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SURFACE TRANSPORTATION BOARD
Hearing on the Proposed CP/KCS Merger
Docket No. FD 36500
REMOTE PUBLIC HEARING

Friday, September 30, 2022

9:00 a.m.

Surface Transportation Board
395 E Street, S.W.
Washington, DC

The above-entitled matter came on,
pursuant to notice, at 9:00 a.m., Chairman Martin
Oberman presiding.

1 P R O C E E D I N G S

2 CHAIRMAN OBERMAN: We are always optimistic and
3 ambitious about how much time things will take and
4 they always take longer, so before we wade into the
5 completion of the BNSF presentation, you may have
6 seen -- I don't know about the folks on YouTube, I
7 was having some discussions with the Canadian Pacific
8 Team, but solely about logistics and availability of
9 their witnesses and counsel for purposes of
10 rescheduling, as well as everybody on this side of
11 the table who has to also be available.

12 So, here is the current plan. I don't
13 think it will change or change very much. So, we are
14 going to complete Burlington Northern's presentation
15 first. We then have one, a very brief witness, and
16 then we are going to move to the panel of CSX and
17 Union Pacific.

18 After that, we are going to have Panel 18
19 and Panel 19, and there were a number of other
20 witnesses who were scheduled for yesterday or today
21 and I don't have that list in front of me, but I will
22 have momentarily, who were cooperative enough and able

1 enough to move their presentations to Monday and
2 Tuesday, virtually.

3 If any of them are available and would
4 like to be heard today, I think we will have some
5 time to have more of those witnesses this afternoon
6 before we finish. Whoever has not been able to
7 finish testifying today, we will convene virtually,
8 and we will give you these times with more precision,
9 around midday on Monday, and if needed, on Tuesday
10 morning and we will not work later than midafternoon
11 Tuesday because it is Yom Kippur and a lot of people,
12 including me, are not going to be available after
13 midafternoon.

14 It is now the plan to convene on Thursday
15 with about a 99 percent chance virtually, rather than here in
16 person, and we will devote as much time as is needed
17 on Thursday to CP's rebuttal. If we had tried to do
18 this any other way, we had the risk of really
19 compressing other presentations, including the other
20 railroads who undoubtedly will generate some more
21 questioning, and also trying to squeeze in CP's
22 rebuttal, and that are the proponents and really are

1 entitled to an adequate time, whatever adequate time
2 they need to respond to just a lot of stuff that's
3 been heard here.

4 So, I think the only fair way and
5 thorough way and for the Board to get all the
6 information we need to reach a reasonable and a
7 correct decision on this matter is to do it this way.
8 So, we would've hoped to have finished the whole
9 thing three days virtually. Obviously, that didn't
10 work. I think maybe after the Gulf Coast case and
11 this case we're learning about scheduling.

12 So, that's the plan. It's possible, but
13 I think unlikely that we would convene in person next
14 Thursday. I just don't think the logistics are going
15 to work. I think we're going to have to do it
16 virtually, but we did the entire Pan Am CSX case
17 virtually and that went well and so I think we can do
18 this hybrid. So, that's the plan.

19 With that, let's begin. Peter, your
20 case.

21 MR. DENTON: Thank you, Mr. Chairman.
22 I'm not going to reintroduce everybody. I think for

1 the last couple of hours yesterday we started to
2 introduce the topics that we've covered in our
3 briefing. We are now onto Paul Hirsch, who is the
4 Assistant Vice President of the Mexico Business Unit
5 and then after Mr. Hirsh, Dr. Reishus will have a
6 presentation.

7 We have a slide deck, if we could hook
8 that up please, and it actually starts at Slide 28,
9 if you're able to advance it that far. Okay.

10 MR. HIRSCH: Good morning Mr. Chairman,
11 members of the Board. My name is Paul Hirsch. I'm
12 the Assistant Vice President of the Mexico Business
13 Unit for BNSF. In that capacity, I lead a team of
14 U.S. and Mexico-based professionals that focus on
15 rail and intermodal transportation, the five
16 international gateways accessed by BNSF, and its
17 federal partners in Mexico.

18 I will address the importance of access
19 to Mexico through Laredo. There are two main reasons
20 for BNSF and its shippers, foreclosure to Mexico at
21 Laredo and worsening congestion at Houston, as
22 merger-related Mexico traffic is diverted through the

1 Houston Complex. And you heard yesterday from my
2 colleague, Mr. Gabriel, that explained to you the
3 risks at Houston.

4 KCS failed to keep the Laredo gateway
5 open on commercially reasonable rates. Since KCS
6 acquired the Tex-Mex, BNSF cannot effectively compete
7 for traffic over Laredo and is foreclosed from
8 accessing major markets in Houston and Central
9 Mexico.

10 BNSF is concerned that the merger with --
11 will worsen this problem and is here to request that
12 the Board put complete measures in place to ensure
13 that carriers can compete fairly for businesses over
14 Laredo.

15 This merger is all about Mexico. As of
16 2019, Mexico is the largest trading partner of the
17 U.S. with over 614 billion in total trade.
18 Mexico has grown and will continue to grow and is
19 therefore an important market to BNSF and its
20 shippers.

21 BNSF wants to be able to compete for that
22 business. This slide shows a tremendous growth in

1 the U.S. freight trade with Mexico since the Board
2 last evaluated the Laredo Gateway in the KSC/Tex-Mex
3 proceeding in 2003 and you can see there on the chart
4 that growth is 165 percent.

5 Laredo is a key rail gateway for
6 accessing major markets and population centers in
7 Mexico. This Board has previously recognized the
8 importance of Laredo. In the UP/SP merger in 1996,
9 the Board recognized that, and I quote, "Laredo is a
10 principal rail gateway between the United States and
11 Mexico." And it is a gateway of, and I quote,
12 "Separate and surpassing economic significance."

13 The statistics and maps demonstrate the
14 importance of Laredo. Between 2003 and 2019, the
15 value of freight carried by rail over Laredo grew 85
16 percent and the tonnage increased by 46 percent.
17 Compared to other gateways, the value of the freight
18 traffic traveling over Laredo was more than doubled,
19 actually, 106 percent, than the value of traffic over
20 Eagle Pass and it's more than the value of rail
21 freight traveling over Eagle Pass, El Paso, Nogales,
22 and Brownsville combined.

1 So, the Board may ask why is Laredo
2 favored over gateways like Eagle Pass. It's
3 important to differentiate between gateways and
4 markets. The Board heard yesterday -- actually, on
5 Wednesday, from Applicants that there was no
6 foreclosure at Laredo because BNSF chose to shift its
7 business to Eagle Pass. This is not true.

8 BNSF was foreclosed from businesses at
9 Laredo and lost that business and never recovered it.
10 BNSF built new business with new customers and
11 destinations from Eagle Pass. Laredo and Eagle Pass
12 serve different markets and are not substitutes for
13 each other. There are markets and destinations from
14 Mexico that cannot realistically be served from Eagle
15 Pass due to the additional time and distance
16 involved.

17 From the heart of U.S., Laredo and KCSM
18 combine for the best route to the Golden Triangle of
19 Mexico from Laredo to Mexico City and Guadalajara
20 where 80 percent of the population lives.

21 The industrial destinations of Monterey,
22 San Luis Potosi and Mexico City are best served

1 through Laredo. The large market of agricultural
2 products, including grain, around Mexico City and
3 eastern Mexico, are best served through Laredo. The
4 slide shows the Golden Triangle.

5 We need the Golden Triangle. Automotive
6 assembly plants are clustered along KCSM routes that
7 are accessed through Laredo. The distance to these
8 plants from Eagle Pass is generally longer and often
9 involves interchanging from FXE to KCSM.

10 Grain traffic provides another good
11 example of the importance of Laredo. As the slide
12 shows, Laredo has the most direct access to the high
13 grain demand centers of Mexico City and eastern
14 Mexico over KCSM. Applicants' own data show that the
15 key to the merger is increasing CP/KCS traffic over
16 Laredo.

17 Applicants expect two-thirds, two-thirds
18 of traffic growth for CP/KCS following the merger
19 will travel over Laredo and only one-third from
20 anywhere else in North America. Applicants predict
21 that 926 additional carloads and containers will
22 travel on CP/KCS over Laredo daily due to diversion

1 from competitors or growth. The Board must ensure
2 that growth is achieved through fair competition and
3 not by freezing out competitors.

4 I've talked about the importance of
5 Mexico and how things might change. You heard on
6 Wednesday from KCS that there has been no foreclosure
7 at Laredo. Now, I will talk about our experience
8 with KCS.

9 For years, KCS has made it difficult for
10 BSNF to compete for traffic over Laredo. Following
11 the KSC/Tex-Mex merger, KCS doubled the rates and
12 there was a decline in BNSF traffic over Laredo from
13 which BNSF has never recovered. Dr. Reishus will
14 cover this issue.

15 KCS has been obligated to interchange at
16 Robstown since the Tex-Mex merger. To this day, BNSF
17 still cannot win carload business over Laredo when
18 KCS serves the U.S. location. When KCS quotes a
19 shipper for interline move with BNSF over
20 Robstown, the shipper chooses the single line KCS
21 option.

22 BNSF doesn't see the KCS rates that are

1 quoted to shippers, but we know that we're not
2 getting the business. This is because KCS is not
3 providing commercially reasonable rates to
4 interchange at Robstown and is quoting rates that
5 force traffic to KCS long haul routes.

6 Two exceptions have been BNSF raising
7 traffic increases over Laredo due to contracts for
8 finished autos and a contract for intermodal traffic
9 with KCS and you can see that volume on the blue
10 line on the chart. BNSF has been able to gain this
11 traffic to certain locations in the U.S. because KSC
12 doesn't offer such service independently today, but
13 CP/KCS will offer it post-merger.

14 If this business is lost, BNSF traffic at
15 Laredo will again drop drastically and BNSF will
16 revert to having little to no role as a competitor at
17 Laredo. If the Board does not impose conditions to
18 ensure competition at Laredo, the merged CP/KCS will
19 have much greater power and incentive to foreclose
20 BNSF customers from accessing Mexican markets through
21 Laredo because it's network will be larger in the
22 U.S. and it will include Canada.

