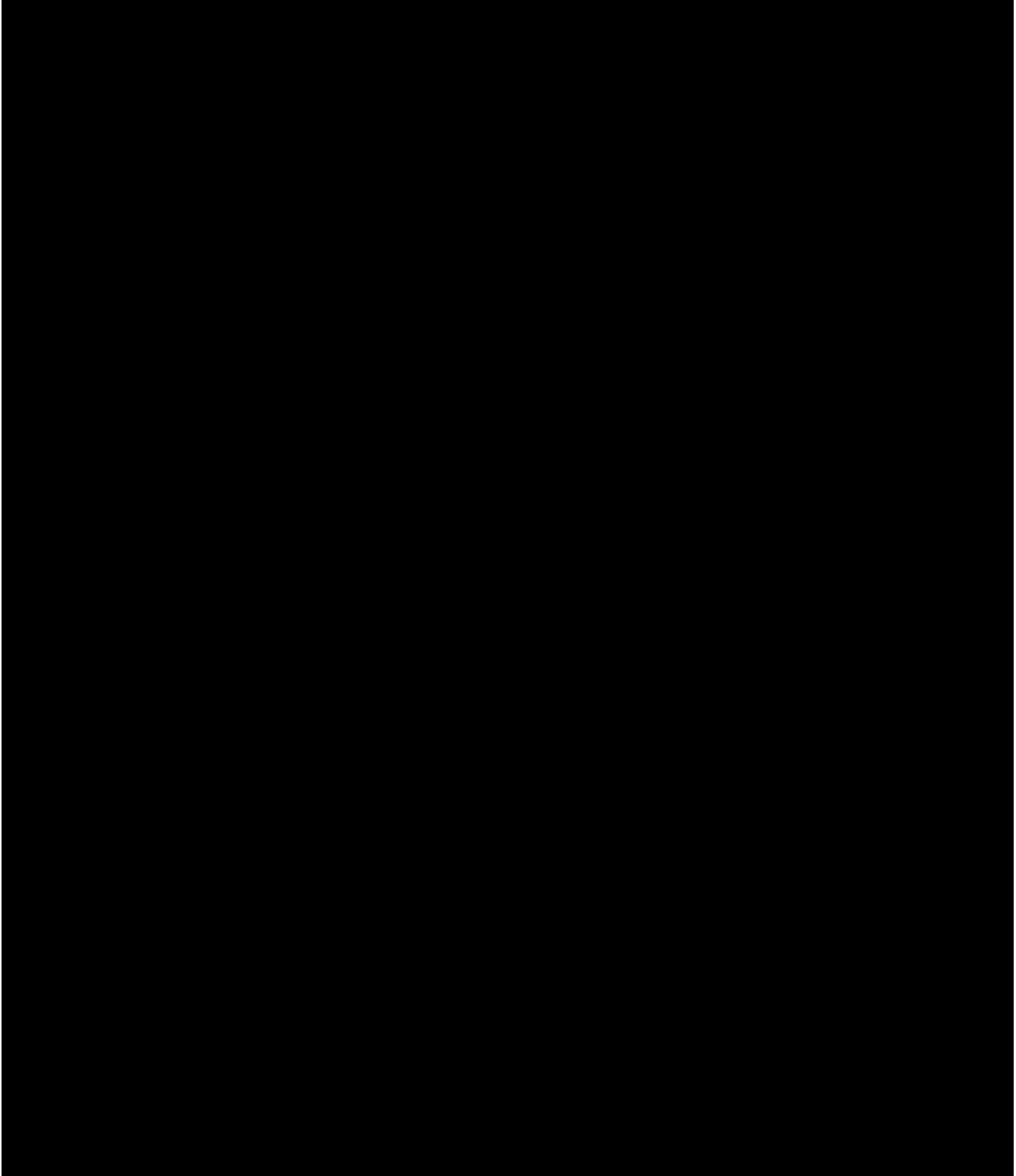
