

BEFORE THE SURFACE TRANSPORTATION BOARD

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Docket No.36500

CANADIAN PACIFIC RAILWAY LIMITED; CANADIAN PACIFIC RAILWAY
COMPANY; SOO LINE RAILROAD COMPANY; CENTRAL MAINE & QUEBEC
RAILWAY US INC.; DAKOTA, MINNESOTA & EASTERN RAILROAD CORPORATION;
AND DELAWARE & HUDSON RAILWAY COMPANY, INC.

-CONTROL-

KANSAS CITY SOUTHERN; THE KANSAS CITY SOUTHERN RAILWAY COMPANY;
GATEWAY EASTERN RAILWAY COMPANY; AND THE TEXAS MEXICAN RAILWAY
COMPANY

U.S. WHEAT ASSOCIATES FINAL BRIEF

U.S. Wheat Associates (USWA) respectfully submits its Final Brief in the above-captioned proceeding. USWA opposes this transaction as it is inconsistent with the public interest. Alternatively, if the Board approves this transaction, USWA respectfully requests that certain conditions be imposed on this transaction in accordance with 49 U.S.C. § 11324(c). USWA seeks these conditions to eliminate the adverse impacts this transaction will have on wheat shippers that are large rail shippers in the United States and the areas affected by this transaction.

USWA INTEREST IN TRANSACTION

USWA is the export market development organization for the U.S. wheat industry. USWA promotes the reliability, quality, and value of all six U.S. wheat classes to wheat buyers,

millers, bakers, food processors, and government officials in more than 100 countries around the world. Its mission is to “develop, maintain, and expand international markets to enhance wheat’s profitability for U.S. wheat producers and its value for their customers.” Funding is made possible through farmer dollars, goods, and services from 17 state wheat commissions, and cost-share grants from the U.S. Department of Agriculture’s Foreign Agricultural Service.

USWA created an internal Transportation Working Group (TWG) in 2018 after the realization that increasing rail rates were having a large impact on the wheat industry’s export competitiveness. TWG is a working group within USWA that examines rail and other transportation issues on behalf of these member Commissions. Wheat is heavily reliant first on exports, exporting on average half of all US production, and second on rail transportation to move this commodity across the U.S. to feed the world. Rail rates have a disparate impact on wheat shippers vis a vis other bulk US commodities due to the large percentage of production that is exported and having major growing regions not generally adjacent to the Mississippi waterways. Distances from the central and northern plains wheat producing areas are far too great to truck wheat to export facilities, making railroads a crucial and irreplaceable link in the wheat export logistics chain.

The results of this increased dependence on rail for the movement of wheat exports have been clear. Over the last decade, rail rates have increased exponentially, and wheat continues to be charged higher rates than other commodities with similar handling characteristics. These premiums relative to these other commodities clearly demonstrate the current market power of the Class I railroads and the lack of any serious competition afforded to wheat shippers.

That unchecked market power has had serious implications for U.S. wheat's competitive position vis a vis other major world exporters, such as Canada. The Canadian comparison is particularly telling as the two spring wheat and durum growing regions are similarly positioned in the interior of each country, with nearly identical distances to traverse to export facilities in each country, with differing government rail policies being one of the only large differences in market position. However, despite the similarities, work collected by one of USWA's member states showed similar origin to export point rail moves in Canada were 30% below the US moves at the time.

Specifically, USWA has some concerns about how this transaction will affect wheat shippers in the U.S. While USWA welcomes the addition of the CP's Northern US plains network to the KCS system, we are concerned that Canadian shippers may gain an unfair advantage over US wheat shippers. Canadian railroads, including the CP, have a recent history of involvement from the Canadian government. Revenue caps, known as Maximum Revenue Entitlement or MRE, on grain transportation movements to port facilities effectively limit rail rates by statute, rather than the market, lowering the transportation costs that exporters must pay for grain. This in turn means that Canadian exporters can undercut U.S. exporters. USWA has routinely raised these export subsidy concerns before the U.S. government.¹ Mandated grain shipping minimums during times of supply chain logistics challenges, implemented as recently as 2014, have shown the Canadian government's willingness to prioritize Canadian grain shipments over other sectors and originations.² In addition, Canadian shippers currently have

¹ See USWA Comments to Office of United States Trade Representative, USTR-2018-0029, Canada, Oct. 30, 2018, <https://www.regulations.gov/comment/USTR-2018-0029-0043>.

