

BEFORE THE SURFACE TRANSPORTATION BOARD

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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

**Final Brief of
The American Chemistry Council, The Fertilizer Institute, and
The National Industrial Transportation League**

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The American Chemistry Council (“ACC”), The Fertilizer Institute (“TFI”), and The National Industrial Transportation League (“NITL”) (collectively “Joint Associations”) hereby submit this “Final Brief” on the application of Canadian Pacific Railway Company (“CP”) to acquire Kansas City Southern Railway Company (“KCS”) (collectively “Applicants”).¹

In their “Comments and Requests for Conditions,” filed February 28, 2022 (ACC-6/TFI-5/NITL-3) (“Joint Association Comments”), the Joint Associations offered conditional support for the proposed merger provided that the following three competitive concerns are satisfactorily addressed through appropriate conditions:

1. The loss of competition resulting from the extension of Applicants’ origin and destination bottleneck segments.
2. Potential adverse service impacts resulting from implementation of the merger.
3. The extension of CP’s tariff indemnity provisions for the transportation of toxic-by-inhalation (“TIH”) materials to movements that originate, terminate, or traverse the pre-merger KCS network.

Multiple railroad and shipper interests also filed comments that echoed one or more of these same concerns.² The Applicants contend that these conditions are unnecessary or inappropriate.

¹ All references to “CP” also include Canadian Pacific Railway Limited; Soo Line Railroad Company; Central Maine & Quebec Railway US Inc.; Dakota Minnesota & Eastern Railroad Corp; and Delaware & Hudson Railway Company, Inc. All references to “KCS” also include Kansas City Southern Corporation; Gateway Eastern Railway Company; and The Texas Mexican Railway Company.

² *E.g.*, “Comments of BNSF Railway Company,” at 16-50 (issue #1), 51-72 (issue #2) (filed Feb. 28, 2022) (BNSF-9) (“BNSF Comments”); “Union Pacific Railroad Company’s Comments and Request for Conditions,” at 12-46 (issue #1), 50-67 (issue #2) (filed Feb. 28, 2022) (UP- 10) (“UP Comments”); “Comments of The Chlorine Institute, at 2-4 (issue #1 & #3) (filed Feb. 28, 2022); Letter from U.S. Dept. of Agriculture (issue #1 & #2) (filed Feb. 28, 2022); Letter from U.S. Dept. of Agriculture (issue #3) (filed April 22, 2022).

The Applicants, however, are wrong. First, extended bottlenecks enable the Applicants to foreclose existing competition over competitive route segments. The Joint Associations' proposed remedy ensures that the Applicants cannot quote bottleneck rates on post-merger moves that foreclose competing interline alternatives and, in so doing, encourages the Applicants to share the merger benefits with shippers through their post-merger single-line rates. Second, merger-related service disruptions are a genuine concern due to the Applicants extensive trackage rights operations along the Gulf Coast, including through Houston. The Applicants' service commitment is full of platitudes but no substance. The Joint Associations have requested modest conditions to protect shippers in the event of service disruptions that are modeled on an agreement from a prior merger. Third, the Joint Associations have requested a condition to protect TIH shippers from the anti-competitive effects of extending CP's current TIH liability, indemnity, and insurance tariff requirements to TIH shipments over KCS lines. Because CP is on the record before the Board stating that it would not transport TIH traffic but for its common carrier obligation, there is a real concern that extending application of the CP tariff to movements over KCS will be anti-competitive for TIH traffic.

I. COMPETITION LOST THROUGH THE EXTENSION OF BOTTLENECK SEGMENTS.

A. The Vertical Competitive Harm of The Proposed Merger.

The Joint Associations have described significant harm to vertical competition that will be a direct consequence of the proposed transaction.³ This harm will occur because, at locations where either Applicant has a bottleneck, the merger will extend those bottlenecks over greater distances, potentially over the entire route of many movements. Because U.S. law guarantees the

³ See Joint Association Comments at 7-9.

origin carrier its long-haul in most circumstances, 49 U.S.C. § 10705(a)(2), the Applicants will be able to foreclose competition from other carriers over longer distances than either can do pre-merger.

Although this anti-competitive effect will occur for all movements that will have extended bottlenecks due to the merger, the potential harm is most prevalent for U.S.-Canada cross-border movements for two reasons.⁴ First, there will be a significant overlap between the CP and Canadian National (“CN”) rail networks in both countries, which means that large numbers of cross-border movements will experience this harm. Second, Interswitching in Canada means that there are large numbers of locations within Canada that have competitive rail options despite being physically captive to either CP or CN, which prevents those carriers from foreclosing competition from other carriers by exploiting their bottlenecks to favor their long-haul.⁵ This merger will subvert the pro-competitive effects of Interswitching on movements between U.S. and Canadian locations. On movements to and from KCS-served locations in the U.S. pre-merger, because KCS is neutral as to whether it interchanges with CP or CN, Interswitching forces CN and CP to compete regardless which carrier physically serves the Canadian location. The proposed transaction will destroy that neutrality and enable Applicants to favor their long-haul through non-competitive pricing of their U.S. bottleneck segment on interline movements with CN.

⁴ *Id.* at 8.

⁵ Interswitching is the Canadian equivalent of reciprocal switching in the U.S. See 49 U.S.C. 11102(c). In Canada, however, Interswitching is a right of all shippers at every location within statutorily defined distances, whereas U.S. law requires a showing of anti-competitive conduct by a carrier before granting reciprocal switching. This distinction makes this loss of competition most prevalent for cross-border movements between the U.S. and Canada.