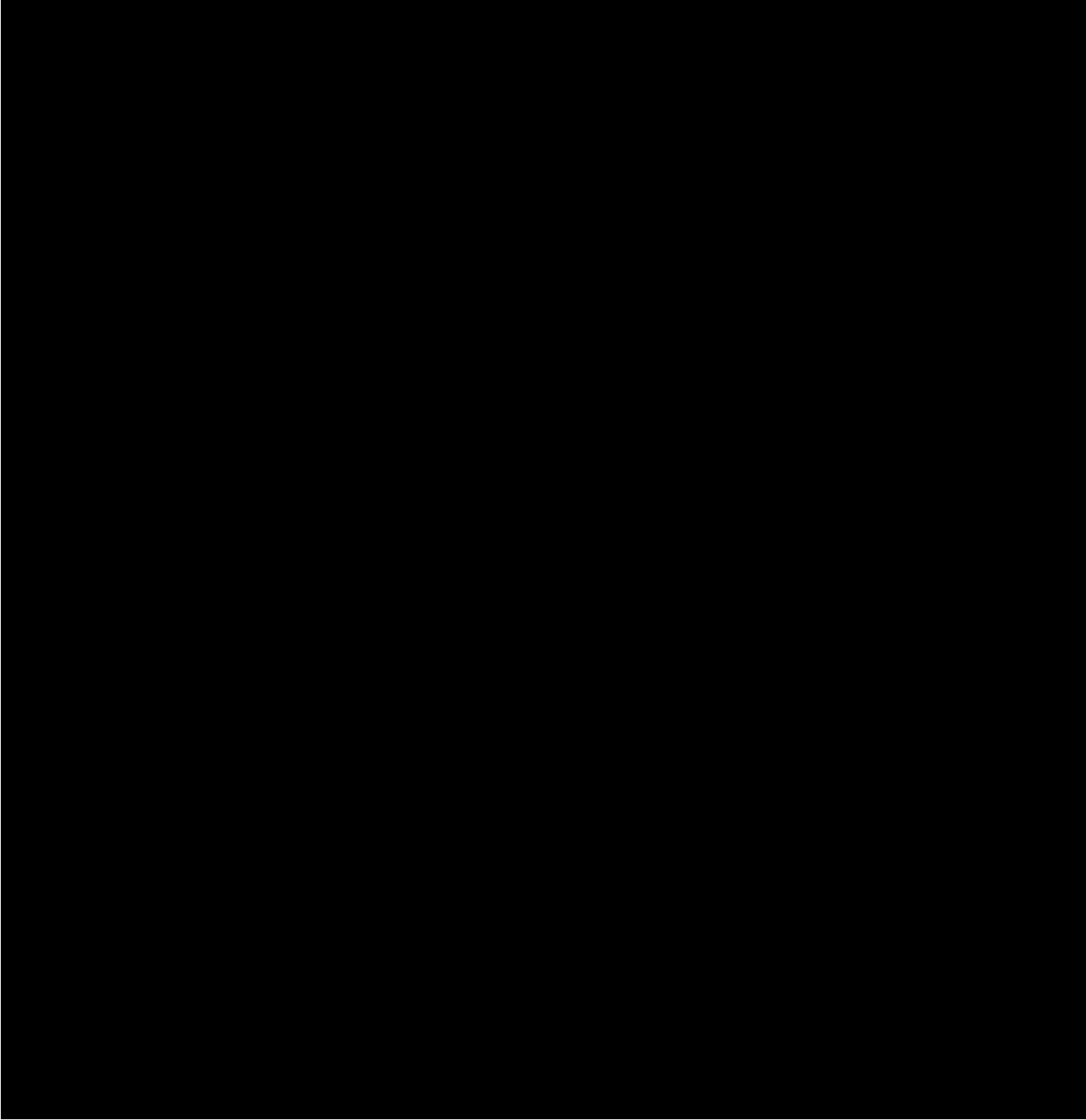