1 Let me now turn to the affect of gateway
2 closure on truckers. Applicants assume 87,000 rail
3 traffic diversions of intermodal traffic going
4 through from Mexico each year from BNSF and UP routes
5 that travel outside Houston. If CP/KCS cannot
6 develop a competitive service over its longer route
7 for these time-sensitive freight and continues to
8 foreclose BNSF at Laredo, the result will be more
9 than 235 trucks returned to the road every day in
10 Texas and beyond with associated traffic accidents,
11 emissions, and noise. Also, the additional truck
12 traffic could create congestion by the border
13 checkpoints.

14 KCS's pledge to preserve an open gateway
15 at Laredo and to charge commercially reasonable
16 rates has not worked. The merger with CP will expand
17 the KCS network and make it more powerful at Laredo.
18 If the Board wants BNSF to be an effective
19 competitor at Laredo, it needs to impose conditions
20 that are transparent and certain to allow BNSF and
21 others to compete.

22 As Mr. Nober explained yesterday, BNSF

1 has proposed a proportional rate mechanism for
2 traffic over Laredo similar to the I-5 proportional
3 rate agreement that BNSF and UP have used for
4 decades following the UP/SP merger. It's a simple
5 and effective mechanism that has not required overly
6 regulatory oversight.

7 Dr. Reishus will now explain in more
8 detail how the BNSF prop rate mechanism will work.

9 CHAIRMAN OBERMAN: I think we may have a
10 few questions. Patrick?

11 BOARD MEMBER FUCHS: Thank you, Mr.
12 Hirsch. I'm wondering if you could describe how the
13 Mexican regulatory regime may play a role in the
14 foreclosure issue, what you see as the restrictions
15 that are imposed by that regime and what, if any,
16 gaps exist?

17 MR. HIRSCH: I'm not sure if I understand
18 your question. You're asking me what the Mexican
19 regime is, as far as rates?

20 BOARD MEMBER FUCHS: Yes.

21 MR. HIRSCH: What we know is that the
22 concession requires the Mexico concessionaires to

1 give the same rates to all users -- the same rate to
2 all carriers that interchange with them for the same
3 location. So, what we're saying here is that that
4 rate may be the same as everybody, but CP/KCS will
5 have the ability to modify that rate, even the same
6 rate to everybody, but they can move that so that it
7 will make the other interline carriers
8 noncompetitive.

9 BOARD MEMBER FUCHS: Is the implication
10 that CP/KC would be able to increase the rate on
11 other types of traffic? In other words, why wouldn't
12 the market, why wouldn't competition in other
13 lanes constrain their ability to raise rates on the
14 interline moves that you are alleging would be
15 foreclosed?

16 MR. HIRSCH: As I said, the importance of
17 the Mexico market -- there are certain industries and
18 certain markets that are best served by KCSM, so the fact
19 that you can access other gateways in Mexico that doesn't
20 mean that you can go and compete for that market,
21 right? We interchange at different gateways, but
22 that's with a different rate. Actually, we have two

1 interchanges with KCS, one is Matamoros and the
2 other one is in Laredo, but the only one that can
3 compete for the markets in Mexico or the important
4 markets in Mexico is Laredo, so if you cannot get
5 access to Laredo, it's very difficult to compete to
6 those markets.

7 So, if you have a facility that is on
8 KCSM today and you can access another railroad
9 through Eagle Pass, that doesn't mean that you can
10 serve that facility, right? So, it's very difficult
11 for a different railroad to access -- actually,
12 impossible to access some of those locations if you
13 are a grain shipper shipping into a facility that is
14 on KCSM and there's a shell station to receive
15 unit trains. You can have another competing railroad
16 that's close by, but you're not going to have access
17 to that. You're not going to be able to serve that
18 customer, so that customer is only going to be served
19 by KCSM.

20 MR. DENTON: To put it another way,
21 Commissioner Fuchs, it seems like you were getting to
22 the question of nondiscrimination versus how this all

1 interplays.

2 BOARD MEMBER FUCHS: Exactly.

3 MR. DENTON: So, our understanding, and
4 Applicants have told you, is that the Mexican
5 regulatory regime requires KCSM to not discriminate
6 on a rate basis for any traffic that it receives
7 from interline partners, all right. And what we have
8 explained to you and Roger explained to you
9 yesterday, what Dr. Reishus will explain further
10 today, is that all a customer sees if they have a
11 through route on CP/KCS or KCS today, is the end
12 rate. So, in the example we had up yesterday it was
13 \$1,000, right? And to the extent that KCSM can
14 increase the Mexican portion of that through rate
15 from, say, initially, it was \$400. If they're able
16 to increase that to \$700 and decrease their U.S.
17 portion because to them it doesn't matter which side
18 of the border the KCS vs. KCSM takes. Then they are able
19 to take that increase of the Mexican rate and apply
20 that to any interline traffic that they receive.

21 A competing carrier like BNSF or UP
22 wouldn't have that same ability to hide --

1 MR. NOBER: You're asking if they can bring a rate
2 case in Mexico to challenge that?

3 BOARD MEMBER FUCHS: Yes. I'm trying to
4 disentangle -- so, Peter, it sounded like what you
5 were saying is that it's a visibility problem as
6 opposed to a regulatory gap problem. It's a
7 practical problem, not a theoretical problem; is that
8 basically --

9 MR. DENTON: Both.

10 BOARD MEMBER FUCHS: Okay.

11 MR. DENTON: Yes. So, our expert, Dr.
12 Dychter, in his opening verified statement, talked at
13 length about the Mexican regulatory regime and he has
14 real concerns that shippers in Mexico will not have
15 the ability to challenge a rate or really the ability
16 to receive effective relief on Mexican rates.

17 BOARD MEMBER FUCHS: If there were
18 perfect visibility shippers had in terms of what the
19 rate revenue divisions were of a rate, would you
20 think that the nondiscrimination principle in the
21 Mexican regulatory regime would at least serve as
22 some countervailing force for CP/KC's ability to embark

1 on vertical foreclosure?

2 MR. DENTON: I really do not. I think
3 what Mr. Nober and what Dr. Reishus will walk through
4 today is that that ability to go up is pretty
5 significant on the Mexico side. And if they're able
6 to push their rate on the Mexico side, for example,
7 from 400 to 700 and then hide that on the U.S. side,
8 then they're able to foreclose and that's really the
9 essential issue here.

10 MR. NOBER: So, there was a back and
11 forth, I think it was on Wednesday, about the
12 difference between the commercially reasonable rate
13 and the maximum lawful rate -- regulatory rate and that's another
14 place that impacts the market here. And again, Paul
15 will have to speak to what the rate regulatory regime
16 in Mexico is. I'm not aware of anybody ever bring a
17 rate case in Mexico.

18 MR. HIRSCH: There's a maximum rate that
19 the regulated are allowed to charge, but normally
20 the rates that are used in any business are well
21 below that one, so they have a lot of room to
22 increase the rates.

1 So, you would be in a place where it's
2 not commercially competitive, yet still below the
3 maximum reasonable rate, which I know was an issue
4 that Chairman Oberman raised. I think it was
5 Wednesday.

6 CHAIRMAN OBERMAN: Go ahead, Karen.

7 BOARD MEMBER HEDLUND: Sir, could you go
8 back to the slide that shows the Eagle Pass and El
9 Paso Gateways and the lines into Mexico because it's not
10 -- you showed it, but it's not in our book.

11 CHAIRMAN OBERMAN: No, it is. It's on
12 page 30.

13 BOARD MEMBER HEDLUND: Oh, you're right.
14 Thank you. So, the green lines represent what
15 railroads, are they BNSF railroads, are they Mexican
16 railroads?

17 MR. HIRSCH: On blue, you have KCS, KCSM
18 and on green that's Ferromex, also known as FXE and
19 that's the other railroad that we interchange with in
20 Mexico.

21 BOARD MEMBER HEDLUND: Right. And how
22 much has your business increased in Mexico, what is

1 your total volume in Mexico, what are you shipping
2 through El Paso, Nogales, and Eagle Pass?

3 MR. HIRSCH: So, if you want to know in
4 total number of units?

5 BOARD MEMBER HEDLUND: Yeah -- and
6 revenue.

7 MR. HIRSCH: It's about 350,000 shipments
8 a year.

9 BOARD MEMBER HEDLUND: Oh. And have you
10 transferred business from Laredo to these other
11 gateways?

12 MR. HIRSCH: No, ma'am. What we have
13 done -- BNSF has a bias for growth, so we try to
14 grow our business and we have several gateways into
15 Mexico. We're going to try to grow in all of that.
16 What happened when we were foreclosed in Laredo, we
17 lost that business. We never recovered that, so
18 you're not going to see that the same customer we
19 were serving over Laredo is the same customer that
20 we're serving over Eagle Pass. That's not the case.

21 We developed new markets. We developed
22 new business. You're going to see that that volume

1 that we grew over Eagle Pass was not as rich. It
2 took us several years to grow that business.

3 BOARD MEMBER HEDLUND: But the point is
4 that you do a significant amount of business in
5 Mexico notwithstanding the fact that you feel you've
6 been foreclosed from Laredo.

7 MR. HIRSCH: Yes. But let me tell you
8 something, if you look at the growth of BNSF since we
9 were able to compete on the Laredo Gateway with the
10 older contracts and intermodal service that we put
11 together with KCS in the last six years, we've grown
12 the volume going over Laredo to a point that today
13 that volume is double what we do in Eagle Pass.

14 So, when we have the ability to go -- and
15 that's where we're showing the importance of Laredo.
16 Laredo is the gateway to Mexico. There's a lot of
17 markets in Mexico.

18 BOARD MEMBER HEDLUND: So, you're saying
19 you're currently going through Laredo.

20 MR. HIRSH: Yes. We have two services.
21 As I mentioned, we have a contract with an automotive
22 service and an intermodal business that we put

1 together with KCS that we are growing and we have
2 done it, [inaudible] -- because of an agreement with KCS. Yes.