Both BNSF Railway Company (“BNSF”) and Union Pacific Railroad Company (“UP”) have raised similar foreclosure concerns in their comments.⁶ The primary difference between their concerns and those of the Joint Associations is that BNSF and UP are focused on cross-border shipments from Mexico, in contrast to the Joint Associations’ concern generally with all extended bottlenecks and especially Canada cross-border movements. Despite this difference in geographic focus, the economic concepts underlying all three positions are very similar.

B. Application of the One-Lump Presumption Is Unwarranted.

Applicants cite Board precedent adopting the “one-lump” theory to argue that there will be no competitive harm from extended bottlenecks.⁷ They rely solely upon their promises to keep gateways open both physically and commercially as sufficient to prevent foreclosure without offering any means to validate their compliance with the latter of these commitments.⁸ Indeed, the Applicants reject all the proposals of UP, BNSF, and the Joint Associations to validate their compliance, insisting that none are necessary.⁹

The Joint Associations have challenged the practicality of applying the one-lump theory to carload traffic like that tendered by the Associations’ members, pointing out that the theory has been applied only in the context of unit train traffic in Board precedent.¹⁰ In addition, UP and BNSF have challenged the economic underpinnings of the one-lump theory based upon the

⁶ UP Comments at 12-32, 67-76; BNSF Comments at 16-51.

⁷ “Applicants’ Response, to Comments and Requests for Conditions, Opposition to Responsive Applications, and Rebuttal in Support of the Application,” Vol I, at 47-52, 59-68 (filed July 12, 2022) (CP-53/KCS-39) (“Applicants’ Response”). Applicants included two different sets of pagination. All page citations to Applicants’ Response herein are to the pagination identified as “Reply Volume I” on each page.

⁸ *Id.* at 110-12.

⁹ *Id.* at 112-123.

¹⁰ Joint Association Comments at 13-21.

evolution of economic thought since the Board last applied the one-lump theory nearly two decades ago.¹¹ Although the Applicants attempt to rebut the UP and BNSF economic testimony, they offer no response at all to the Joint Association arguments. Both sets of arguments, separately and together, demonstrate why the Board should not automatically apply its one-lump precedent to this transaction.

As the Joint Associations have pointed out, the one-lump precedent establishes a rebuttable presumption that an end-to-end merger does not harm vertical competition.¹² The theory assumes that, when any Applicant has a bottleneck segment at the origin or destination of a movement pre-merger, any extension of that bottleneck resulting from consolidation with a connecting carrier will not have anti-competitive consequences because the pre-merger Applicant already was in a position to capture the entire monopoly profit. Thus, the Board presumes that the merger has not increased the Applicants' market power or otherwise reduced competition.¹³ As a consequence of that presumption, the Board has shifted the burden of proof to shippers to rebut the presumption by showing both that the benefits of pre-merger competition over the connecting segment flowed through to the shipper despite its captivity pre-merger and that any such flow-through will be significantly curtailed post-merger. The Joint Associations noted that the one-lump theory is controversial, and its accuracy has long been disputed.¹⁴

¹¹ UP Comments at 32-46 and "Verified Statement of Steven C. Salop" at ¶¶ 21-72 ("Salop V.S."); BNSF Comments, "Verified Statement of David Reishus, PhD," at ¶¶ 31-51 (Reishus V.S.).

¹² Joint Association Comments at 14. *See also, Kansas City Southern – Control – The Kansas City Southern Ry. Co, Gateway Easter Ry. Co, and The Texas Mexican Ry. Co.*, STB Fin. Dkt No. 34342, Decision No. 12, slip op. at 17 (served Nov. 29, 2004) ("The Board has subscribed to the one lump theory (as a rebuttable presumption) in approving several end-to-end mergers.") ("KCS/Tex-Mex").

¹³ Joint Association Comments at 13.

¹⁴ *Id.* at 14.

In their comments, UP and BNSF provide economic testimony demonstrating a shift in economic thinking since the Board last applied the one-lump theory nearly two decades ago.¹⁵

The testimony of UP's economic witness, Steven Salop, illustrates the diversity of competitive impacts from end-to-end mergers that renders a rebuttable presumption in favor of such mergers both impractical and inappropriate:

46. The ultimate impact of the merger on shippers depends on the tension and magnitudes of these upward and downward pricing pressures. As a general matter, a vertical merger can lead to a diverse set of outcomes. In some cases, the merger can lead to higher rates borne by all shippers. This is the expected outcome when the merger-specific efficiency benefits are small. The merger alternatively can lead to higher rates borne by the shipper customers that rely on interline movements with the foreclosed independent carriers, while leading to lower rates for the shippers that opt for single-line service by the merged carrier. The merger also can lead to lower rates charged to all shippers. This is most likely to occur when both merging parties have monopoly positions and the merger-specific EDM and merger-specific efficiencies are very large. *Because carriers do not set uniform rates for all movements, a vertical merger can lead to a diversity of outcomes across commodity groups, routes and specific shippers.*¹⁶

Professor Salop constructed two versions of a general simulation model to demonstrate “that there is no economic basis for presuming that end-to-end rail mergers involving a monopoly carrier are procompetitive or competitively neutral.”¹⁷ Summarizing the results of these simulations, Professor Salop observes:

54. The results of the simulation models show that some or all shippers can be harmed from foreclosure effects of end-to-end mergers. They also show the possibility that some shippers can be benefited. Because the simulations cover such a broad range of circumstances to capture different competitive interactions, the

¹⁵ BNSF Comments, Reishus V.S. at ¶¶ 31-43; UP Comments, Salop V.S. at ¶¶ 21-72.