² See Wall Street Journal, *Canada Mandates Higher Minimum Grain Shipments for Railroads*, Aug. 1, 2014, <https://www.wsj.com/articles/canada-mandates-higher-minimum-grain-shipments-for-railroads-1406913099>

access to policy tools such as their final offer rate arbitration and competitive switching that provide them with an edge vis a vis US producers. The results of those policies have become clear over time. If that advantage were to extend to Canadian shipments farther into the US domestic market, and into Mexico – great harm could come to the US wheat industry. As such, it is important that the STB consider measures such as more competitive access and additional transparency measures to ensure that this merger results in healthy competition between railroads and their customers, rather than a further consolidation of market power and uneven advantages accruing to certain shippers.

Moreover, Mexico is USWA's largest export customer, taking in more than 3 million tons of wheat from the US annually. An increasing share of that wheat is moving directly to Mexico via rail. Mexican customers and US elevators have increasingly added shuttle train capacity to support those moves. More than 75% of current year shipments to Mexico have been shipped via direct rail, resulting in lower costs, faster transit times, and greater predictability for both shippers and receivers.

Furthermore, the current KCS railroad encompasses large portions of US winter wheat production, adding the CP network to that system is projected to dramatically increase traffic on the now-KCS lines, potentially driving rates higher for US wheat producers, and possibly straining a system under a great deal of scrutiny for service and delay issues.

Wheat shippers have been adversely impacted by the consolidation of the rail industry and their increasingly captive status in many locations. Further consolidation of the rail industry will only make this impact worse. Moreover, USWA has serious concerns discussed above about how this transaction could impact the US wheat market because it could create new inroads into the US and Mexican wheat markets for rail-advantaged Canadian wheat shippers. Furthermore,

major rail mergers are infamous for causing massive rail service issues which is the last thing the country needs at this time. As a result, USWA is opposing this transaction or alternatively seeking conditions in the event the Board approves it.

STB VIEW ON FURTHER MERGER ACTIVITY

The regulations applicable to this transaction as noted are set forth at 49 C.F.R. part 1180, subpart A, in effect before July 11, 2001, pursuant to the waiver for a merger transaction involving KCS and another Class I railroad under 49 C.F.R. § 1180.0(b). These merger regulations were adopted soon after passage of the Staggers Act of 1980. The Board has explained that “the widespread financial distress faced by our nation’s rail carriers in the period leading up to enactment of that statute, and the associated deteriorating service levels faced by their customers, were due in large measure to an overly restrictive regulatory system that unduly limited the ability of railroads to effectively rationalize what was at that time a significant degree of excess rail infrastructure.”³ These merger regulations — aimed at encouraging railroads to formulate proposals that would help rationalize excess capacity so long as competition, access to essential service, and other public interest goals were not degraded — were in response to these serious problems affecting railroads and their customers at that time.⁴

As the Board explained, however:

The goals of that merger policy have largely been achieved. It does not appear that there are significant public interest benefits to be realized from further downsizing or

³ *Major Rail Consolidation Procedures*, EP 582, slip op. at 3 (STB served Mar. 31, 2000).

⁴ *Id.* See 49 CFR 1180.1(a) (The Surface Transportation Board encourages private industry initiative that leads to the rationalization of the nation’s rail facilities and reduction of its excess capacity. One means of accomplishing these ends is rail consolidation).

rationalizing of rail route systems, as there is little of that activity left to do. Looking forward, the key problem faced by railroads — how to improve profitability through enhancing the service provided to their customers — is linked to adding to insufficient infrastructure, not to eliminating excess capacity.⁵