Figure 4: Correction to Applicant's Claimed Public Benefits to Remove Incremental Profits Associated with Unsupported Diversion Traffic



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Pages 375-376 from STB Decision in Union Pacific and Southern Pacific Transaction ⁴

UNION PACIFIC/SOUTHERN PACIFIC MERGER

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leading to the breakup of that company, or a substantial retrenching of its service. It might ultimately preclude the solution that we have before us, one that allows the network efficiencies of the SP system to be preserved, with tremendous public interest benefits. If SP were sold in pieces, shippers, labor, and SP shareholders would all be adversely affected. Substantial divestitures would almost surely destroy the BNSF agreement, which has its own substantial pro-competitive features and efficiency gains.

In sum, the merger benefits here outweigh any competitive harms of the transaction, and the public interest requires that we approve it. The conditions we are imposing will effectively mitigate the competitive harms of the merger, while preserving its benefits. We will turn now to a more detailed discussion of the various merger benefits and competitive issues that we have examined in carrying out our balancing of interests under the statute.

PUBLIC BENEFITS OF THE MERGER. Despite significant parallel aspects examined below, the merger as conditioned clearly will be pro-competitive in the sense that it will stimulate price and service competition in markets served by the merged carriers. The merger will create a more efficient and competitive UP/SP system competing head-to-head throughout the West with BNSF, whose efficiency was greatly enhanced by its recent merger. UP/SP customers will benefit from tremendous service improvements brought about by reductions in route mileage, extended single-line service, enhanced equipment supply, better service reliability, and new operating efficiencies. Similarly, BNSF shippers will receive substantial benefits from the improved service efficiency of that carrier as a result of the merger conditions that we are imposing. Shippers now served by SP, whose service is threatened by that carrier's decline, will now be assured of quality service by UP/SP or BNSF.

QUANTIFIABLE PUBLIC BENEFITS. Applicants argue that the merger will yield about \$752 million in quantifiable public benefits in a normal year, including just over \$580 million in operating efficiencies and cost savings,¹⁰⁵ \$76 million in net revenues from diverted traffic, and \$93 million in shipper logistics savings. We have excluded the \$76 million related to net diversion gains and \$47.2 million in net trackage rights proceeds from BNSF that should not be included as quantifiable public interest gains. This still leaves \$627 million of quantifiable benefits per year, as follows:

¹⁰⁵ Applicants have withdrawn a benefit claim of \$1.7 million in the procurement area. See, UP/SP-230 at 69 n.25.

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⁴ Decision, Union Pacific Corporation, Union Pacific Railroad Company, and Missouri Pacific Railroad Company – Control and Merger – Southern Pacific Rail Corporation, Southern Pacific Transportation Company, St. Louis Southwestern Railway Company, SPCSL Corp., and the Denver and Rio Grande Western Railroad Company, Finance Docket No. 32760, Decision No. 44, August 6, 1996, 1 STB 233 (1996) at 375-376.

*STB's Restatement of Applicants' Projected
Annual Efficiencies and Cost Savings
(in \$ millions)*

OPERATING BENEFITS	
Labor Savings	261.2
Non-Labor Savings	
Car Use	12.7
Communications/Computers	14.2
Operations	116.5
General/Administrative	129.7
Subtotal (Operating Benefits)	\$ 534.3
 SHIPPER LOGISTICS SAVINGS	 \$ 93.1
 TOTAL BENEFITS	 <u>\$ 627.4</u>

Thus, we find that applicants should realize public benefits from more efficient operations of \$534.3 million per year. These savings would reduce the combined UP/SP operating ratio by four or five points. BNSF's costs will fall further as well, as a result of the trackage rights. UP/SP will: (a) streamline and consolidate operations at major common terminals; (b) combine terminal and station facilities at a number of common points; (c) establish new blocks and new trains to improve service and efficiency; and (d) pursue numerous coordinations and consolidations of transportation, mechanical, engineering, information, purchasing, customer service, and other operating and marketing functions and activities. In addition, traffic will be handled more efficiently, in many instances by using shorter, faster routes. The combined car fleet will be managed on a coordinated basis to reduce empty movements and improve equipment use. Economies will also be achieved in applicant carriers' administrative functions by combining SP and UP departments to permit more efficient use of existing personnel and reduce overall staff and office space.