¹⁶ UP Comments, Salop V.S. at ¶ 46 (footnote omitted) (italics added).

¹⁷ *Id.* at ¶ 51.

models indicate a wide range of possible results for particular shippers. This is precisely the point. While the one-lump theory implies that the price to shippers would not change as a result of a vertical merger when one of the merging parties appears to have a monopoly over certain routes, the simulations show that significant price changes are far from being the exception and, in fact, occur in a broad set of market conditions. Thus, these results make it clear that the one-lump theory does not apply when there is product differentiation in the competitive segment. An end-to-end merger can harm some or all shippers, even after taking any EDM into account. *The simulation results thus also make it clear that a general procompetitive presumption cannot be justified with respect to the proposed merger on the basis of economic analysis.*¹⁸

Professor Salop's analysis thus leads to the ineluctable conclusion that a rebuttable presumption that a vertical merger does not harm competition is not justified.¹⁹

Applicants have the burden of proof to demonstrate that their combination is in the public interest, which includes a showing of no significant harm to competition. The one-lump presumption is inconsistent with that requirement by shifting that burden to opponents of the transaction to show that there is harm to vertical competition. Professor Salop's analysis demonstrates why the one-lump presumption is unreasonable.

Furthermore, as the Joint Associations have demonstrated, even if reasonable, the one-lump presumption cannot be rebutted as a practical matter by carload shippers.²⁰ The presumption must be rebutted for individual movements. But many carload shippers have hundreds of lanes that frequently shift, and they do not tender sufficient traffic over any single lane to justify the time and expense of attempting to rebut the presumption. That explains why

¹⁸ *Id.* at ¶ 54 (underline in original, italics added).

¹⁹ *See also*, BNSF Comments, Reishus V.S. at ¶ 43 ("Rather than a presumption of no harm, careful review of the proposed transaction, the markets, and the available evidence are required.").

²⁰ Joint Association Comments at 19-21.

the only attempts to rebut the one-lump theory in prior mergers have been made by unit train shippers with large traffic volumes over a handful of lanes at most.²¹ Thus, the burden shift that the one-lump theory imposes upon carload shippers is unreasonable.

The Board also has rejected arguments that vertical integration would foreclose efficient through routes, concluding that “there is no reason for a carrier to foreclose an efficient connecting carrier just to achieve a long-haul.”²² But as railroads have shifted more and more costs to shippers (*e.g.*, rail car ownership), the most efficient through route for the railroad may not be the most efficient for the shipper.²³ Yet the Board’s analysis ignores this distinction. Furthermore, the one-lump theory only considers competitive impacts upon rates, while ignoring service impacts.²⁴ Lastly, if two routes are of comparable efficiency, preserving its long-haul is sufficient reason for the bottleneck carrier to foreclose a competitive alternative route. The Applicants’ reply ignores these points.

Instead, the Applicants assert that:

there is exactly zero evidence (at least over the past multiple decades) that mergers have even led merging railroads to shut down efficient routing options that shippers had preferred pre-merger by implementing ‘foreclosure’ strategies. To be sure, they won traffic away from less-efficient interline routes by persuading shippers to switch, but in the decades-long history of oversight of end-to-end mergers there has *never* once been a finding that a gateway was closed, much less in the face of commitments made to the Board to keep those gateways open.²⁵

²¹ These are the same obstacles that effectively have prevented carload shippers from employing the stand-alone cost (“SAC”) methodology to challenge the reasonableness of rail rates.

²² *Burlington Northern Inc. et al. – Control and Merger – Santa Fe Pac. Corp. et al.*, 10 I.C.C.2d 661, 751-52 (1995).

²³ Joint Association Comments at 15.

²⁴ *Id.* at 16.

²⁵ Applicants’ Reply, Vol I, at 73 (*italics in original*).

That observation should not be surprising in the absence of any standard to determine whether a gateway has been *commercially* closed and the obstacles described above to carload shippers' ability to rebut the one-lump presumption.²⁶

The Applicants suggest that shippers "will know if [Applicants' Rule 11 bottleneck] rate is the reason why an interline route they previously relied upon is no longer viable."²⁷ That is overly simplistic for several reasons. First, how does the shipper (and the Board) distinguish situations where the interline route is no longer viable due to the greater efficiency of the single line route from situations involving foreclosure? The only hint in Board precedent is for the shipper to challenge the reasonableness of the Rule 11 rate.²⁸ But the Board's rate reasonableness standards are designed to determine a maximum level of differential pricing for captive traffic, not to determine foreclosure resulting from a vertical merger. Second, what is the remedy? Again, a rate case is not designed for that purpose. But just as important, the Joint Associations have demonstrated that it is not a practical remedy for carload shippers.²⁹

The comments in this proceeding demonstrate why the Board should not automatically apply the one-lump presumption to this transaction. The question thus becomes how the Board can protect shippers from the anti-competitive consequences of this end-to-end merger.

²⁶ At the public hearing in this docket, the Applicants claimed that sophisticated organizations, like the Joint Associations, have the capacity to demonstrate foreclosure from past mergers and their failure to submit such evidence in this proceeding means that there has been no foreclosure. But as the Joint Associations testified, the data does not exist for such analysis of mergers that occurred nearly 20 years ago. Moreover, a thorough and efficient analysis would require pre- and post-merger traffic and rate data from the railroads involved in those mergers.