Therefore, the Board noted that any additional rail mergers presently offer very little opportunity for additional efficiencies through elimination of excess capacity. And while extensions of single-line service as touted by Canadian Pacific here can offer benefits to railroads and their customers, the Board has expressed that these benefits could be better achieved, short of merger, through innovative joint marketing arrangements and other cooperative efforts, such as joint dispatching to more efficiently move trains through congested terminal areas.⁶ With respect to transactions like here, the Board advised that “[j]oint marketing arrangements, which enable railroads to offer joint-line service almost as seamless as single-line service, could be more practicable and more likely to be in the public interest when the carriers connect largely end-to-end, rather than competing over broad territories.”⁷ Further, the Board expressed concern that the integration of two large railroads is complicated and takes a significant amount of time, and has been associated with severe service disruptions.⁸

Additional service disruptions at the present time would be devastating to the U.S. supply chain. There are already major service issues on the U.S. rail network brought on by the

⁵ *Public Views on Major Rail Consolidation*, EP 582, slip op. at 6 (STB served Mar. 17, 2000).

⁶ *Major Rail Consolidation Procedures*, EP. 582, slip op. at 3.

⁷ *Id.* at 3, note 10.

⁸ *Id.* at 3.

pandemic and the widespread adoption of Precision Scheduled Railroading as the Board has noted and even held a major hearing on in April.⁹

The prospect of reducing the already small number of major Class I railroads even further is deeply concerning. As a result of the intense merger activity that took place in the 80s and 90s, the number of overall railroad companies has been reduced dramatically, and the size of the remaining carriers has increased correspondingly. This consolidation has resulted in less competition, higher rates, and poorer service over the last twenty years.¹⁰

OPPOSITION TO TRANSACTION/REQUEST FOR CONDITIONS

USWA opposed this transaction and alternatively sought conditions in its Comments/Request for Conditions filed on February 28, 2022 herein. In the filing, USWA noted that under 49 U.S.C. § 11324, the Board must consider the public interest in addressing rail mergers, considering, at a minimum, **adequacy of transportation to the public**; including other rail carriers in the area involved; **competitive effects**; financial impacts on the involved carriers; and impacts on employees. “The Board shall approve and authorize a transaction under this

⁹ See, e.g., *First-Mile/Last-Mile Service*, EP 767 (STB served Sept. 2, 2021).

¹⁰ See, e.g., Escalation Consultants, “*Economic Analysis: Consolidation and Increasing Freight Rail Rates*,” June 2021, <https://www.freightrailreform.com/new-report-finds-rail-customers-paying-a-steep-price-for-consolidation-and-dwindling-competition/>; Rate Reform Task Force, Report to the Surface Transportation Board, at 11, Apr. 25, 2019, <https://prod.stb.gov/wp-content/uploads/Rate-Reform-Task-Force-Report-April-2019.pdf>; U.S. Senate Committee on Commerce, Science, and Transportation, *The Current State of the Class I Freight Rail Industry*, at 9-10 (Sept. 15, 2010) (describing increased “pricing power” and higher margins for Class I railroads); U.S. Gov’t Accountability Office, *Freight Railroads: Industry Health Has Improved, but Concerns about Competition and Capacity Should be Addressed*, at 13-16 (Oct. 6, 2006) (documenting rate increases from 2000 to 2004, and explaining “the rail industry has continued to consolidate, potentially increasing the market power of the largest railroads. ...[A]ccording to freight railroad officials, shippers, and financial analysts, since 2004, rates have continued to increase as the demand for freight rail service has increased, and rail capacity has not kept pace with demand.”).

section when it finds the transaction is consistent with the public interest. The Board may impose conditions governing the transaction, including the divestiture of parallel tracks or requiring the granting of trackage rights and access to other facilities.” *Id.* at (c). In addition, the rail transportation policy set out in 49 U.S.C. § 10101 directs the Board, among other things, to promote safety, efficiency, good working conditions, an economically sound and competitive rail transportation system, and the needs of the public and the national defense.

USWA’s reasons for its opposition to this transaction are further loss of rail competition, unfair competitive advantage for Canadian wheat, and poorer rail service. These impacts from this transaction clearly make it inconsistent with the public interest, thereby requiring the Board to deny it.