Several parties, notably DOJ and KCS, challenge applicants' calculation of quantifiable benefits. However, we find, in particular, the testimony of DOJ's witness Christensen to lack credibility. In the recently completed BN/SF merger proceeding, only one expert witness, Christensen, mounted a detailed challenge to the cost savings estimates in the application. Christensen, then representing selected utilities, claimed that the BN/SF merger would produce few quantifiable efficiency benefits. He asserted that the economic literature

Application is Missing Investment Necessary to Achieve Claimed Traffic Diversions

The Application is missing investment that are necessary to achieve the claim traffic diversions. For example, Wahba and Naatz in their Verified Statement claim” “We anticipate that this improved competitive posture will support additional investments by CPKC in rail capacity on our North-South main line, while also justifying investments by us and our prospective shippers in new facilities (like intermodal terminals, auto compounds, transloads, and others) that realize the full potential of the CP/KCS network.”^{5 6}

The Application does not identify the additional investments need to generate additional business to, from or through Mexico,⁷ which includes (1) Purchases of CPKC-owned containers, rail cars, locomotives, or facilities,⁸ (2) Infrastructure improvements at the border crossings in Laredo, TX and Brownsville, TX ⁹, and (3) Infrastructure improvements at the port of Lazaro Cardenas.

In response to an interrogatory, the Applicants produced a document that states { {“ [REDACTED]

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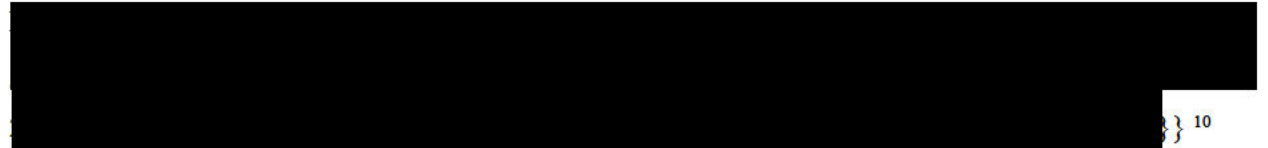
⁵ Wahba and Naatz V.S., at P 7.

⁶ The Application only provides for \$275 million in future investment to achieve the claimed transaction benefits. “Applicants expect to invest more than \$275 million in network capital expenditures to implement the Transaction, primarily to add double track, add and extend sidings, and install CTC signaling systems on the core CPKC North-South corridor lines between Louisiana and St. Paul/Chicago.” App. Vol. 1, p. 23.

⁷ CSXT asked questions regarding this topic area in its second set of requests to Applicants. Applicants Responses to CSXT’s Second Set of Discovery and Interrogatory Requests, February 18, 2022, No. 59.

⁸ Trade press indicates that CP-KCS will acquire additional assets to meet the future demand. “CPKC will acquire 265 multilevel auto-rack cars, 831 intermodal cars, 194 boxcars, and 604 covered hoppers to meet rising freight demand.” “CPKC will have a combined fleet of 2,421 units. The optimized plan will allow CPKC to store at least 135 locomotives, but by year three of the growth plan all 135 will be added back to the active fleet to handle traffic growth. CPKC estimates it will need an additional 14 units, which will come from locomotives currently not part of either railroad’s active fleet” Bill Stephens, “CP and KCS project dramatic rise in daily train counts”, November 2, 2021, available at <https://www.trains.com/trn/news-reviews/news-wire/cp-and-kcs-project-dramatic-rise-in-daily-train-counts/>