²⁷ Applicants' Reply, Vol I, at 111.

²⁸ Joint Association Comments at 17-18.

²⁹ *Id.* at 18-19.

C. The Requested Conditions Preserve Competitive Interline Routes as a Reasonable Constraint Upon the Applicants' Ability to Exercise Market Power Through Extended Bottlenecks.

The Joint Associations have requested conditions to protect existing interchanges both physically and commercially and thereby preserve the benefits of pre-merger competition that alternative routes via those interchanges currently provide to CP/KCS routes.³⁰ As the Board considers these conditions, the Joint Associations urge it to be mindful that the ultimate objective is to constrain the Applicants' enhanced ability to exploit their extended bottlenecks resulting from the merger.

The Joint Associations' have proposed conditions that are reproduced below with one minor edit to Condition #1, reflected in the italicized text, to eliminate an unintended consequence identified by the Applicants:

1. Gateway/Interchange Protections: Applicants shall preserve all interchanges with Class I and II railroads that were active at any time from January 1, 2018, through the consummation date of the merger *for any bottleneck movement that originates or terminates (including via reciprocal switch or inter-switching) on Applicants or a connecting Class II or III railroad for which the merger of Applicants creates the opportunity for a longer haul on their combined network than either Applicant would have by itself.*³¹
2. Rule 11 Rates: Applicants shall quote Rule 11 rates for all traffic to/from the interchanges referenced in Condition #1 in the shipper's choice of a contract or tariff. Where there are multiple routing options via different interchanges with the same Class I or II railroad, a Shipper may request rates to any or all such interchanges. To implement this commitment, Applicants waive any rights that they may have now or in the future to refuse to quote Rule 11 rates to any of these interchanges.

³⁰ *Id.* at 9-13.

³¹ Applicants accuse the Joint Associations of pursuing "open access" through Condition #1 that would extend beyond the effects of the proposed transaction. Applicants' Reply, Vol. I, at 125-27. This was not the goal of this condition. To clarify this fact, the Joint Associations, in the italicized text, replicate language from Condition #3.a. to similarly limit application of this Condition #1 to the effects of the proposed transaction.

3. Bottleneck Rate Protections:

- a. Application: This condition applies to any bottleneck movement that originates or terminates (including via reciprocal switch or inter-switching) on Applicants or a connecting Class II or III railroad for which the merger of Applicants creates the opportunity for a longer haul on their combined network than either Applicant would have by itself.³²
 - b. Rate Level: A Rule 11 rate provided in accordance with Condition #2 on qualifying movements under Condition #3.a. may not exceed a rate determined by the following method:
 - i. Applicants shall first quote a rate for their long-haul route. Applicants may quote any rate for such service subject only to the rate reasonableness requirements codified at 49 U.S.C. § 10701. If the Board prescribes a maximum reasonable rate for the Applicants' long-haul route, that rate shall be used in this methodology.
 - ii. Calculate the rate per mile of the Applicants' long-haul rate quote (using PC*Miler).
 - iii. Multiply the rate per mile by the distance of the bottleneck segment (calculated using PC*Miler) to calculate a Rule 11 rate for the bottleneck segment. If the Applicants' long-haul rate is predicated upon a minimum volume commitment, Applicants may require the same commitment for the Rule 11 rate.
 - c. Duration: A Rule 11 rate determined pursuant to Condition #3.b. may not be modified by either railroad or shipper for a minimum of one year unless they mutually agree otherwise. Nothing herein shall preclude the parties from entering a multi-year contract that contains a mutually agreeable method to adjust the initial base rates established pursuant to this condition after Year 1.
4. Rate reasonableness. Nothing in these conditions shall preclude a shipper from challenging the reasonableness of a Rule 11 rate determined pursuant to Condition #3.b.
 5. Dispute Resolution: If a dispute arises over calculation of a Rule 11 rate pursuant to Condition #3, the shipper may elect to resolve such dispute pursuant to the Board's arbitration rules at 49 C.F.R. Part 1108. If the shipper makes such election,

³² BNSF inexplicably interprets both this condition and a similar one proposed by UP as applying only to dual-served locations. "Response Comments of BNSF Railway," at 16 (filed July 12, 2022) (BNSF-12) ("An important feature of both proposals is that they are generally limited to locations that are jointly served (directly or through switching or haulage) by CP-KCS and a competing railroad."). That is inaccurate as to the Joint Associations' proposal and there does not appear to be any basis for finding such a restriction in UP's proposal either.

Applicants are deemed to have opted into the Board's arbitration program as a requirement of this condition. Any dispute that is arbitrated shall be subject to the limitations upon arbitrations contained in the Board's rules.

In Condition #3.b, the Joint Associations have proposed a method for calculating a rate for the Applicants' Rule 11 bottleneck segment to interchanges with connecting carriers, which will be an alternative to the Applicants' extended long-haul or single line route resulting from the merger. This method would serve as an objective measure of Applicants' compliance with their commitment to keep a gateway open commercially.