As the U.S. Department of Justice explained in its comments¹¹ filed earlier in this proceeding:

Although on its face this transaction may raise fewer competitive problems than other possible combinations of Class I railroads, the Board should carefully consider the competition implications posed by this transaction. As the Board has recognized, a railroad merger can harm competition even if the parties do not compete head to head to provide single-line service between the same origin and destination pairs. As one example, railroads can also compete through “source competition”—that is, the ability of

¹¹ Comment of the U.S. Dept. of Justice, Apr. 12, 2021, at 9-10. STB is required to give substantial weight to any competition-related recommendations by the DOJ. 49 U.S.C. § 11324(d).

shippers to choose between railroads that can carry their goods to (or receive goods from) different endpoints.¹² As the Board has explained:

[S]ignificant losses in geographic competition could occur even where carriers truly are “end-to-end,” because there are many commodities (such as phosphate and soda ash) that have a limited number of sources. Similarly, a merger between BNSF and a Canadian carrier, even if largely end-to-end, could raise potential competitive concerns in western export wheat markets. End-to-end carriers that compete with each other geographically would stand to gain market power if we were to approve their merger without imposing effective conditions, which, as discussed above, could be difficult.¹³

Railroads can also compete by serving portions of longer multi-carrier or multi-modal shipping routes. For instance, CP and KCS might each provide part of competing multi-modal routes between Asia and the eastern United States or might compete to serve north-south routes by each partnering with other rail lines. A merger could reduce this type of competition by depriving current or future interchange partners of CP or KCS of a

¹² See Statement of Interest for the United States, *In re Rail Freight Fuel Surcharge Antitrust Litigation*, MDL Docket No. 1869, at 12-13 (July 13, 2020), <https://www.justice.gov/atr/casedocument/file/1294246/download> (explaining that two hypothetical railroads that interline to serve a move from San Francisco to New York, with one carrying the traffic from San Francisco to Chicago, the other from Chicago to New York, could still compete with one another for the business of a shipper in Chicago: “Thus, if a Chicago-based shipper disliked western carriers’ rates to San Francisco, it could shop for a lower price and send its product instead to New York on an eastern carrier if a market for its product existed in both cities. Western and eastern carriers are rivals in this scenario – they are not competitively neutral and they are certainly not partners.”); Russell Pittman, *Options For Restructuring The State Owned Monopoly Railway*, *Railroad Economics* 182 (2007).

¹³ *Major Rail Consolidation Procedures*, EP 582 (Sub-No. 1), slip op. at 16 (STB served June 11, 2001).

means to compete for this traffic, and thus reduce choices for shippers and ultimately raise prices.

Class I railroads that do not compete on a day-to-day basis for current shippers may compete in broader ways that are socially important, for example in seeking to attract new shippers to locate on their lines and in the adoption of technological and productivity enhancing innovations; or, correspondingly, they may coordinate tacitly or explicitly in anticompetitive actions.¹⁴ The Board has rightly been attentive to such concerns,¹⁵ and should carefully consider these issues when evaluating this transaction or other potential rail mergers.

Thus, before permitting additional consolidation, the Board should thoroughly examine the competition concerns raised by commenters and ensure that this transaction would not exacerbate these trends. As the Board recognized in adopting the 2001 major rail consolidation procedures, the consolidation that has already occurred in this industry means “There is little margin for error as we proceed ahead.”¹⁶

The number of Class I railroads has remained the same since 2001 when the Board expressed its strong concerns over any further major mergers and adopted the new merger

¹⁴ See Comment of The Freight Rail Customer Alliance et al., Apr. 1, 2021, at 3 (expressing concern that “the reduction in Class I railroads from seven to six, even if unaccompanied by further consolidation, will facilitate further rate and practice coordination in what is already a highly concentrated and coordinated industry.”).

¹⁵ See, e.g., *Petition for Rulemaking to Adopt Revised Competitive Switching Rules*, EP 711, slip op. at 9 (STB served July 27, 2016) (“[T]he consolidation of class I carriers ... could lead to reduced competitive options for some shippers and thus should be considered.”); Rate Reform Task Force, Report to the Surface Transportation Board, at 11, Apr. 25, 2019, <https://prod.stb.gov/wp-content/uploads/Rate-Reform-TaskForce-Report-April-2019.pdf> (“As a result of mergers, there are now only seven class I railroads, and they have rationalized their routings and increased rates.”).