3 BOARD MEMBER HEDLUND: And so, are you
4 concerned you're going to lose that because they're
5 going to change the terms?

6 MR. HIRSH: Yes. As I said before, today
7 we are doing that and KCS has incentive to work with
8 us in that service because they cannot reach those
9 destinations on their own today, so it's beneficial
10 for them to work with us.

11 With the CP merger, they will have direct
12 access to those destinations, like Chicago, and then
13 they will have the incentive to make sure that all
14 that freight moves on CP/KCS and not with BNSF. Like
15 today when we move this freight come say from Mexico
16 City to Chicago service, it comes out of Mexico City,
17 we go through Laredo. That's on KCSM. Then KCS
18 [inaudible] them and there we interchange. We bypass
19 Houston and we go through Chicago with a very
20 competitive intermodal service.

21 Today KCS cannot reach Chicago, but in
22 the future they will. So, they will have the

1 incentive to make sure that after Robstown, instead
2 of going on BNSF that freight continues on CP/KCS.

3 BOARD MEMBER HEDLUND: And your concern
4 is that they will manipulate the rates --

5 MR. HIRSCH: To do that.

6 BOARD MEMBER HEDLUND: -- in Mexico to do
7 that.

8 MR. HIRSCH: From Robstown to Mexico we
9 interchange in Robstown, so they can manipulate the rate on the
10 Mexican side or the U.S. side in our case so that it
11 will make it noncompetitive for BNSF.

12 MR. DENTON: And one concern, just to add
13 to that, that we have from a market and service
14 standpoint is we have the superior route north/south
15 going to Chicago versus what CP can offer. Our
16 concern is that through the rate manipulation they'll
17 pull it over to CP and not hang onto the traffic and
18 those 80,000 trucks that we have today will make way
19 back to the truck as that will be the best
20 alternative, so commercially infeasible to stay on
21 BNSF railway to Chicago, will float to CP, the
22 service through Houston, per the conversations we had

1 yesterday, won't sustain the service needs of the
2 market and it will flip back the trucks going up the
3 I-35 corridor, so 80,000 plus trucks get dumped back
4 on the highway.

5 DR. REISHUS: And I think it's important to
6 recognize that this is incremental business. The
7 intermodal business is put on. This is new business
8 to both KCSM and BNSF that was never there. It took
9 10 years to be able to get an agreement in place to
10 be able to move this additional traffic. So, this is
11 a case where KCSM has the incentive currently to move
12 this traffic because otherwise it would have none of
13 it and it was otherwise just going by truck.

14 BOARD MEMBER HEDLUND: Do you have the
15 ability to seek any recourse to the Mexican
16 authorities?

17 MR. HIRSCH: Not that I know of.

18 CHAIRMAN OBERMAN: Robert?

19 BOARD MEMBER PRIMUS: Thank you, Marty.
20 I'm going to try to dumb it down because I'm not a
21 lawyer. So, you do business in Mexico. Correct?

22 MR. HIRSCH: Yes, sir.

1 BOARD MEMBER PRIMUS: So, you are subject
2 to the same rules and regulations as KCS currently
3 and UP and anybody else who's operating down there.
4 Correct?

5 MR. HIRSCH: We do not operate in Mexico, to be clear.
6 The routes that we showed earlier have FXE and KCSM.
7 Those are the two operators.

8 MR. DENTON: We just go the border
9 and Eagle Pass, not even Eagle Pass, El Paso, and
10 then we interchange inland at Robstown in South Texas
11 and then it goes over the Old Tex-Mex to Laredo.

12 BOARD MEMBER PRIMUS: Okay. With the
13 interchange, do you still have any indication or
14 understanding of what's the fees or the rates. So
15 basically, you're going into it blind when you do it
16 for your customers?

17 MR. HIRSCH: Yes, depending on the
18 railroad, depending on the agreement that we have.
19 If we have a through rate, then we're going to know
20 the divisions because we worked together to put the
21 rate together, but in the case of KCS when we have
22 just Rule 11, we have no visibility on what they're

1 charging the customer on the Mexican side.

2 BOARD MEMBER PRIMUS: And so, you also
3 have no visibility on that interchange, what your partner
4 in Mexico is charging also; is that correct?

5 MR. HIRSCH: That's correct, sir.

6 BOARD MEMBER PRIMUS: Okay. So, would it
7 be fair to say what you're asking for is for full
8 transparency for KCS going forward if this
9 transaction were to be consummated?

10 MR. HIRSCH: What we're asking for is the
11 ability to compete and then we are proposing one
12 mechanism there may be others, but what we want is to
13 make sure that we cannot be foreclosed by
14 manipulating the rates on the Mexican side.

15 BOARD MEMBER PRIMUS: I guess my last
16 question is, so if we were to impose this upon KCS
17 would we then have to impose it upon you or anybody
18 else for doing business in Mexico also. Whether or
19 not you have a partner down there or not, should we
20 be aware of the rates that are being charged there
21 for your business too?

22 MR. HIRSCH: No, sir, because the

1 situation at Laredo is unique, as I was trying to
2 explain. What you have today in Laredo with the U.S.
3 railroad owning the Mexico portion, it's unique to
4 KCS, KCSM.

5 BOARD MEMBER PRIMUS: Okay. So, you're
6 saying basically it would be transparency for them,
7 but not necessarily for you, for your business?

8 MR. DENTON: I'm not sure that's the way
9 to characterize this. What we're talking about is a
10 rate in Mexico right now which has zero transparency
11 and that's where the issue that we've identified
12 here. Frankly, it's a narrow issue. There are
13 others who have talked about open gateways across the
14 entire country and trying to identify mechanisms to
15 solve for that.

16 We've identified a very narrow issue here
17 about being able to hide the rate in Mexico and what
18 we've proposed is a solution for that. And we think
19 that the idea that we would be able to, UP, anyone
20 else would be able to use this proportional rate
21 mechanism to compete is the fix.

22 MR. NOBER: If I could just, Commissioner,

1 just make one more point. I think the difference
2 here is that the Mexican railroad and the competing
3 U.S. carrier would all be owned by the same entity.
4 So, in the other gateways, the FxE, the Mexican
5 carriers is independent and independent U.S. carrier
6 interchange with an independent Mexican carrier and
7 we have models for that all over the country as to
8 how independent railroads are able to set rates with
9 each other.

10 In this instance, you'd have the company
11 that owns the entire route setting rates for those
12 that it competes with and that's why you would ask
13 for a different regime at Laredo than you would
14 anywhere else because what's happening now is that
15 KCS is being bought by CP will now have reach to go
16 all the way to Chicago. And what Mr. Hirsch was
17 saying before is that right now KCS can't get to
18 Chicago. So, if they want to move intermodal auto
19 parts, intermodal goods, anything to Chicago they
20 have to interchange with another railroad.

21 We have a marketing agreement with KCS.
22 You see on this line that when we have a cooperative

1 agreement we're able to grow business because there's
2 demand for that. When CP can get to Chicago by
3 itself, then the desire to be able to -- and their models
4 show that they're going to want to keep that traffic
5 on the combined railroad.

6 BOARD MEMBER PRIMUS: I get that. I
7 appreciate that, Roger. Where I get stuck is just
8 that transparency aspect where I know it's all owned
9 by the U.S., but there's still that transaction at
10 the border and others that we don't know. And if
11 we're going to put that full transparency on one
12 carrier and the other carriers don't have that, then
13 maybe there's a way for us in terms of how we deal
14 with Mexico and others to figure it out. The same
15 thing would be applied in Canada too. I mean if we
16 didn't know that I'd ask the same questions for that
17 from U.S. going into Canada.

18 MR. NOBER: And Courtney, we have the I-5
19 prop rate that goes from the Northwest does apply
20 to British Columbia.

21 MS. ESTES: Yes, we have the prop rate
22 in place already for the I-5 between us and UP where

1 we populate a matrix with actual market rates that we
2 use for moves that cross over the Portland Gateway and go
3 into -- from the northern region, which includes British
4 Columbia and also includes interchange to Canadian
5 carriers with origins or destinations in Alberta,
6 Saskatchewan, and British Columbia. So, we have that
7 today and that works pretty well to populate those
8 rates.

9 CHAIRMAN OBERMAN: I have a few
10 questions. Preliminarily, who owns FXE?

11 MR. HIRSCH: It's Grupo Mexico; it's a
12 Mexican company.

13 CHAIRMAN OBERMAN: So, neither you nor UP
14 have any interest in that railroad?

15 MR. HIRSCH: UP has an interest on
16 Ferromex, yes.

17 CHAIRMAN OBERMAN: Do you know what the
18 percentage is?

19 MR. HIRSCH: I think it's about 26
20 percent.

21 CHAIRMAN OBERMAN: I want to get back to
22 a few issues that you covered here. Looking at the

1 chart that's up there now, what page is that? I can
2 look at it. Say it again, 36?

3 So, in 2016, as I understand it, you're
4 telling us that you made a deal with KCS which
5 allowed for KCS to participate in some rate or
6 revenue because it could ship all these intermodal
7 containers and automotive shipments, I guess both, to
8 Chicago and beyond by making a deal with you; is that
9 what happened here?

10 MR. HIRSCH: We had a joint agreement,
11 yes, to provide intermodal services through Mexico
12 and the U.S., yes.

13 CHAIRMAN OBERMAN: And KSC was motivated
14 to do that, I think you said, because otherwise they
15 would not have moved any of this traffic because they
16 couldn't get it to Chicago.

17 MR. HIRSCH: That's correct.

18 CHAIRMAN OBERMAN: Is that right?

19 MR. HIRSCH: Yes, sir.

20 CHAIRMAN OBERMAN: Now, you're telling us
21 that they will no longer have the motivation to make
22 a deal with you because they can get to Chicago on

1 CP, if the deal goes through.

2 MR. HIRSCH: That's correct.

3 CHAIRMAN OBERMAN: And then you're
4 telling us that because of the congestion in Houston
5 the customers won't want to actually go through them
6 to Chicago, so all this intermodal traffic will go
7 back on the road, or much of it.