UP and BNSF also have offered their own proposals for this purpose. The UP proposal, which was developed by UP's economic witness, Professor Salop, who calls it the "Commercially Reasonable Rate" formula or "CRR," is nearly identical to the Joint Associations' proposal and UP offers the same justifications.³³ BNSF's proposal is modeled after the so-called "I-5 Prop Rate Agreement" between UP and BNSF that was adopted as a condition in the UP/SP merger for interline traffic over the Portland gateway.³⁴ A common feature underlying all three proposals is the establishment of the bottleneck segment interline Rule 11 rate as a mileage pro-rated portion of the Applicants' actual market rates for their long-haul or single-line movements of the same traffic. Although the Joint Associations would find any of these proposals acceptable, the complexity of administering the I-5 Prop Rate Agreement renders it difficult to apply compared to the UP and Joint Association proposals and thus may be impractical for application to all affected gateways.³⁵

³³ UP Comments at 68-74, Salop V.S. at ¶¶ 107-120.

³⁴ BNSF Comments at 44-48.

³⁵ Whereas the Joint Associations and UP would apply their proposals to all affected gateways, BNSF would apply its proposal only to the Laredo gateway.

Applicants reject these mileage pro-rate proposals for setting the Rule 11 interline rates because “divisions are not set based on any mileage formula; they are set by market forces.”³⁶ But this ignores the fact that these methods are based upon the Applicants’ long-haul or single-line rate(s) which Applicants are free to set at any level they deem appropriate for the market, subject only to the Board’s rate reasonableness jurisdiction. The Applicants lose sight of the fact that the “market” is for origin-to-destination transportation, not origin-to-gateway or gateway-to-destination transportation. By pegging the bottleneck rate to the Applicants’ market-based long-haul rate(s), all three proposals prevent the Applicants from setting a disproportionately higher rate for the bottleneck segment that forecloses existing competition over the non-bottleneck segment.³⁷

In addition, Applicants contend that, by linking their post-merger interline division to their post-merger single-line rates, these proposals would impose a “tax” on their ability to compete against interline service with post-merger single-line service anytime that their pre-merger interline rates happen to be higher than the mileage-based pro-rate for any reason.³⁸ They further contend that this tax will “subsidize” and “insulate” other carriers from Applicants’ single-line competition, and even discourage Applicants from offering rates that reflect their post-merger single-line economics.³⁹

To illustrate their objections, Applicants create a hypothetical that shows how, post-merger, the mileage pro-rate method would cap Applicants’ Rule 11 interline rate below the pre-

³⁶ Applicant’s Reply, Vol. I, at 113.

³⁷ See Joint Association Comments at 11; UP Comments, Salop V.S. at ¶ 120; BNSF Comments, Reishus V.S. at ¶¶ 98-104.

³⁸ Applicants’ Reply, Vol. I, at 119-21, “Expert Reply Statement of W. Robert Majure, PH.D,” at ¶¶ 143-44 (“Majure R.V.S.”).

³⁹ Applicants’ Reply, Vol. I, at 119-20.

merger level whenever Applicants' pre-merger division exceeded Applicants' proportion of total route miles.⁴⁰ Figure 1 below reproduces Applicant's hypothetical in the context of the Canadian cross-border movements that are the focal point of the Joint Associations. Column B depicts the Applicants' pre-merger interline scenario; Column C assumes the Applicants' post-merger single-line rate is the same as the pre-merger interline rate; and Column D assumes the Applicants' post-merger single-line rate is 20% below the pre-merger interline rate.

Figure 1

	A	B	C	D
1		Pre-merger Joint Rate	Post-merger Long Haul Rate (no decrease)	Post-merger Long Haul Rate (20% decrease)
2	Total rate	\$3,000	\$3,000	\$2,400
3	KCS division (Cols. C & D = (Row 2/Row 5) * Row 6	\$1,200	\$1,000	\$800
4	CN division (Row 2 - Row 3)	\$1,800	\$2,000	\$1,600
5	Total miles	3000	3000	3000
6	KCS gateway miles	1000	1000	1000

In Figure 1, Column C, Applicants claim that CN⁴¹ could pocket the \$200 reduction to the KCS division and still match the \$3000 single line rate. Although the illustration in Column C is mathematically accurate, there are three flaws with the Applicants' conclusion. First, CN will not know the Applicants' single line rate;⁴² second, one would expect the Applicants' post-

⁴⁰ *Id.* at 120-21.

⁴¹ The Applicants' hypothetical refers to "UP" as the interline carrier. In the above illustrations, the Joint Associations have substituted "CN" for "UP" to reflect the Canadian cross-border scenario most prevalent for their members.

⁴² Applicants' economic witness, Robert Majure, claims that "shippers would need to reveal the provided CPKC interline quote to prospective interline partners in order to negotiate over the total rate for the interline movement [and that] [w]ith this information, [connecting carriers] would know CPKC's single-line rate as well." Applicants' Reply, Vol. I, Majure R.V.S. at ¶ 141, note 166. That is not true when negotiating Rule 11 rates. Many Joint Association members favor Rule 11 rates over joint rates for interline moves precisely so the connecting carriers are not aware of each other's division. It would be nonsense for shippers to share one

merger single line rate to be less than the pre-merger interline rate due to merger-related efficiencies; and third, because it is illogical to assume the shipper would pay the same rate for interline service as single-line service, CN could not expect to win this business by appropriating the \$200 reduction to Applicants' interline division for itself (assuming CN had knowledge of the reduction). In other words, if the through rate remains constant despite increased efficiency and competitiveness, where are the alleged merger benefits for shippers?

In recognition of the second flaw underlying the hypothetical in Column C, the Applicants pose the hypothetical in Column D, which assumes a post-merger single-line rate that is 20% below the pre-merger through rate. But Column D still exhibits the same first and third flaws as Column C. Moreover, because the single-line rate has been reduced to reflect its greater efficiency, both carrier's interline divisions in Column D must decrease just to match the single-line rate. Indeed, CN will need to take an even greater reduction to its pre-merger division than Column D depicts because the interline rate will need to be less than the single-line rate to win the business. The alleged "tax" and "subsidy" disappear.