¹⁶ *Major Rail Consolidation Procedures*, slip op. at 66.

guidelines. Now, CP and KCS want to change the landscape to only six Class I railroads in the US. As noted, the effects of rail consolidation in the 80s and 90s after 2001 have led to higher rates, less competition, and poorer service. The statement by Chairman Morgan at that time that there is little margin for error when addressing the next major merger is even more true today as the railroads have clearly used their market power to their overwhelming advantage and to the disadvantage of their customers over the past two decades. Therefore, the Board should deny approval of this transaction as it is clearly against the public interest.

Alternatively, if the Board approves the transaction, it should impose the three forms of statutory competitive access as conditions on this transaction for use by any shipper on the new CP/KCS system that is subject to market dominance or receives inadequate service.

Competitive access generally refers to the ability of a shipper to use the facilities or services of an incumbent railroad to extend the reach of the services provided by a competitor railroad. The provisions of 49 U.S.C. §§ 11102 and 10705 make three competitive access remedies available to shippers: the prescription of through routes, terminal trackage rights, and reciprocal switching.

For example, with respect to conditions that could help ameliorate the anticompetitive effects of a major transaction in the post-2001 era, in a quite similar situation, Canadian Pacific announced a proposal to acquire Norfolk Southern in November 2015. Canadian Pacific stated repeatedly that it believed its proposal to acquire Norfolk Southern would have a significantly pro-competitive outcome, emphasizing there is minimal overlap between the track networks of the two companies, and instead the merger would be a market-extension creating an end-to-end

transcontinental solution for customers in large parts of the US and Canada.¹⁷ In making this proposal, CP offered to include as a part of the transaction modified terminal access which would have allowed another carrier to operate over CP+NS lines to serve a customer if the customer is not receiving adequate service or is being charged an unreasonable rate. CP also offered to end the bottleneck pricing approach, allowing customers to obtain a separately challengeable rate to the customer's preferred interchange location. It noted that these proposals are consistent with the type of competitive enhancements that the STB has found would offset merger-related competitive harms.¹⁸ Also, in this proceeding, Applicants have already fully committed to keeping all existing gateways open both physically and commercially and ensuring that shippers' existing bottleneck rate regulatory options are not adversely affected by the transaction.¹⁹

These crucial competitive access conditions will help to alleviate the inevitable service issues that will occur when the two railroads begin to merge their operations. This outcome is one of the major reasons behind why the new merger guidelines were created and should not be taken lightly here.²⁰ The U.S. rail network is already under tremendous strain at the present time due to the use of Precision Scheduled Railroading and the ongoing supply chain issues caused by the pandemic. Both KCS and CP are Precision Scheduled Railroading railroads and could easily have crushing service issues from the implementation of this merger at a time when the country certainly does not need additional supply chain problems. As a result, by providing these captive

¹⁷ *CP Asks U.S. Dept. of Justice to Review Recent Meeting of Some Class I Railroads to Oppose CP Acquisition of NS* (Jan. 19, 2016), <https://www.cpr.ca/en/investors/cp-asks-doj-to-review-recent-meetings>

¹⁸ *CP Responds to Norfolk Southern White Paper* (Dec. 15, 2015), <https://www.cpr.ca/en/investors/cp-responds-to-ns-white-paper>

¹⁹ Applicants' Reply to Objections to KCS Waiver from 2001 Major Merger Rules, Apr. 12, 2021, at 21.

²⁰ *Major Rail Consolidation Procedures*, EP, slip op. at 3.

or inadequately served shippers with access to competing railroads, the Board would be ensuring a better transition during the implementation of this merger and protecting the U.S. from additional mayhem brought on by the service issues that will occur as a result of this transaction during a time when the national supply chain cannot afford any additional issues.

Moreover, as discussed, this further consolidation of an industry that is clearly overly consolidated already and lacking competition in many instances will only result in less competition, higher rates, and poorer service on this new rail system. While an end-to-end merger will not result in the normal 2-1 railroad effects that the Board has remedied in the past to preserve competition, the impacts of further consolidation of the Class I railroads will only decrease the options available to the shippers that are on these two rail systems as discussed herein. As a result, the time has come for the Board to remedy this loss of competition caused by this merger through these three competitive access remedies. The way to avoid deterioration in competition on this system is to introduce new competition. Otherwise, the new CP/KCS system will reap the benefits of this loss in competition at the sole expense of its shippers. In addition, by providing competitive access to wheat shippers in the U.S., they will be able to better compete with the Canadian wheat shippers who will now have improved inroads to access the U.S. wheat market and the valuable export market in Mexico due to the reach of this transaction across three countries.