8 MR. HIRSCH: The intermodal business is
9 basically competing against trucks and it's a
10 combination of transit time and rates.

11 CHAIRMAN OBERMAN: I understand.

12 MR. HIRSCH: So, what we are saying is
13 here is that on the rate side we can be manipulated
14 so that it's more expensive to interact and then
15 because of what Mr. Gabriel said yesterday and the
16 fact that today there is no intermodal service
17 running there and that's a longer route that there's
18 a chance that the service over there is not going to
19 be that competitive.

20 CHAIRMAN OBERMAN: Right. So, it won't
21 work and the trucks will go back on the road and you
22 won't have the traffic either and KCS won't have the

1 traffic.

2 MR. HIRSH: That's correct.

3 CHAIRMAN OBERMAN: That doesn't make a
4 lick of sense to me because the whole reason for this
5 agreement was so KCS could get the traffic that they
6 weren't getting. Now, you're saying that they're
7 going to put themselves in a position where they
8 can't deliver and they still won't get the traffic,
9 so they won't have you and they won't be able to get
10 there on CP. If that were to happen, I can't see why
11 KCS wouldn't come back to you and at least get the
12 traffic they're getting now rather than getting none
13 and all of it goes on the highway.

14 MR. HIRSCH: That could probably happen.

15 CHAIRMAN OBERMAN: Yes. So, I think
16 there's a missing link here in your logic.

17 MR. HIRSCH: In the intermodal business,
18 that competes against truck. Those customers are
19 very transit time sensitive. So, this happens regularly
20 whenever there's congestion in the U.S. that those
21 customers divert the traffic right away. It happens
22 during the crisis that we're having right now. A lot

1 of traffic than normally goes intermodal went back to truck.
2 So, what we're saying is that if it's not a
3 competitive service that can provide the transit
4 time required by these time sensitive shipments,
5 those could go back to truck in a matter of hours.

6 CHAIRMAN OBERMAN: I understand that, but
7 they also could come back to you rather than lose the
8 traffic to truck and lose it all together why
9 wouldn't KCS say, you know what, we can't hold onto
10 these intermodal customers because we're too slow
11 through Houston? If that happens now, why wouldn't
12 it happen in the future?

13 MR. DENTON: Mr. Chairman, look at the
14 blue line.

15 CHAIRMAN OBERMAN: I'm looking at it.

16 MR. DENTON: From before 2016.

17 CHAIRMAN OBERMAN: I'm looking at it.

18 MR. DENTON: They have the same incentive
19 that they did when the blue line started going up to
20 move this traffic. It was incremental traffic
21 starting at the KCS Tex-Mex merger and it wasn't
22 moving then. It was moving by truck. I mean that is

1 the distinct possibility that could happen here as
2 well.

3 MR. NOBER: That's real-world
4 experience.

5 CHAIRMAN OBERMAN: No, no, I understand.
6 But you're saying once they take the traffic away
7 from you, they won't be able to deliver it, it's
8 going to go back to truck. So, KCS will be left, the
9 new combined railroad will be left without these
10 movements. You said the incentive to KCS to enter
11 into the deal which resulted in the blue line was it
12 was better for them to get some revenue and the rest
13 for you to go to Chicago than to get none of it.

14 MR. DENTON: That incentive existed
15 starting in 2006 and existed for 10 years and you can
16 see the blue line bouncing on the bottom there.

17 CHAIRMAN OBERMAN: Well, I assume that
18 KCS has now figured it out. Maybe they're slow
19 learners, but the notion that they're going to
20 immediately revert 80,000 potential loads that they
21 could take at least to interchange with you doesn't
22 make any economic sense to me. I just want to tell

1 you I think the argument defeats itself based on the
2 way you described it.

3 MR. REISHUS: Mr. Chairman, I'm sorry as
4 an economist to bring up the notion of
5 tradeoffs, but there's tradeoffs. There's this vast
6 pool of trucks that are moving between the U.S. and
7 Mexico and the question is how much of that pool can
8 CP/KCS and KCSM get and at what rate.

9 They have incentive to get as much of
10 that traffic as they can at a good rate and whether
11 they can do it or not that's a question the future
12 will decide, but they would rather move their
13 traffic on their system at a higher rate if they can
14 do it. And if the tradeoffs are big enough and good
15 enough they may permit others, but their first
16 incentive is going to be --

17 CHAIRMAN OBERMAN: I understand that, but
18 you just said it isn't going to work because Houston
19 congestion will prevent them from delivering and it's
20 sensitive traffic, so it will leave them and go to
21 truck. Why won't it leave them and come back to you?

22 MR. HIRSCH: That's for sure a

1 possibility.

2 CHAIRMAN OBERMAN: Not only a
3 possibility, it seems to me a high probability based
4 on the arrangement you have now.

5 MR. HIRSCH: But again, the moment that
6 they have a service that they think could be
7 competitive --

8 CHAIRMAN OBERMAN: Yeah.

9 MR. HIRSCH: -- in this market, they will
10 have the ability to foreclose us and make sure that
11 all that freight goes on CP/KCS.

12 CHAIRMAN OBERMAN: In other words, if
13 they spend all the infrastructure in Houston that you
14 think they should spend and move trains fast through to
15 Houston, then maybe you're right.

16 MR. HIRSCH: That's correct.

17 CHAIRMAN OBERMAN: So, I mean I don't
18 know how you can have it both ways. You know you
19 want them to have a better route through Houston and
20 if they do that they're going to provide better
21 intermodal service than you, but if they decline to
22 build infrastructure in Houston, you're going to keep

1 all this intermodal service because they can't do it.

2 MR. HIRSCH: We just want to compete.

3 CHAIRMAN OBERMAN: Pardon?

4 MR. HIRSCH: We just want to compete.

5 CHAIRMAN OBERMAN: No. I understand.

6 BOARD MEMBER HEDLUND: Could I -- well, I
7 don't want to interpret your train of thought.

8 CHAIRMAN OBERMAN: Well, I was sort of
9 finished with this train of thought, so I have a few
10 more questions. Go ahead.

11 BOARD MEMBER HEDLUND: Roger, could you
12 educate me on what our jurisdiction is in terms of the concern
13 about competition in a foreign country?

14 MR. NOBER: Well, the STB does not have
15 jurisdiction over internal cabotage in Mexico to
16 pickup to drop off, but these are international
17 movements and the STB has rate jurisdiction in the
18 United States over through movements. It does and it
19 has service and it approves mergers. And as Courtney
20 said earlier, in the UP/SP merger, it approved a
21 condition that included international rates to and
22 from Mexico. So, what we are asking for here and

1 what we think the agency absolutely has jurisdiction
2 to do is to condition an international movement on a
3 certain rate that's a component of the overall
4 through rate.

5 BOARD MEMBER HEDLUND: I understand that.
6 Mine is a little more subtle of a question and that
7 is we are to look at competitive effects. I mean are
8 we to take into account competitive effects outside the United
9 States?

10 MR. DENTON: Absolutely. So, your
11 organic statute specifically contemplates that and all
12 of your precedent on mergers that have international
13 aspect, that your predecessor agency and the STB have
14 asserted jurisdiction to deal with these issues.

15 BOARD MEMBER HEDLUND: No. I mean I
16 understand we have jurisdiction to look at
17 competition to serve foreign markets, but do we also
18 look at competition that originates, I guess, in
19 foreign markets?

20 MR. NOBER: Yes, you do because it's part
21 of cross-border traffic. So, whether they're
22 international shipments to or from Mexico, to or from

1 the United States. So, what you're looking at is the
2 ability of U.S. shippers to be able to serve
3 destinations in Mexico and then Mexico destinations
4 to be able to serve U.S. shippers, so you're really
5 on behalf of the U.S. shippers in both instances.

6 But yes, and in fact, way back in the day
7 the BNSF suggested using the new rules because the new
8 rules call out clearly the analysis to be done for
9 international. Now, I think we still feel you could
10 do the same analysis here and strongly urge you to do
11 that.

12 BOARD MEMBER HEDLUND: Unless it's
13 implicated by the new rules.

14 MR. NOBER: It's implicated by both.

15 MR. DENTON: This is not a new rule/old
16 rule issue. This is going back to the beginning
17 issue of the ICC. This is really at its heart.
18 Applicants have said that they want to keep an open
19 gateway, right? They've offered a mechanism that's
20 been described during this hearing as kind of
21 amorphous, squishy by the Applicants, I think they
22 described it as, but what we are saying is that there

1 needs to be an actual mechanism to enforce what
2 Applicants have already said you can do, right, which
3 is keep an open gateway between Mexico and the U.S.

4 BOARD MEMBER HEDLUND: I'm new here. I'm
5 the new kid on the block.

6 MR. DENTON: Sure.

7 BOARD MEMBER HEDLUND: And I just want to
8 be educated about what the scope of our legitimate
9 concerns ought to be.

10 MR. DENTON: Completely fair, Commissioner
11 Hedlund. And again, I would commend you to read
12 Section 3 of our opening comments that really goes into
13 depth on this issue.

14 BOARD MEMBER HEDLUND: Okay. Thank you.

15 BOARD MEMBER FUCHS: Would you propose
16 that your suggested rate regulation apply to exempt
17 traffic?

18 MR. DENTON: This is not a rate
19 reasonableness issue, right? Yes, so it would apply
20 to -- we've come up with an idea of, right, of a
21 prop rate mechanism. What we've described is that
22 there are many ways to figure out how this prop

1 rate mechanism might work, and Dr. Reishus is going
2 to talk about this in some detail. So yes, it could
3 apply to intermodal, it could apply to grain, it
4 could apply to --

5 BOARD MEMBER FUCHS: That's the
6 disconnect. Marty, this is maybe a pinch and I know
7 you're talking about the disconnect between Houston
8 and this, but there's a bit of a disconnect for me
9 because BN and others have said for years you don't
10 need to touch the rates of these in any way because
11 there's such strong competition in these markets and
12 I understand you exclude autos and intermodal from
13 your carloads and perhaps there are some carloads in
14 here that might not have that much market
15 flexibility. The railroad might have more market
16 power than they do for intermodal and auto, but
17 particularly for intermodal and auto, and I think
18 some of your focus on trucks being -- rail freight being
19 diverted to trucks is on the intermodal side.
20 There's all this competition and that would seem to
21 imply that CP/KC would not have much pricing power.
22 Where are they going to get the pricing power?