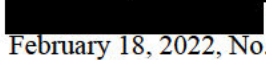
⁹ An article in The Journal of Commerce Online notes that there is “... chronic congestion over the Rio Grande bridge.” and that “KCS has received permits for a second span, but all of these infrastructure concerns will require capital investment.” Ari Ashe, “A merged CP-KCS would offer new cross-border intermodal growth ramp”, The Journal of Commerce Online, March 25, 2021, available at https://www.joc.com/rail-intermodal/class-i-railroads/canadian-pacific-railway/merged-cp-kcs-offers-new-cross-border-intermodal-growth-ramp_20210325.html

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For the other interrogatory questions regarding additional investments, the Applicants did not provide further information although Applicants' claimed the information was in specifically identified documents.¹¹

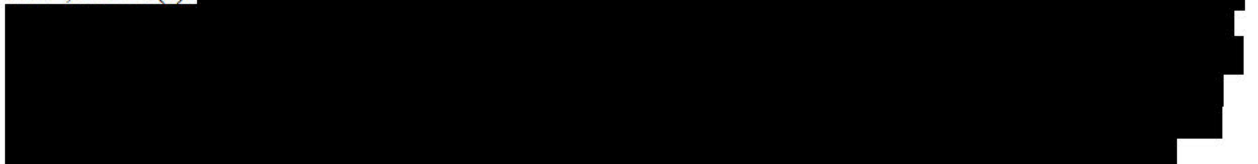
The Application has a number of statements made regarding investments in the Verified Statements that are unsupported, which are listed below.¹²

- a. "CP/KCS offerings will support investment in efficient new rail served grain elevators in the growing region of Southeastern Iowa." See Creel V.S. ¶ 25.¹³
- b. "CP and KCS were simply unable individually to financially justify certain infrastructure investments that were needed to unlock commercial opportunities to move more freight on intermodal trains." See Ottensmeyer V.S. 12.^{14 15}
- c. "CP anticipates that new investments in grain-loading capacity on CP's lines in the United States could begin as soon as the first year following control approval, taking advantage of the improved market access we will offer and our improved incentives to

¹⁰ 
 Applicants Responses to CSXT's Second Set of Discovery and Interrogatory Requests, February 18, 2022, No. 59.

¹¹ Applicants Responses to CSXT's Second Set of Discovery and Interrogatory Requests, February 18, 2022, No. 59.

¹² Applicants Responses to CSXT's Second Set of Discovery and Interrogatory Requests, February 18, 2022, No. 60.

¹³ Applicants Responses to CSXT's Second Set of Discovery and Interrogatory Requests, February 18, 2022, No. 60(a). 

¹⁴ In contrast, the 2021 CP Special Management Proxy Circular describes the success of the combination of CP and KCS depending upon KCS executing its business plan. **"Failure by KCS to successfully execute its business strategy and objectives may materially adversely affect the future results of the combined company and, consequently, the market value of CP common shares."** (Bold in original). "The success of the combination of CP and KCS will depend, in part, on the ability of KCS to successfully execute its business strategy, including making deliveries in a safe and reliable manner, minimizing service interruptions and investing in its infrastructure to maintain its rail system and serve its customer base. These objectives are capital intensive." Canadian Pacific Railway Limited, Notice of Special Meeting and Management Proxy Circular, Special Meeting of Shareholders to be held on December 8, 2021, November 1, 2021, p. 58, available at https://s21.q4cdn.com/736796105/files/doc_downloads/2021/11/CP-Circular_Bannerless.pdf

¹⁵ Applicants Responses to CSXT's Second Set of Discovery and Interrogatory Requests, February 18, 2022, No. 60(b). 