Finally, as an additional condition, the Board should permit USWA access to unmasked Confidential Carload Waybill Sample (with masking factors) to study the impacts this transaction will have on the U.S. wheat market. If Canadian wheat shippers are receiving better rail rates than U.S. wheat shippers, thereby causing a loss in business because of this transaction,

the U.S. wheat industry should be aware of these issues. This result would certainly not be in the public interest and should warrant action by the Board.

APPLICANTS' REPLY TO CONDITIONS

Applicants argue in defense that USWA is using its comments in this proceeding to advance its longstanding efforts to have the Board order railroads to grant other railroads “reciprocal switching” access to on-line customers or other forms of competitive access. They argue this relief is untethered to any effect of this transaction and USWA offers no predicate evidence of a single shipper losing access to an existing rail option as a result of this transaction, or any evidence at all of any adverse impact on competition.

The Applicants claim these competitive access conditions USWA seeks are precisely the kind of broad industry restructuring that the Board’s precedents forbid. They also argue that conditions of this sort are especially inappropriate considering the Board’s conclusion that the pre-2001 rules should apply, under which the “competitive enhancements” USWA proposes are out of place. Applicants conclude with this statement that conditions untethered to transaction impacts and with such unpredictable effects are not permitted under the Board’s pre-2000 rules and precedents.

APPLICANTS' POSITION ON COMPETITION COMES FROM A BYGONE ERA IN THE RAILROAD INDUSTRY

Just because the transaction is being reviewed under the older merger guidelines does not change history and the devastating impact rail mergers have had on rail competition. As a result of mergers, reclassifications, and bankruptcies, the number of Class I railroads has plummeted from 40 in 1980 to seven, its current level, in 1998 upon the Board’s approval of the Conrail

transaction.²¹ In addition, the TRB Report noted that the UP-SP merger was approved by the STB in 1996, which was an extremely controversial decision due to the massive overlap between the networks of these two major railroads in the western half of the US. The TRB Report described the DOJ's concerns about this merger in detail, all of which have come to fruition. The DOJ explained that such a significant loss of rail competitors in the western half of the US from three to two Class I railroads would lead to "overwhelming competitive harm" as the combined railroad would use its market power unilaterally and through coordinated behavior with the single remaining competitor (BNSF). In granting approval, the STB focused on the financial benefits of the merger. The financially weak SP would become part of a financially strong UP network that would be in a better position to compete aggressively with the newly merged BNSF, to the benefit of shippers in western markets. The STB adopted UP's proposals to offset competition losses by providing trackage rights agreements to BNSF. The DOJ raised concerns about how long these arrangements would be effective and whether they even would be enforceable. In addition, the DOJ was skeptical of the public interest benefits the railroads claimed would result from mergers arguing they were overstated, not recognizable as public benefits, or achievable through other means. In general, the DOJ's concerns were like past criticisms of the Interstate Commerce Commission as being too accepting of industry estimates of efficiencies, cost savings, and other claimed benefits from proposed mergers. In other words, past competitive review of major mergers had been flawed at best.

The TRB Report went on to explain that by the end of this merger frenzy in 1999, the STB had expressed that the industry's excess capacity had been largely eliminated through line

²¹ Transp. Research Bd. of the Nat'l Acad, Modernizing Freight Rail Regulation ("TRB Report"), 156-166 (2015)

abandonments and prior mergers; therefore, the possibility of additional efficiencies from more mergers had been more or less eliminated.²² The STB became extremely concerned that another merger could result in a final round of mergers involving the remaining few Class I railroads.²³ Furthermore, the BNSF-CN merger was proposed in the wake of a severe and prolonged service meltdown after UP's merger with SP. Consequently, the STB imposed a 15-month moratorium on further merger applications until it finished reviewing its merger evaluation criteria.²⁴

In June 2001, the STB issued its *Major Rail Consolidation Procedures* to address its concerns about further rail consolidation.²⁵ In that decision, it noted the statutory requirement to use a public interest standard but stated that applicants would have to meet a more stringent standard to demonstrate that anticipated public benefits would be “substantial and demonstrable”, thereby outweighing any anticompetitive effects. It stated that

while 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.**²⁶

It is a well-established principle in economics that a small number of competitors may be able to coordinate, either explicitly or tacitly, to charge higher prices than would arise in a

²² *Major Rail Consolidation Procedures*, (STB served April 7, 2000).