1 MR. DENTON: All of this is so narrowly
2 focused on Laredo for us because of the problem that
3 we've identified for you.

4 BOARD MEMBER FUCHS: But why does CP/KC
5 have pricing power over intermodal when you all have
6 maintained for years that there is no pricing power
7 in intermodal.

8 MR. NOBER: Because we're talking about
9 pricing power in intermodal in the United States, so
10 you start at Los Angeles where there are two
11 competing railroads and multiple interstate highways
12 and trucks. This is a different market,
13 Commissioner. This is looking at the market in
14 Mexico where there's one border crossing and so the
15 regulatory structure is different. The access is
16 different. The ability to access the other market is
17 different. So, I would respectfully submit that
18 you're comparing apples and oranges to say a
19 statement that's made about intermodal traffic in
20 the United States is the same as a potential
21 intermodal traffic from the valley of Mexico.

22 BOARD MEMBER FUCHS: Well, there's quite

1 a bit of the intermodal traffic that's going to go
2 through the Port and we have heard, including from
3 Port witnesses, including from Commissioner Bentzel
4 worried about the intense competition in the West
5 Coast ports. I hear all the time about the intense
6 competition between LA and Long Beach and say Prince
7 Rupert and to some extent Vancouver with you all, so
8 this is a new argument that there's not intense
9 competition between West Coast ports because of the
10 country?

11 MR. NOBER: We are not talking about
12 intermodal shipments into Manzanillo. This is
13 domestic intermodal, which is a different market
14 that's going from the United States, say auto parts
15 that are put in containers that are manufactured in
16 the Midwest that are going to auto assembly plants in
17 Mexico. This is not about going to the Mexican ports
18 and moving international intermodal. This is almost
19 principally domestic intermodal movements from
20 factories in the valley of Mexico to the United
21 States and vice versa. And I would respectfully say,
22 and Mr. Hirsch can go into that, I think you're

1 mixing up markets.

2 BOARD MEMBER FUCHS: Does your prop rate
3 mechanism exclude international intermodal?

4 MR. DENTON: So, what we have proposed is
5 showing you how the prop rate works. Right? We have
6 not come in and asked you to implement a particular
7 mechanism that deals with particular types of traffic
8 to particular destinations, right? We've explained
9 how I-5 works.

10 BOARD MEMBER FUCHS: Well, then
11 respectfully then, I'm not the one that's mixing up
12 markets because you have mixed all the markets
13 together in your prop rate mechanism. You have not
14 differentiated competitive traffic versus
15 non-competitive traffic.

16 MR. DENTON: I respectfully disagree and
17 again I think Dr. Reishus to going to get
18 into this.

19 BOARD MEMBER FUCHS: Does your prop rate
20 mechanism apply to competitive traffic?

21 MR. DENTON: The very premise of our prop
22 rate mechanism is that there is a lack of competition

1 and a competitive issue in Mexico.

2 BOARD MEMBER FUCHS: So, is there any
3 competitive traffic coming over the Laredo Gateway?

4 MR. NOBER: I don't think the Board's
5 exemption of what's competitive and exempt from
6 regulation has ever analyzed or looked at Mexico. So,
7 I think you're applying a U.S. doctrine which is what
8 is market dominant and competitive in the United
9 States versus what is in Mexico and those are not --
10 no finding has ever looked at is there domestic
11 intermodal competition in Mexico or not.

12 BOARD MEMBER FUCHS: My question is a bit
13 more simple, which is -- is there competitive traffic
14 coming over Laredo?

15 CHAIRMAN OBERMAN: Patrick, can I just
16 amend that because I think I understand what you're
17 focused on. Is there international container traffic
18 coming from the Mexican port and then coming through
19 Laredo.

20 BOARD MEMBER FUCHS: More broadly, is
21 there competitive traffic, product competition,
22 geographic competition, multiple lanes, is there

1 competitive traffic coming through that gateway
2 because what you're having us do with a prop rate
3 mechanism that applies to competitive traffic is
4 artificially lower rates for rates that are already
5 constrained for what the top line interline rate is.

6 So, if there is a competitive rate for a
7 top line interline rate and then you're going to have
8 us divide up a competitive rate on a mileage basis it
9 would seem to me that we're distorting competitive
10 markets.

11 CHAIRMAN OBERMAN: Dr. Reishus?

12 DR. REISHUS: Yes. I said if you start
13 with the premise that this is already competitive
14 traffic --

15 BOARD MEMBER FUCHS: I'm asking is there
16 competitive traffic. There's no competitive traffic
17 that goes over Laredo?

18 DR. REISHUSH: There are degrees of
19 competition. There's going to be some with more or
20 less market power for different traffic. I think
21 that's clear, but the notion that the --

22 BOARD MEMBER FUCHS: Doctor, let me just

1 focus on that for a second. It's your view that it's
2 a good idea for the Board to divide rate divisions
3 based on mileage for an interline rate that is set
4 competitively?

5 DR. REISHUS: It is my opinion that when
6 the gateway behavior precludes the competitive rate
7 then it is a good idea to --

8 BOARD MEMBER FUCHS: I'm talking about
9 the competitive traffic.

10 CHAIRMAN OBERMAN: Let me make a
11 suggestion. On this topic, because I have some more
12 questions before we get to Dr. Reishus, let him make
13 his presentation and then I think the questioning
14 will probably be more efficient based on what his
15 overall views are, if you're okay with that.

16 I have some follow-up questions primarily
17 for Mr. Hirsch on some of these charts. I'm a little
18 uncertain about what BN's goal is here, looking at
19 the chart that's up there now. If whatever kind of
20 remedy we were to grant resulted in BN being able to
21 retain this traffic on that blue line, does that
22 satisfy what you're asking of us or do you want more

1 than that?

2 MR. HIRSCH: We're not asking to retain
3 that. We're asking to be able to compete for that business.

4 CHAIRMAN OBERMAN: No, no, I understand,
5 but just that business?

6 MR. HIRSCH: No, all business that can go
7 over Laredo.

8 CHAIRMAN OBERMAN: So, you're not seeking
9 a result which just enables you to be competitive on
10 the automotive and intermodal part of it that's
11 represented by the blue line.

12 MR. HIRSCH: That's correct.

13 CHAIRMAN OBERMAN: Your relief that
14 you're seeking goes beyond that, is that right?

15 MR. HIRSCH: Because of the uniqueness of
16 Laredo and all the markets that are served by Laredo.

17 CHAIRMAN OBERMAN: I understand. When
18 the rates at Laredo to Robstown, when those doubled,
19 did BN examine whether to bring a rate case to us to
20 challenge the rate?

21 MR. HIRSCH: I think it was explained by
22 Mr. Nober yesterday on the difficulty to do that

1 because of the lack of transparency and the inability
2 to see those rates and that this happened over a period of
3 time.

4 MR. NOBER: We had no ability.

5 CHAIRMAN OBERMAN: What do you mean you
6 had no ability.

7 MR. NOBER: We had no idea what the rate
8 being charged in Mexico was. It was only in this
9 proceeding that we were able to discover that, so
10 that's the point about visibility, Mr. Chairman, is
11 that we have no -- all we know is that we didn't win
12 the business. We don't know why.

13 CHAIRMAN OBERMAN: But you've said your
14 rate just between Robstown and Laredo you knew what
15 that was and it doubled. You didn't bring a rate
16 case to challenge it.

17 MR. DENTON: A few things, BNSF's instinct
18 is not to run to the regulator when something like
19 this happens, it's to try to build new business and
20 compete. I mean we've seen what the effect,
21 practical effect of coming to the Board and asking
22 for relief, petitioning for enforcement of merger

1 conditions. The pace of that relief often exceeds
2 the pace of commercial activity and by the time we
3 get the relief, we're often vindicated, frankly, the
4 commercial opportunity that we -- was the reason why we
5 sought relief is gone and so our instinct is to go
6 compete and try to build new business.

7 CHAIRMAN OBERMAN: Well, I appreciate
8 that. You may not be running, but you're certainly
9 walking at a fast pace to the Board now asking for
10 relief and if it was so detrimental to your
11 business, I don't know how much was at stake, if the
12 rate was so high as to prevent competition it's hard
13 for me to imagine why you didn't contemplate a rate
14 case. It's been 17 years and the slowest rate case
15 we've ever had has never taken 17 years. So, I'm a
16 little bit confused as to why if this completely cut
17 off your ability to compete because the rate was so
18 high and none of our rate mechanisms would've
19 provided relief to you? All of these were -- was it
20 your conclusion that you couldn't win at such a rate
21 case?

22 MR. NOBER: Well, I explained it

1 yesterday and I'll repeat it again today and you may
2 or may not accept it, but there's several reasons.
3 The first is this looks dramatic now in hindsight,
4 but you have to remember at what point in time do we
5 then say, well, this latest commercial action is the
6 reason that we would -- that's the first thing.

7 The second thing is that, as we said, our
8 experience in coming to the Board or customers coming
9 to the Board to try to get addressed, post-hoc,
10 looking backwards, merger conditions hasn't really
11 worked very well for us and one of the cases we have
12 has been pending for more than 10 years.

13 And third, I'm not sure we would have
14 standing to look at this, to bring a rate case. We
15 might've had standing to say you're not complying
16 with the merger condition, which is what Mr. Meyer
17 said the other day, but we don't have standing to
18 bring a rate case or at least I'm not sure that we
19 would have standing to bring a rate case.

20 And customers have looked at the 10 years
21 it's taken, for example, in one of the other docket
22 matters we have and said how is that going to work?

1 And so, these are dynamic markets. And finally, and
2 I think most importantly, you could see that our
3 business growth depended on cooperating with KCS, not
4 bring litigation against them.

5 CHAIRMAN OBERMAN: So Roger, can I infer
6 that at least BN doesn't agree with what I frequently
7 hear from AAR, that the reason nobody brings rate
8 cases here is because they're happy with their rates?