In its evaluation of the mileage prorate conditions requested by BNSF, UP, or the Joint Associations, the Board should be mindful that the ultimate objective of those conditions is to preserve a viable interline competitive option that constrains the Applicants' ability to exploit extended bottlenecks resulting from their merger. Alternatively stated, the objective is to encourage the behavior depicted in Column D, rather than Column C, of Figure 1. In Column C, either there are no merger benefits from Applicants' longer haul or the Applicants are exploiting their extended bottlenecks to avoid sharing those benefits with the shipper through lower rates.

carrier's rates with the other when doing so would undermine the objective of the proposed merger condition.

In Column D, when Applicants share the merger benefits through lower rates, they will always win the shipper's traffic with their more efficient single-line service, unless CN is able and willing to reduce its division far enough below its pre-merger level to attract the traffic from Applicants' single line service. In other words, shippers will seldom, if ever, use the interline rate. This fact exposes the Applicants' "tax" and "subsidy" concerns as red herrings. The mileage pro-rate condition is just a means to preserve the interline option as a competitive constraint upon Applicants' single-line pricing. When viewed through this lens, the mileage prorated condition fulfills its objective well, without the consequences that Applicants predict.

D. Proposed Alternatives to the Mileage Prorate Proposals Are Inadequate.

At the public hearing, Chairman Oberman asked if the Joint Associations have considered alternatives to a mileage pro-rate proposal. He specifically referenced the interchange protections contained in an agreement between the NITL and the applicants in *KCS/Tex-Mex*. The Joint Associations have considered both the *Tex-Mex* agreement and an option that would establish post-merger interline divisions to gateways based upon the Applicants' current interline divisions over the same routes and concluded that their mileage prorated proposal is superior to both alternatives.

The *Tex-Mex* agreement required the applicants to "establish and maintain commercially reasonable contract or common carrier rates and charges over any existing interchange with that railroad" and required that any disputes regarding such rates be resolved by arbitration. NITL Agreement, § 2. The agreement does not define "commercially reasonable" or propose any standards for assessing commercial reasonableness. The Joint Associations thus are not satisfied with a similar condition in this proceeding because the commercial closure of a gateway is very

difficult to ascertain.⁴³ This concern extends to the Applicants' commitment, which they made at the public hearing, to arbitrate gateway closures, because there is no standard or remedy associated with that commitment.

The Joint Associations did consider an alternative that would moot the Applicants' complaint that divisions typically are not mileage based, but that alternative could not be implemented without litigation. Instead of determining the Applicants' post-merger interline division based on a mileage prorate of their single-line rate, the division could be determined by applying the proportion of the bottleneck carrier's pre-merger division to the pre-merger total through rate with the alternative carrier to CP. For example, if the KCS pre-merger bottleneck rate to the interchange with CN was \$1000 and the total KCS-CN through rate was \$4000, the Applicants' post-merger division for that route would be 25% of the Applicants' post-merger single-line rate. If there was no pre-merger through rate or no evidence of such rate, the fall-back would be the Joint Associations' mileage prorate proposal.

This alternative requires litigation because, depending upon the form of the pre-merger through rate, the information needed to apply this standard will be within the exclusive knowledge of either the shipper or the carrier, but not both. For example, if the pre-merger interline rate was a joint rate, the Applicants will know the divisions but the shipper most likely will not. Conversely, if the pre-merger interline rate was a combination of Rule 11 factors established by confidential contracts, only the shipper will know the divisions. Consequently, discovery with appropriate protective orders will be required to share this information even in situations where the shipper and Applicants otherwise are willing to do so. An additional

⁴³ See, UP Comments at 69-71.

concern is that this method of determining the Applicants' post-merger bottleneck division would enable Applicants to mathematically back into their competitor's pre-merger division, resulting in disclosure of that information even when otherwise protected by the Board's standard protective order.

The foregoing issues stand in contrast to the simplicity of the mileage prorate approach which seldom, if ever, will require a formal proceeding or arbitration. When the Board considers the mileage prorate approach in the context described in the final paragraph of Part I.C. above, that approach constitutes the best and most well-defined option to preserve the interline rate as a reasonable, market-based competitive constraint upon the Applicants' post-merger single-line rate without litigation.

II. **SERVICE PROTECTIONS.**

The Joint Associations harbor significant concerns over the potential for merger-related service disruptions. Those concerns are shared by the U.S. Department of Agriculture, which has asked the Board to require the Applicants to file a Service Assurance Plan, or "SAP."

USDA has specific concerns about both potential transitional service impacts and permanent impacts from increased volumes. Having a SAP would help alleviate these concerns by requiring the applicants to address any transitional service issues that might arise. Within the SAP, the applicants would have to proactively allocate locomotives, labor, and equipment to potential pain points. Applicants would also be required to identify potentially congested infrastructure over the longer term and to invest at those points to relieve the congestion. Multiple railroads have raised congestion concerns, and the SAP requirement could pose an effective alternative solution to their concerns Finally, also, a SAP would provide benchmarking measures to assess service after the merger.⁴⁴

This merger entails extensive trackage rights pursuant to which KCS operates along the Gulf Coast and that require careful coordination with the track owner, UP, and a co-tenant, BNSF. Both railroads have raised concerns in this proceeding that Applicants are projecting

⁴⁴ Letter from U.S. Dept. of Agriculture (filed Feb. 28, 2022).

additional traffic over those lines without additional infrastructure, which the Applicants have denied. Whether or not service disruptions occur due to the transitional or permanent impacts of this merger is outside of shipper control, but it is shippers who will suffer the most extensive harm. The Board's prior decision not to require the Applicants to prepare an SAP enhances the need for alternative measures to protect shippers from merger-related service disruptions.