²³ *Id.*

²⁴ *Id.*

²⁵ STB EP 582 (Sub-No. 1), June 7, 2001.

²⁶ *Id.* (emphasis added).

competitive market.²⁷ The rail industry is particularly susceptible to this kind of coordination because there are often only two class I railroads in a given region. As a result, railroads can easily monitor the actions of their competitors and “punish” competitors that make competitive offers to carry freight by competing aggressively for that railroad’s customers. Concerns about the effects of the rail industry concentration justify seeking new avenues by the STB to further competition in the industry. Obviously, the previous methods have not been successful.

Since the last wave of Class I mergers in the 90s, railroad markets are more concentrated, railroads have more pricing discretion, and railroad rates have more than doubled since 2002, rising twice as fast as general inflation.²⁸ As Chairman Oberman recently recognized, “since 2010, the [class I railroads’] owners have taken home more than an astounding \$183 BB (\$196 BB in inflation adjusted dollars) in buybacks and dividends, far more than the \$138 BB (\$150 BB in inflation adjusted dollars) spent on the [railroads’] infrastructure.”²⁹ Injecting competition through competitive access here may require additional investment and may trim these profits,

²⁷ U.S. Dep’t of Justice and Fed. Trade Comm’n, Horizontal Merger Guidelines § 7 (2010) (describing a “range of conduct” that constitutes coordinated interaction and discussing how market consolidation can make such conduct easier and more likely). See also generally GEORGE STOCKING & MYRON WATKINS, CARTELS IN ACTION (1947); George Stigler, A Theory of Oligopoly, in STIGLER, THE ORGANIZATION OF INDUSTRY (1968); F.M. SCHERER & DAVID ROSS, INDUSTRIAL MARKET STRUCTURE AND ECONOMIC PERFORMANCE, 3rd ed. (1990), at ch. 8; Louis Kaplow & Carl Shapiro, Antitrust, in A. MITCHELL POLINSKY & STEVEN SHAVELL, HANDBOOK OF LAW AND ECONOMICS, vol. 2 (2007), at sec. 3.2.

²⁸ See U.S. Bureau of Labor Statistics, Producer Price Index by Industry: Rail Transportation [PCU48214821], retrieved from FRED, Federal Reserve Bank of St. Louis; <https://fred.stlouisfed.org/series/PCU48214821>, February 8, 2022.

²⁹ Remarks of Chairman Martin J. Oberman to the North American Rail Shippers Association Annual Meeting (Sept. 8, 2021), at 1, 19 (emphasis in original), available at <https://www.stb.gov/wp-content/uploads/NARS-Speech9-8-21.pdf>

dividends, and stock buybacks, but it will hardly constitute a serious threat to the operation and financial health of the rail industry.

While Applicants claim that USWA's request for competitive access here is untethered to this proposed transaction, they completely ignore the basic economic principle that consolidation of the rail industry from a meager seven Class I railroads to six will lessen competition even further through tacit collusion. Moreover, Applicants only focus on 2-1 competition scenarios in response to USWA's request and completely ignore the *per se* geographic and product competition effects that will result from this transaction.

In other words, this is a completely new era in the rail merger arena. Merger benefits are minimal because of the elimination of excess capacity in the past and predictably will involve CP imposing its more advanced Precision Scheduled Railroading ("PSR") operating model on the KCS system. KCS has been known as the most customer responsive and pro-competitive railroad over the last 20 years. It did not slash its workforce like the other Class I railroads have done under the guise of PSR. Now, KCS will be swallowed into one of the original PSR railroads and will be forced to behave accordingly with less emphasis on customer service and more on elimination of costs.