9 MR. DENTON: I think they're apples and
10 oranges, Mr. Chairman.

11 CHAIRMAN OBERMAN: Are your frustrations
12 and understandable reluctance to bring long rate cases
13 similar to shippers' same reluctance.

14 MR. NOBER: I respectfully disagree. I
15 mean we're talking about merger conditions.

16 CHAIRMAN OBERMAN: No, no, I'm talking
17 about --

18 MR. NOBER: I said we have no standing to
19 bring a rate case. These are all about imposing --
20 and the cases I've talked about are about evaluating
21 and imposing merger conditions, not about rate cases.
22 These are not rate case matters. These are merger

1 conditions.

2 CHAIRMAN OBERMAN: Well, I'm not going to
3 opine on standing, but it does seem to me that you
4 pretty much hit bottom about 12 years ago and that
5 was a long time to suffer this loss of business.

6 Let me ask this question, if this merger
7 request had never gelled, would BN have just been
8 content to let this graph look like it did into the
9 indefinite future?

10 MR. DENTON: Well, just first, before, Paul,
11 we're not going to engage in hypotheticals about what
12 our commercial strategy might've been if this merger
13 -- what we've done is looked at what the Applicants
14 have proposed and clearly identified an issue and
15 identified frankly what we think is a relatively
16 straightforward solution.

17 CHAIRMAN OBERMAN: Well, it does strike
18 me -- this came up yesterday in a different context
19 with CN, that there's a certain reactiveness here to
20 say, well, we were living with this situation,
21 everything was stable and fine, but now somebody
22 comes in for a merger it gives us a chance to jump in

1 and get some goodies.

2 MR. NOBER: I strongly disagree with that
3 characterization. When you are merging, you are
4 changing the competitive landscape permanently and
5 that is the juncture when this agency should be
6 looking at what are the competitive landscape and
7 conditions. That is an inflection.

8 CHAIRMAN OBERMAN: It is, but this merger
9 isn't going to change the competitive landscape of
10 those orange bar charts. The fact that the --

11 MR. NOBER: Yes, it will because it's
12 expanding the scope of the KCS. It's expanding its
13 geographic scope through much of North America and
14 that is changing the competitive landscape and so we
15 would urge you to think about that. When CP buys
16 them it is adding single-line service to a much
17 larger portion of the North American continent and
18 that is changing the competitive landscape.

19 CHAIRMAN OBERMAN: You've already lost
20 that business, according to you, so now you're using
21 the merger to try to get it back. That's what it
22 sounds like to me.

1 MR. HIRSCH: No. What we're trying to
2 say is that if business that we lost was from places
3 where KCS was there before and we lost that part, now
4 that there's an opportunity for KCS through Laredo to
5 access other markets in the U.S. and Canada,
6 business of today we may be moving now may go into
7 that.

8 CHAIRMAN OBERMAN: And by the way,
9 nothing I am saying suggests that whatever the
10 pricing instituted by KCS back in 2005 was proper or
11 supportable. I'm not making that observation. I'm
12 trying to assess the credibility of the case you're
13 putting on now.

14 MR. DENTON: Mr. Chairman, if I may
15 briefly, we are not seeking any level of traffic here. We
16 are not saying that we need to restore that bar chart
17 up to the top. All we are asking for is an
18 opportunity to fairly compete for that traffic and we
19 recognize that CP/KCS will have single-line
20 efficiencies and benefits and they very well may win
21 significant portions of this traffic. We get that.

22 CHAIRMAN OBERMAN: Well, I don't think

1 you're here wasting your time or your client's money
2 because you don't think you're going to get traffic
3 if we acceded to what you're asking to be done, so I
4 assume you see a business advantage.

5 Let me go back to page 30, if we could.
6 When you say the value of rail traffic over Laredo,
7 what's that number, in what respect, the revenue that
8 the railroad earns?

9 MR. HIRSCH: No. That's the value of the
10 goods.

11 CHAIRMAN OBERMAN: The value of the
12 goods. It doesn't tell us what the respective
13 revenues and profits are to the railroad.

14 MR. HIRSCH: No, it doesn't.

15 CHAIRMAN OBERMAN: Could you tell us what
16 such a bar graph would look like?

17 MR. HIRSCH: Not off the top of my head,
18 sir. What I can tell you is that, in units, where we move
19 most units through the border. So, as I was saying
20 before, today after what you saw the growth on the
21 chart, the number of units that we cross over Laredo
22 today is about double that we cross over Eagle Pass.

1 CHAIRMAN OBERMAN: Now, that I
2 understand, but I can't draw much conclusion about
3 what it means financially to the railroads from this
4 bar chart. It doesn't tell me because the value of
5 goods doesn't equal value of revenue.

6 DR. REISHUS: Mr. Chairman, I agree with
7 that. I point to my Figure 2 in my initial report
8 where we to show tonnage --

9 CHAIRMAN OBERMAN: Why don't we
10 hold off until you get to that, maybe --

11 DR. REISHUS: Okay.

12 CHAIRMAN OBERMAN: -- because I'm
13 frustrated that you keep getting interrupted and
14 don't give a chance to get us your full
15 presentation. You may be frustrated too.

16 I want to go back to the map of different
17 routes into Mexico. There it is on page 30 -- well,
18 it's on the same page, I guess, I'm sorry. That's
19 why I couldn't find it. If I look at this map and
20 then look at the -- you know I think that's an
21 unfortunate name, Golden Triangle. It has a lot of
22 other meanings in the world.

1 But I tried to look at those maps
2 together and this is a question out of my ignorance
3 of what the landscape is there, but it looks to me,
4 just looking at the map on page 30 that I can't
5 quite figure out why you can't go into Mexico on Eagle
6 Pass down to FXE and turn east and interchange and
7 get right into that Golden Triangle, why does that
8 not work?

9 MR. HIRSCH: Well, there is, as you know,
10 different quality on the tracks in Mexico and then
11 there's the population in Mexico is centered in
12 certain parts. So, when you see there the green part
13 eastern of KCS that's not where the population or the
14 people live, right? So, the map doesn't show you the
15 concentration of population, but it's not where that
16 green line is on the right side. So, that's why we
17 said the importance of Laredo is that it has direct
18 access to major metropolitan areas of Monterey, San
19 Luis Potosi, Mexico City, and a lot of cities that
20 are there in between, like Queretaro -- . So, the industrial
21 and the concentration of the population in Mexico is
22 actually over KCS lines. And when you see on the map

1 that there's a green line over there, but if you're
2 talking about 100 miles from the population, then
3 you're not going to be able to serve it when you have
4 KCS that's goes through the middle of that population.

5 CHAIRMAN OBERMAN: Well, I'm just trying
6 to understand the map and these are small maps, but
7 it looks to me on page 30, just south of Laredo where
8 the green and the blue lines intersect is roughly
9 where Monterey is.

10 MR. HIRSCH: That's where Monterey is,
11 correct.

12 CHAIRMAN OBERMAN: So, if you go through
13 Eagle Pass and down the FXE line then turn east you
14 at least get to Monterey and then you're saying you
15 can't use the KCSM lines to get through the rest of
16 the triangle even after you're in Mexico.

17 MR. HIRSCH: No. And if you look, the
18 two green lines they show a lot closer on the map,
19 but you're talking about more than 100 miles there,
20 so there's significant distance between one and the
21 other. And again, KCS and KCSM line goes through
22 these major populations and where most of the

1 industries are. So, if you have something that's 100
2 miles way from that, you're not going to be able to
3 compete.

4 CHAIRMAN OBERMAN: A hundred miles is
5 sufficient to eliminate your competitive ability?

6 MR. HIRSCH: Well, it depends on the
7 different commodities and then the other thing you
8 need to consider is that today in Mexico you have a
9 lot of these facilities that are on KCS, so you may be
10 pretty close, but if you have a shuttle station that is
11 on KCS that today they can go to the border and have
12 options then in the future they're not going to have
13 any options and you cannot compete to that shuttle
14 station from a route even if it's a few miles away.

15 CHAIRMAN OBERMAN: Well, I've been
16 hearing, and correct me if I'm wrong, that in the
17 merged KCS/CP route up through Chicago and points
18 north and east is not necessarily the most efficient
19 U.S. route compared to BN, so doesn't that give you a
20 competitive advantage once you get into Mexico, maybe
21 you got 100 more miles there to get into the Golden
22 Triangle, but when you get back to the United States

1 you have something to offer that maybe KCS/CP doesn't
2 and I don't know if you've analyzed that or not or
3 you're putting all your eggs in this prop rate
4 basket.

5 MR. HIRSCH: What I can tell you is that
6 over all these years we have been trying to compete
7 for that business, so we have tried. We couldn't
8 make it.

9 CHAIRMAN OBERMAN: Have you tried to do
10 it through Eagle Pass?

11 MR. HIRSCH: Yeah.

12 CHAIRMAN OBERMAN: And customers don't
13 chose you, is that what you're saying?

14 MR. HIRSCH: That's what we're saying.

15 CHAIRMAN OBERMAN: Just to get back to
16 something you said, Roger, are you telling me that if
17 you had seen the rate over the Robstown portion
18 double and you came in here and said they're
19 violating the Tex-Mex merger condition, through
20 discovery you wouldn't have gotten visibility that
21 you needed to prove your case?

22 MR. NOBER: As I said, I'm not sure that --

1 we're not a ratepayer, okay.

2 CHAIRMAN OBERMAN: No. But you could
3 enforce the merger conditions.

4 MR. NOBER: But enforcing the merger
5 conditions, as I said, I don't know and I don't want
6 to speculate as to what discovery a Board in 2007
7 might've given us.

8 CHAIRMAN OBERMAN: Well, do you have some
9 reason to think it wouldn't have been worth asking
10 for? I mean you seem to put all the roadblocks on
11 the fact that you don't have visibility into the
12 Mexico portion.