The Joint Associations have requested the following conditions to mitigate the impacts of any merger-related service disruptions upon shippers:⁴⁵

1. Upon the request of any Shipper, CP shall make a good faith offer to enter into an agreement with that Shipper with respect to that Shipper's traffic affected by this transaction that, at a minimum:
 - a) identifies that Shipper's base service level as the average transit time during each base period (i.e., the 12 calendar months preceding the month in which the transaction is consummated, or such other time period agreed to by CP and the Shipper) for each of the commodities shipped or received by that Shipper between each pertinent origin/destination pair affected by the transaction;
 - b) assures that average transit time at the base service level will not be adversely affected by the transaction;
 - c) provides that, if the Shipper notifies CP that the Shipper's average transit time for any post-transaction calendar month has been adversely affected relative to that Shipper's average transit time for the corresponding base period calendar month, CP will have not more than 30 days to bring the average transit time for the

⁴⁵ Joint Association Comments at 21-24.

movement(s) in question up to the base service level for the corresponding base calendar month;

- d) notwithstanding any contrary provision in a contract between CP and the Shipper, the Shipper may divert traffic from CP routes without being in violation of any contract volume commitments during the foregoing 30-day period and continuing until the average transit time has been restored to the corresponding base period calendar month;
- e) provides remedies if the Shipper's average monthly transit time continues to be adversely affected by the transaction for more than 30 days after the date of notification to CP that shall include the following, at a minimum:
 - on-the-ground management flexibility and top-level backing with whatever resources are necessary to affect a complete and timely resolution;
 - unless otherwise agreed to by CP and the Shipper, a sliding scale of charges based on CP's post-transaction performance for that Shipper relative to that Shipper's base service levels; and
 - if a Shipper's average transit time calculated over a calendar month for a particular movement exceeds that for the corresponding base period calendar month, CP shall have the burden of showing that the adverse effect was not a result of the transaction; and
- f) provides that, unless otherwise agreed to by CP and the Shipper, any agreement made pursuant to the service protection provisions of this condition will expire 5 years after the consummation of the transaction.

2. CP shall process all claims for service-related damages in accordance with 49 C.F.R. Part 1005.
3. CP shall provide Shippers with at least 30 days prior written notice of any planned service changes at Shipper facilities. If CP fails to provide such advance notice, CP shall be liable for all damages sustained by the Shipper that are caused by or arise from the service change during the first 30 days after the service change.
4. If CP denies a claim for damages resulting from any of the foregoing conditions or any service disruption caused by or arising from this transaction, it agrees to arbitrate such claims, upon a Shipper's demand, under the Commercial Arbitration Rules administered by the American Arbitration Association and such arbitration shall be decided no more than 90 days from the date of selection of the arbitrator. This arbitration condition shall not supersede any arbitration provision in a contract unless the shipper expressly demands arbitration pursuant to this condition.

The foregoing conditions are modeled on an agreement between the NITL and CN in *Canadian National Ry. Co. et al. – Control – Wisconsin Central Transp. Corp. et al.*, Decision No. 10, 5 STB 890, 922 (served Sept. 7, 2001) (“CN/WC”), with a few modifications and additions.

The Applicants have not stated whether they would accept the terms of the CN/WC agreement, but they do expressly object to two components in the foregoing conditions, both of which either modify or add to the CN/WC agreement. First, the Applicants object to Condition #3 on grounds that it “would inject operational rigidity and thereby undermine CPKC’s ability to compete effectively” and would be “unprecedented and misguided.”⁴⁶ This concern is misplaced. Condition #3 does nothing more than require the courtesy of providing 30 days’

⁴⁶ Applicants’ Reply, Vol I, at 143.

notice of “any planned service changes *at* Shipper facilities.” [italics added] Per the italicized text, this condition would apply only to service provided at a Shipper facility, such as the timing and frequency of local switching services. It would not apply, as the Applicants seem to believe, beyond this type of first-mile/last-mile service.⁴⁷ A 30 day notice requirement for such operational changes that can have dramatic effects upon a shipper’s operation of its business is eminently reasonable, and Applicants have not explained why or how they would be harmed if they could not implement such changes within less than 30 days. Furthermore, the Applicants’ response to this concern at the public hearing was tone-deaf. They protested that the complexity of rail operations may require changes with less notice but showed no appreciation or concern for the complexity of the shipper operations that abrupt rail service changes would disrupt.

Second, the Applicants object to the second bullet under Condition #1(e).⁴⁸ That condition is directly from the *CN/WC* agreement with one modification. The *CN/WC* agreement states that “CN/WC and the Shipper *may* agree upon a sliding scale of charges based on CN/WC’s post-transaction performance for that Shipper relative to that Shipper’s base service levels....”⁴⁹ In the *CN/WC* agreement, this term was permissive, whereas the Joint Associations would make it mandatory in this transaction. A condition that is purely permissive is meaningless. The Joint Associations seek to make this a substantive condition that can be enforced. It is appropriate to strengthen this condition in this proceeding because this is a “major” transaction, whereas the *CN/WC* transaction was subjected to a lower standard that applies to “significant” transactions.⁵⁰

⁴⁷ *Id.* at 144.