support those investments with attractive transportation services." See Wahba and Naatz V.S. ¶ 26.¹⁶

d. "CP anticipates that demand for fertilizers from Canada moving via efficient CPKC single-line routes to growers in Southwestern Missouri could support future investment in a potash shed on KCS's lines south of Kansas City. Such an investment could enable the rail Movement of potash originating on CP in Fort Saskatchewan, AB." See Wahba and Naatz V.S. ¶ 33.¹⁷

e. "The broader reach of the combined CP/KCS network will open up opportunities for investment in intermodal network expansion that would not have made sense for CP or KCS standing alone." See Wahba and Naatz V.S. ¶ 54.¹⁸

f. "CP's access to substantial originations of automotive traffic, will open up opportunities for the investment in traffic growth that would not have made sense for KCS standing alone." See Wahba and Naatz V.S. ¶ 77.¹⁹

g. "With the CP/KCS combination, the combined company would explore investing in a new auto compound adjacent to KCS's lines in the Beaumont/Port Arthur area (where UP's restrictions would not apply) that could allow CP/KCS to offer single-line Movement of finished autos from assembly plants in Ontario and imported autos from the Canadian ports served by CP to all of Eastern and Central Texas." See Wahba and Naatz V.S. ¶ 78.²⁰

¹⁶ Applicants Responses to CSXT's Second Set of Discovery and Interrogatory Requests, February 18, 2022, No. 60(c). [REDACTED]

¹⁷ Applicants Responses to CSXT's Second Set of Discovery and Interrogatory Requests, February 18, 2022, No. 60(d). [REDACTED]

¹⁸ Applicants Responses to CSXT's Second Set of Discovery and Interrogatory Requests, February 18, 2022, No. 60(e). [REDACTED]

¹⁹ Applicants Responses to CSXT's Second Set of Discovery and Interrogatory Requests, February 18, 2022, No. 60(f). [REDACTED]

²⁰ Applicants Responses to CSXT's Second Set of Discovery and Interrogatory Requests, February 18, 2022, No. 60(g). [REDACTED]

h. "CP/KCS Transaction will support the investments needed to accelerate the transition away from traditional crude-by-rail and towards the Movement of Alberta crude in private cars in non-hazardous DRUbit form." See Wahba and Naatz V.S. ¶ 92. ²¹

i. "Transition to DRUbit from investments prompted by CP/KCS Transaction displaces traditional (flammable/hazardous) crude-by-rail volumes." See Wahba and Naatz V.S. Figure 11. ²²

j. "CP and KCS have been at the forefront of a transition toward a safer and more efficient way to move Alberta Crude by Rail. Through investments at origin and destination, the hazardous dilbit can be converted to non-hazardous "DRUbit" that can be more safely moved by rail." See Wahba and Naatz V.S. ¶ 90. ²³

k. "The benefits of a new, strong, competitor against other railroads and trucks that will possess new single-line services and routes will accrue to customers, employees, shareholders, and stakeholders. It will unleash new infrastructure investment that CP and KCS standing alone could not justify." See Ottensmeyer V.S. 2-3. ²⁴

l. "CP and KCS have already determined that there are several opportunities to route freight in more efficient ways, Including by routing certain freight away from Chicago. These new routings will require new infrastructure investment, investment that could not be justified if the parties were to remain separate entities." See Ottensmeyer V.S. 7. ²⁵

²¹ Applicants Responses to CSXT's Second Set of Discovery and Interrogatory Requests, February 18, 2022, No. 60(h). {{[REDACTED]}}