13 MR. NOBER: Correct. And the short line
14 is --

15 CHAIRMAN OBERMAN: And it's inconceivable
16 to me if you had a meritorious claim on its face of a
17 violation of the commercially reasonable terms of the
18 merger condition that to litigate that claim you
19 wouldn't have been entitled to get the information you
20 needed to prove your claim. I'm not ruling on it at
21 this point, but I don't see how any Board would've
22 said, no, you can't have the facts so you may or may

1 not have a claim, but you don't get to prove it
2 because we won't give you the facts. That seems
3 unreasonable.

4 MR. NOBER: That very well may be the
5 case, Mr. Chairman. And none of us were there when
6 this happened, none of us were with BNSF. We
7 can't say what the decision was then, but really what
8 we're saying now is we've identified the issue.
9 We've seen through the course of this merger
10 proceeding, through discovery in this proceeding, what
11 the issue is and we're bringing it to you.

12 CHAIRMAN OBERMAN: Well, all I'm saying
13 is, as I weigh all these requests. And one of the
14 reasons that I've gone into it with you, with CN, and
15 so forth is the need for the relief that you're
16 asking has to be measured against how this has
17 functioned over the last period of time, at least
18 since the initial KCS acquisition of the Mexican
19 railroad. And when I don't see somehow the evil
20 being so great as to warrant your coming in to try to
21 do something about it and then all of a sudden I see
22 it, it just affects my ability to judge how much it's

1 needed. That's why I'm asking these questions.

2 MR. DENTON: I will offer, Mr. Chairman,
3 that I think this is exactly the right time to deal
4 with these issues and we've seen that coming back to
5 the Board maybe 5 years, 10 years after a merger and
6 trying to get some type of specific relief with
7 respect to a particular customer is difficult.

8 Again, we are often vindicated when we
9 seek such relief, but by the time we get the relief
10 the commercial opportunity is gone. And frankly,
11 this is the time to address these types of issues.

12 CHAIRMAN OBERMAN: Well, let me just say
13 this from where I sit, and I don't know about the
14 other Board members, this argument about foreclosure
15 is not in a vacuum. We've got a lot of people in
16 here arguing about foreclosure and so is there
17 foreclosure and then just a little foreclosure? I
18 mean foreclosure strikes me as an all-encompassing
19 word and concept and it strikes me you had a lot of
20 foreclosure, but now you're afraid of just a little
21 more foreclosure, so you're seeking relief. That's
22 the way I'm hearing it and I'm trying to figure out

1 how much foreclosure, if there is foreclosure, is too
2 much to warrant the kind of relief you're seeking.

3 Listen, as you all know, I have felt --
4 not felt, concluded strongly since I've been here
5 that this industry needs more competition, so I'm not
6 looking for ways to avoid it, but I am looking for
7 the merits of the claims that are being brought here
8 and what we should do within the constraints of our
9 authority. So, I have some other questions on this
10 whole issue, but I think that they'd be more
11 appropriate after Dr. Reishus makes his
12 presentation. Does anybody else have any questions
13 at this point? We may end up coming back, but -- I'm
14 sorry. Michelle, go ahead.

15 BOARD MEMBER SCHULTZ: I think you've
16 kind of covered this, but just to recap for myself
17 maybe, absent this merger the Board would not have
18 jurisdiction to look at the transparency or rate
19 reasonableness of the rates in another country, but
20 BN is seeking a condition and I guess the question I
21 have is if the Board would approve your condition
22 what effect would that have on any other movements

1 that would go across a border, either Canada or
2 Mexico?

3 MR. DENTON: What we're asking for,
4 Member Schultz, is a mechanism to enforce what
5 Applicants have already said they're going to do,
6 which is to maintain an open gateway at the border
7 crossing here. So, what Applicants have already made
8 this an issue in the case, the cross-border traffic
9 between Mexico and the U.S. What we're asking for is
10 Applicants to put in place something that actually
11 allows that to be a real promise, that allows this to
12 actually be implemented in a useable way.

13 We're not asking you to extend your
14 jurisdiction anywhere across Mexican borders that's
15 not appropriate. What we're asking you to do is to
16 allow the promise that Applicants have made to be
17 realized.

18 BOARD MEMBER SCHULTZ: And of course,
19 absent this merger, you would not be in a position to
20 be seeking that level of transparency. Correct?

21 MR. DENTON: I think there's been some
22 confusion over the course of the hearing between rate

1 reasonableness proceedings and merger condition
2 proceedings. I think in a merger proceeding this is
3 an entirely appropriate mechanism, the open gateway
4 between two countries, right?

5 Outside of the context of a merger, as
6 Mr. Nober talked about, there would be no way for us
7 to get into the Mexico side of these rates,
8 particularly if it's a Rule 11 rate between a
9 Mexican origination or destination and the Laredo border.

10 BOARD MEMBER SCHULTZ: Thanks.

11 CHAIRMAN OBERMAN: All right. I don't
12 think there are any more questions at this point.
13 Were you ready to move to Dr. Reishus' presentation?

14 MR. DENTON: We are, yes.

15 CHAIRMAN OBERMAN: Okay.

16 DR. REISHUS: Good morning. My name is
17 David Reishus. I'm an economist retained by BNSF to
18 analyze potential competitive issues in this merger.
19 I've worked on competition and regulatory issues in
20 the rail industry for over 25 years.

21 Following the acquisition of Tex-Mex by
22 KCS, BNFS has no longer been able to compete

1 successfully for traffic over the Laredo Gateway. As
2 the graph you've seen shows, following the Tex-Mex
3 merger, BNFS's carload traffic over the Laredo
4 Gateway began falling.

5 This is a collapse from which BNSF and
6 its shippers have never recovered, but this is not
7 the only evidence of competitor exclusion at Laredo by
8 KCS. Using KCS's data available in this proceeding,
9 I show that where UP and BNFS can actually
10 compete with KCS for traffic over Laredo and traffic
11 for which KCS has the incentive and the ability to
12 exclude interline competition, UP and BNSF have
13 been effectively precluded from obtaining that
14 traffic. I urge the Board members to review this
15 highly confidential evidence in Sections 4B and
16 Appendix B of my initial verified statement.

17 You've heard that while BNSF has lost
18 traffic over Laredo, they have grown it over Eagle
19 Pass. As explained by Mr. Hirsch, this reflects new
20 traffic to mostly new markets served by FXE, not a
21 substitute for lost business over Laredo to KCSM
22 served customers. More than seven years elapsed

1 between the time that BNSF grain business was mostly
2 lost at Laredo and that BNSF developed its new grain
3 business over Eagle Pass and you can see this is the
4 report of BNSF's agriculture expert, Professor
5 Wilson, in his first verified statement in
6 confidential Figures 11 and 12.

7 Most of this traffic goes to destinations
8 not served by KCSM and effectively none goes to
9 KCSM's sole-served customers. The one Mexico market
10 theory promoted Wednesday by CP/KCS in this
11 proceeding is wrong. Rather BNSF growth in traffic
12 over Eagle Pass with FXE shows that where BNFS is
13 given the opportunity it is able to compete for
14 business in Mexican markets using interline
15 service.

16 After the merger, the combined CP/KCS
17 will have the same ability and incentive as KCS now
18 has to exclude interline competition over the
19 Laredo Gateway. But CP/KCS will have a far greater
20 geographic and economic scope by which to do this.
21 CP has five times the traffic north of Mexico that
22 KCS has. And as Mr. Hirsch pointed out, two-thirds of

1 the additional CP/KCS traffic from the merger is over
2 the Laredo Gateway.

3 CP/KCS emphasized the benefits of the
4 merger to Canadian and CP-served grain shippers. The
5 traffic from the Midwest would be disadvantaged by
6 exclusionary behavior of CP/KCS at Laredo. BNSF's
7 agricultural expert, Professor Wilson, showed U.S.
8 Midwest grain shippers not located on CP/KCS would be
9 most likely to suffer.

10 Mr. Nober explained yesterday the
11 mechanics of how a gateway can be commercially closed
12 and how shippers can be harmed. I will not repeat
13 his full explanation, but I would like to highlight
14 certain economic issues, so I'm skipping forward to a
15 slide Mr. Nober used yesterday, Slide 49.

16 On the left, the independent Mexican
17 railroad was charging \$400 for its portion of the
18 move before the merger. On the right, immediately
19 after the merger, the Mexican railroad is now owned
20 by Carrier A, but none of the rates have changed.
21 So, Mr. Nober explained the mechanics of how the
22 merged carrier can raise the rates to Carrier B to

1 the point that it can't compete with Carrier A. So,
2 if you'll flip ahead a couple more slides, you'll see
3 how this happens. Carrier A is able to raise the
4 rates in Mexico to both itself and to Carrier B.

5 So, in this example, Carrier A, by
6 changing the rates in Mexico, is able to make it so
7 that Carrier B is unable to effectively compete for
8 the traffic and this would be true even if Carrier B
9 was able to reduce its rates somewhat in response to
10 the change in rates in Mexico.

11 And by eliminating effective competition
12 from the interline carrier -- yes.

13 CHAIRMAN OBERMAN: Let me just ask you
14 this question. Is it the contention of this slide
15 Carrier B can't afford to go down to \$300.

16 DR. REISHUS: Yes.

17 CHAIRMAN OBERMAN: That would be a
18 money-losing proposition?

19 DR. REISHUS: Yes. We're saying perhaps even
20 if Carrier B were able to go down some, it couldn't
21 go all the way down to \$300.

22 CHAIRMAN OBERMAN: Yes. One of the

1 reasons I asked that is this constant battle of the
2 OR and are we being limited by trying to hold onto a
3 57 OR. In other words, if they went down to \$300
4 might they be at a 70 OR and still make some money or
5 how do we know that from your slide or from any
6 evidence you have?

7 DR. REISHUS: Well, I can go further, but
8 the basic fundamental rationale for why there's no
9 risk of foreclosure of a gateway, as Mr. Meyer said,
10 is the one lump theory and the one lump theory is
11 basically you've already driven down the railroads to
12 the lowest level they're able to take, whether that's
13 100 percent -- whether that's actually variable costs
14 or 120 percent of measured variable cost I don't
15 precisely what the incremental calculation of cost
16 for a railroad on a particular movement would be, but
17 the point is you've already driven it down to the
18 lowest possible level that a railroad could accept.