On top of the lessening of competition through the further consolidation of the industry, the merger of these railroads at this time when rail service has been teetering on the brink of collapse with hundreds of customers forced to shut down their facilities at great cost due to poor service will only cause greater problems and possibly create rail gridlock like after the UP/SP merger. The Board should take a page from Linda Morgan's playbook and slow things down because all the evidence points to greater damage to the rail industry and the service it supplies if this merger is approved.

Moreover, in line with its request for these competitive access conditions, USWA fully supports the conditions requested by BNSF herein. This transaction is focused on obtaining access to Mexico for shippers on CP's network. More than two-thirds of the diversions and growth traffic that Applicants predict will result from the transaction involve shipments moving into or out of Mexico. As Applicants explain – and USWA agrees – Mexican production and consumption markets are growing and likely to become far more important in the future. The increasing importance of Mexican trade means that now more than ever U.S. wheat farmers need to be assured of fair and competitive access to Mexico over U.S. rail carriers considering the extensive amount of wheat exports from the U.S. to Mexico.

BNSF argues that the Board must make sure that the transaction, with the creation of a new Class I Mexican access juggernaut in the combined CP-KCS system, does not diminish that important access to Mexico for U.S. wheat shippers. Indeed, under the applicable legal standard, the transaction must preserve competition to gain approval. To meet the steep volume expectations, revenue projections, and other claims made to investors and to the Board, the combined CP-KCS will be incentivized to divert its traffic through rate manipulations away from competitive routings on other railroads.

Absent imposition of the conditions requested by BNSF, current and future U.S. wheat shippers could be harmed through a lessening of competitive options. BNSF plays a unique role in the Mexican transportation market. For the last quarter-century, BNSF has served the public interest as the replacement for competition that would have been lost when Southern Pacific (“SP”) merged into Union Pacific (“UP”) in 1996. The Board recognized the critical importance of this role when it provided BNSF with access to the Mexican border at Laredo. The Board did so by installing BNSF onto a UP/SP rail line that leads to Robstown, Texas – just west of Corpus

Christi – where BNSF could access Laredo via an interchange with an independent Texas Mexican Railway (“Tex Mex”), which presumably would have no incentive to disfavor BNSF traffic. The Board also gave BNSF trackage rights access to UP/SP lines in Texas leading to the Mexican border at Brownsville and Eagle Pass.

BNSF points out that the Applicants’ focus on Mexico raises two critical issues for the Board to address in this proceeding. First, the Board must ensure that the combined CP-KCS does not use its control over transportation into and out of Mexico via the important Laredo, Texas gateway to frustrate the Board’s competitive objectives in the UP/SP merger and to foreclose access to Mexico by BNSF and its shippers. Foreclosure at Laredo is not a theoretical concern. BNSF explains that following the acquisition in 2005 by KCS of Tex Mex and the predecessor to KCSM, BNSF’s rail movements across the KCS-controlled Laredo border crossing dropped precipitously. BNSF noted that over time, that it has become virtually impossible to compete for certain Mexico business over Laredo if KCS can also serve the business on the U.S. side of the border. BNSF further asserts that in direct contravention of the several open gateway commitments made by KCS when the Board approved the Tex Mex acquisition, KCS has exercised its control over the pricing of the Mexican portion of the movement, and at times, the routing of the US portion, to ensure that BNSF will be frozen out of the market. Accordingly, USWA strongly supports BNSF’s request that the Board must put in place more concrete and enforceable open gateway measures and remedies, including an independent and unqualified open gateway commitment for Laredo. Otherwise, the expansion of KCS’s network to include the large number of northern U.S. locations served by CP where a significant portion of the U.S. wheat crop originates will further solidify this lock-out of BNSF and many of its wheat customers from cost-effective access to Mexico through Laredo.

CONCLUSION

Based on the foregoing discussion, USWA respectfully opposes this transaction. Alternatively, if the Board approves the transaction, USWA asks the Board to impose these competitive access, including the BNSF conditions, and data conditions on this merger to prevent the loss of competition, to improve service, and to protect U.S. wheat shippers.

Respectfully submitted,

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Dated: October 21, 2022

Certificate of Service

I certify that I have, this 21st day of October 2022, served by email copies of the foregoing document on all parties of record in this proceeding and on the parties listed below, by first-class mail, postage-prepaid, or by email:

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