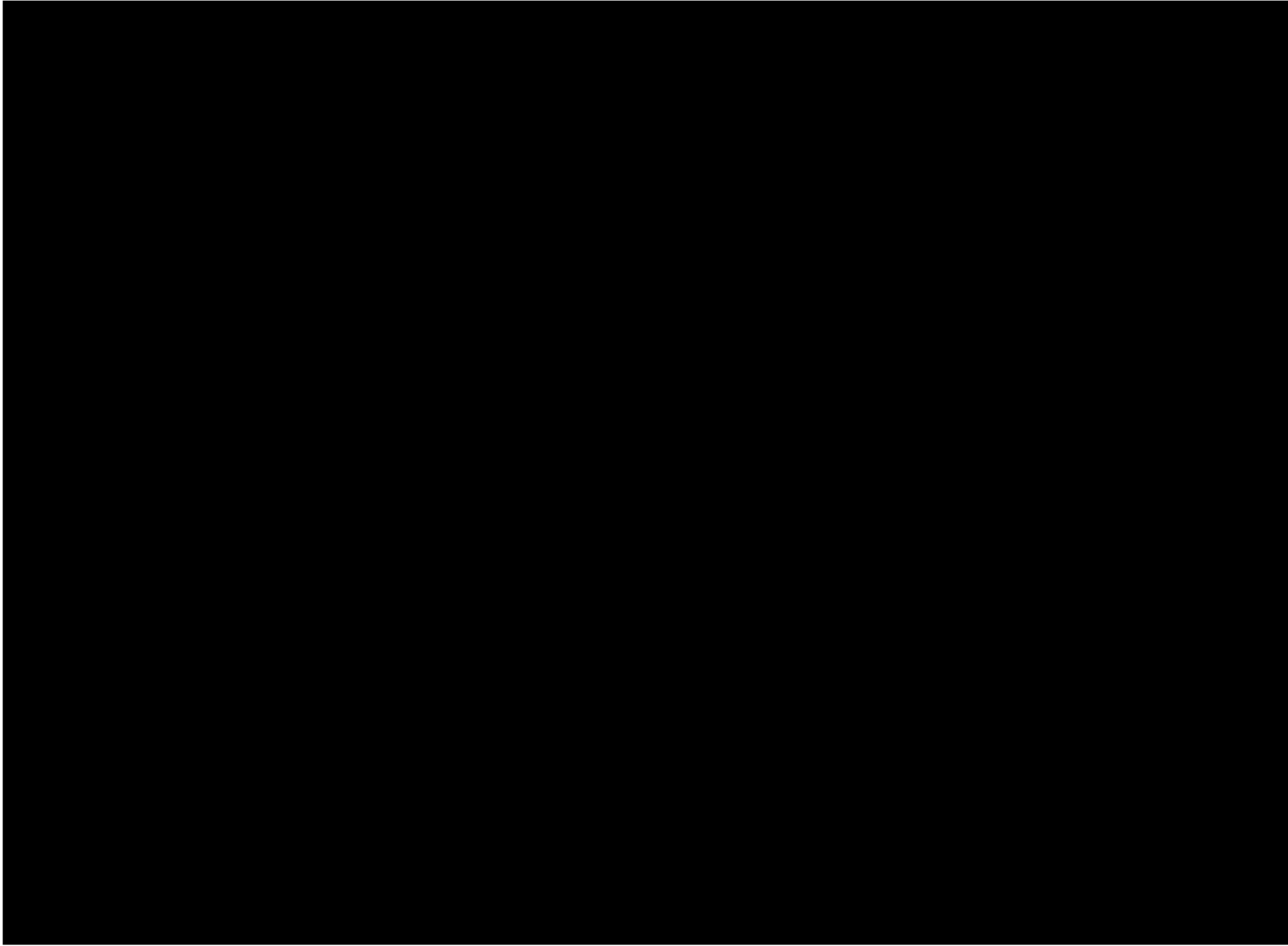
²² Applicants Responses to CSXT's Second Set of Discovery and Interrogatory Requests, February 18, 2022, No. 60(i). {{[REDACTED]}}

²³ Applicants Responses to CSXT's Second Set of Discovery and Interrogatory Requests, February 18, 2022, No. 60(j). {{[REDACTED]}}

²⁴ Applicants Responses to CSXT's Second Set of Discovery and Interrogatory Requests, February 18, 2022, No. 60(k). {{[REDACTED]}}

²⁵ Applicants Responses to CSXT's Second Set of Discovery and Interrogatory Requests, February 18, 2022, No. 60(l). {{[REDACTED]}}

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