⁴⁸ *Id.* at 144-45.

⁴⁹ *CN/WC* at 922 [italics added].

⁵⁰ *See* 49 C.F.R. § 1180.2.

Ultimately, the only service assurances that Applicants have provided are the five pillars in “Our CP/KCS Service Promise.”⁵¹ Those are fine aspirational promises, but they require substantive provisions for enforcement and remedies. Prior post-merger service failures have occurred despite the promises and good intentions of the applicants. But it was innocent shippers and their customers who suffered the most significant consequences. The Joint Associations have requested modest conditions designed to mitigate just *some* of the consequences to shippers if the Applicants experience service disruptions during the integration of their operations.

III. TIH LIABILITY CONDITIONS.

The Joint Associations, The Chlorine Institute, the U.S. Department of Agriculture, and several individual shippers have requested a condition to prevent the Applicants from extending CP’s TIH liability, indemnity, and insurance tariff requirements to post-merger TIH movements over the pre-merger KCS network. The specific condition requested by the Joint Associations is:

- CP may not extend its TIH liability, indemnification, or insurance requirements to TIH shipments that originate on, terminate on, or traverse any segment of the pre-merger KCS network. Such transportation shall continue to be governed by the pre-merger KCS tariff indemnity terms for all hazardous materials shipments.⁵²

Applicants object to this condition on three grounds.⁵³ First, they contend that “the conditions would not truly address any impact of the Transaction” because “[n]othing would

⁵¹ Applicants’ Reply, Vol. I, at 140.

⁵² Joint Association Comments at 25.

⁵³ In addition, CP’s Executive Vice President and Chief Market Officer, John Brooks, testifies, without offering any proof, that “[t]he tariffs of several other U.S. Class 1s establish \$100 million insurance requirements and similar liability allocation principles.” Applicants’ Reply, Vol. II, Reply Verified Statement of John Brooks, at ¶ 67. That claim belies the experience of the Joint Association members with other Class I railroads, which require insurance in amounts that range from \$0 to \$25 million. The Board, of course, can readily verify the amounts in all Class I tariffs.

prevent KCS from choosing to adopt terms that mirror those in CP's public tariffs."⁵⁴ But that is beside the point. KCS has not expressed any such desire or intent; it is solely because of this transaction that the CP tariff *will* be extended to cover the KCS network.

Second, if the Board accepts that this condition would address an impact of the transaction, the Applicants contend that the condition "would in substance freeze KCS's tariff terms permanently in their pre-Transaction state," which would "prevent CPKC from adapting to changes in conditions bearing on the risk profile of TIH/PIH shipments on the CPKC network."⁵⁵ This concern can be easily addressed by allowing Applicants to petition the Board for permission to modify the KCS tariff terms upon demonstrating a material change to the risk profile of TIH shipments on the combined network from conditions existing immediately preceding the merger application. The burden of proof would be on CPKC to make that showing.

Third, the Applicants complain that TIH shippers already have the right to challenge the reasonableness of the CP tariff terms, which is a right that will continue to exist post-merger, and that the requested condition would supplant that process "with a per se rule of invalidity applicable uniquely to CPKC and no other railroad."⁵⁶ Again, that is beside the point. But for this merger, there would be no need to challenge the CP tariff's applicability to TIH movements over the pre-merger KCS network. That is an unreasonable burden that Applicants would impose upon TIH shippers as a cost of the Applicants' transaction. Since CP is expressly on the record as saying that it would not transport TIH materials but for its common carrier obligation, there is no reason to believe that TIH shippers will realize most of the merger benefits that

⁵⁴ Applicants' Reply, Vol. I, at 309.

⁵⁵ *Id.* at 311.

⁵⁶ *Id.* at 311.

Applicants have promised.⁵⁷ Instead, they are facing the prospect of more costs or abandoning markets currently served by KCS.⁵⁸

It is an indisputable fact that the CP TIH tariff does not apply to TIH movements over pre-merger KCS lines and would not apply to such movements in the future but for the proposed transaction. This will have anti-competitive consequences for the transportation of TIH materials. The Board can prevent those consequences by adopting a condition that prevents CP from extending Items 51 through 56 of Tariff 8 to movements over the pre-merger KCS network. To address CP's concern that this would freeze the KCS tariff in perpetuity, the Board can permit CP to petition the Board to change the tariff upon CP showing a material change in its risk profile for TIH movements.

IV. **CONCLUSION**

For the foregoing reasons, the Joint Associations respectfully request that the Board grant the conditions requested in Parts II.B, III, and IV by making its approval of the Applicants' transaction subject to those conditions.

⁵⁷ See, e.g. FD 35504, Canadian Pacific Ry. Co. Comments in Support of Petition, at 3 (filed Jan. 25, 2012) ("CP would not participate in the movement of TIH if given the choice").

⁵⁸ See, "Comments of Bayer Cropscience LP, at 2 (filed Feb. 28, 2022); "Comments of Occidental Chemical Corp. and Oxy Vinyls, LP," at 2 (filed Feb. 28, 2022); "Response to Comments, Protests, Requests for Conditions, and Other Opposition of Olin Corporation," at 7-10 (filed July 12, 2022).

Respectfully submitted,

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Dated: October 21, 2022

Certificate of Service

I certify that I have this day served copies of this document upon all parties of record in this proceeding and the parties listed below, by first-class mail, postage pre-paid, or email:

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