19 CHAIRMAN OBERMAN: In order to accept
20 this analysis then does that mean we have to accept
21 the one lump theory or else it doesn't work?

22 DR. REISHUS: I think in order to accept

1 the basic presumption put forward by CP/KCS that
2 there's no risk of harm in a gateway I do think
3 they're asking you to accept that presumption.

4 CHAIRMAN OBERMAN: All right. Go ahead,
5 proceed.

6 DR. REISHUS: Okay. The point is that
7 even if Carrier B is able to reduce its rates some it
8 may not be able to take it down to 300. And by
9 eliminating competition from the interline
10 carrier, shippers may face higher rates from the
11 merged carrier and shippers are effectively paying
12 more as a result of this behavior.

13 BOARD MEMBER FUCHS: Doctor, this may be
14 a good place to resume and I want you to get through
15 your whole presentation, so I want to do everything
16 now. I appreciate it. But the presumption of this
17 slide is that CP/KC has the market power to go up to
18 \$1100.

19 DR. REISHUS: Yes.

20 BOARD MEMBER FUCHS: Okay. And in your
21 verified statement you said there were a number of
22 types of traffic that you doubted that CP/KCP would

1 have market power.

2 DR. REISHUS: I'm not sure I said that.

3 BOARD MEMBER FUCHS: For auto and intermodal
4 what was your contention about CP/KCP's market power?

5 DR. REISHUS: The auto and intermodal
6 traffic, the intermodal traffic that you see, KCS has
7 very little intermodal franchise in the U.S. It
8 doesn't get very far, Kansas City, Dallas, Jackson,
9 so most of the intermodal traffic that's going over
10 Laredo is traffic that KCS can't really effectively
11 foreclose. That's my point, not the degree of
12 competitiveness of that traffic.

13 BOARD MEMBER FUCHS: But you agree with
14 the general proposition that the theory sort of
15 breaks down if CP/KC, understanding you might say
16 CP/KC after the merger has more opportunities, has
17 more market power, but this could not happen on
18 competitive traffic.

19 DR. REISHUS: I think the distinction
20 between competitive and noncompetitive traffic is a
21 degree of how much market power does a railroad have
22 and what is the levels to which a railroad has the

1 ability to raise rates. I don't think it's a zero,
2 one sort of --

3 BOARD MEMBER FUCHS: Totally agree. But
4 you would say that there is some traffic that has --
5 is closer to the one in terms of competitive traffic.

6 DR. REISHUS: Clearly, there's traffic
7 that the railroads have more power over than others.

8 BOARD MEMBER FUCHS: And I guess what I'm
9 struggling with and what we'll get into in the prop rate
10 mechanism, so we'll prop rate later, but what I'd
11 like you to think about when you're preparing on prop
12 rate is for the traffic that's closer to one,
13 competitive traffic, when you impose -- so they can't
14 do what you're describing, but yet, we're going to be
15 dividing the rate up according to mileage and instead
16 of according to what parties would negotiate in a
17 competitive market and whether or not that
18 effectively, for competitive traffic, effectively
19 subsidizes BN. In other words, what I'd like
20 you to address when discussing the prop rate
21 mechanism is whether or not you feel prop rate is an
22 appropriate economic methodology for traffic that is

1 on the higher end of the competitive scale.

2 MR. DENTON: David, if I could just
3 briefly. So one thing that we've done with our prop
4 rate mechanism is give you a very simple maximalist
5 look at what this would look like. And what we've
6 said in our papers is that we are absolutely willing
7 to talk about nibbling around edges here and even
8 more significantly than that, just talking with
9 Applicants about what works. Is there a particular
10 commodity where this might not work, is there a
11 particular destination where this might not work.

12 MR. NOBER: And also, if I might, I
13 mean, again, we gave an illustration because it's a
14 complicated concept and we wanted to be able to just
15 talk it through, which we did successfully. You guys
16 clearly understand it. At the same time, there are a
17 lot of ways, and think we've opened -- we didn't want
18 to present and say we're only open to one method of
19 establishing and structuring a prop rate. It could
20 be weighted more of it toward Mexico.

21 The point is to come up with something
22 that's transparent and equalizes the two sides and

1 doesn't leave us at the competitive disadvantage, so
2 I wouldn't say that it's this mileage proportionate rate
3 the way we've put it in the simple example or
4 nothing. So, I think that we could work out
5 something if there were direction to look at that.

6 BOARD MEMBER FUCHS: And I would just
7 make two points with that and then I'll let you
8 continue your presentation. First is, Peter -- Mr.
9 Denton, you mentioned nibbling around the edges. I
10 didn't see a really comprehensive analysis of market
11 power of CP/KC on an origin to destination pair basis.
12 It would be extraordinarily difficult for you all to
13 submit that, but I'm saying that there is no evidence
14 in the record about how much we're nibbling and how
15 big are the edges -- not a lot of evidence. But the
16 other thing I would say is I appreciate, especially
17 from the Board's perspective of rate setting, there
18 are always simplifications that need to be made that
19 aren't going to capture perfectly. I just think we
20 need to be transparent about what the
21 simplifications are. If it is the case that, yes,
22 we're going to have to divide up revenues on

1 competitive traffic and yes, that might mean
2 sometimes we have to subsidize BN, but there's no
3 really better way to do this, I think we have to be
4 transparent and straightforward that that's what's
5 going on here.

6 MR. NOBER: We might quibble with the
7 characterization of subsidizing BN because the other
8 extreme -- there's no way --

9 BOARD MEMBER FUCHS: Understood. And
10 there could be situations where the prop rate
11 mechanism is actually of no effective relief because
12 it's oversimplified. So, I didn't mean to say it one
13 way, but of course, you all are before us, so I'm
14 going to say it in a way that you're going to have to
15 respond to.

16 MR. NOBER: What it ultimately is, is
17 it gives the customer more options. So, rather than
18 subsidize us, it gives the customer more competitors
19 in the marketplace.

20 MR. DENTON: Member Fuchs, I would just
21 say that I know Dr. Reishus is going to get into this
22 in his statement.

1 BOARD MEMBER FUCHS: Okay.

2 DR. REISHUS: Notice that in this
3 vertical merger across a gateway here the shipper and
4 the competing interline carrier are both harmed by
5 the anti-competitive rate increase by the merged
6 carrier. Their interests are aligned in preserving
7 competition. This stands in contrast to a horizontal
8 merger where the effects of a merger on customers and
9 the remaining competitors are typically in
10 opposition.

11 CP/KCS argued in its opening that shipper
12 rates couldn't go up following the merger and that
13 competition cannot be harmed. This is based on two
14 assumptions. The first assumption is the rate the
15 shipper pays is already as high as it can be. If the
16 railroad raised rates, it would lose more business
17 than any additional profit could be earned and I
18 think this addresses to some part, the point
19 Commissioner Fuchs made.

20 The second assumption is that the independent
21 Mexican carrier has already obtained all of the
22 profit available from the movement, that the Mexican

1 carrier collected, in the language of Dr. Majure, the
2 full return of its market power. This is the one
3 lump theory referenced by Mr. Meyer on Wednesday.

4 Under this assumption, the Mexican
5 carrier has caused the two railroads in the U.S. to
6 compete so hard that one or both of these railroads
7 would be unable or unwilling to reduce their rates to
8 less than \$600, that's the number shown on the slide,
9 and they would still be able to carry the traffic.

10 As I showed in my initial statement,
11 these assumptions are inconsistent with Mexican
12 regulation. Similarly, UP's expert, Professor Salop
13 and I have shown why the merger almost certainly
14 enhances the ability of the merged railroads to raise
15 rates. It is inconsistent with existing regulation
16 and economics to believe that the Mexican carrier had
17 collected the full return from the move and has
18 driven down rates in the U.S. to a level so that the
19 two railroads could never go lower in the U.S.

20 As a final note, nondiscriminatory rates
21 do not resolve the problem of a loss of gateway
22 competition. Even where the same rates are charged

1 by Carrier A for the movement in Mexico to itself
2 and to the competing Carrier B, the merged carrier
3 has the ability to establish rates that harms
4 competition shippers. I'd also point out that
5 transparency of that rate alone is also insufficient
6 to preserve competition.

7 So, I now want to turn to talk about the
8 potential solution to this issue. Shipper
9 organizations, UP and BNSF have all proposed similar
10 solutions to resolve the potential loss of
11 competition for traffic over gateways. These
12 proposals share a common characteristic. The rate
13 charged by the merged CP/KCS for an interline
14 movement to the gateway is determined by prorating
15 by mileage a CP/KCS total rate over that gateway and
16 Mr. Nober explained yesterday how that works.

17 Forty percent of the CP/KCS miles are in
18 Mexico, the proportional rate on the Mexican portion
19 across the gateway is 40 percent of the full rate of
20 \$1,000 or \$400. This gives a dollar per mile rate in
21 Mexico, \$400 is the resulting prop rate available
22 to a connecting carrier for movements over the

1 gateway, which is the rate available by which the
2 competing interline carrier can attempt to compete
3 for this traffic.

4 CP/KCS criticized proportional rates
5 proposals as discouraging rate competition and being
6 anti-competitive and consistently referred to these
7 as UP and BNSF proposals, but major shipper
8 organizations, including NIT League, the American
9 Chemistry Council, and the Fertilizer Institute also
10 support application of a prop rate mechanism to
11 resolve their concerns regarding vertical
12 foreclosure as a result of the merger.

13 Consistent with the economics of a loss
14 of competition across gateways, the interests in
15 shippers and competitors may be aligned. A prop rate
16 mechanism continues to provide the integrated,
17 single-line carrier the incentive to compete for
18 traffic. And let me briefly walk through this, so on
19 Slide 62, similar to before, assume that the
20 interline carrier is just able to compete for the
21 traffic with Carrier A using a \$400 prop rate for the
22 Mexico portion of the move.

1 This is Slide 62. So, similar to before,
2 Carriers A and B are just able to compete for the
3 traffic using the \$400 prop rate. In this case,
4 let's also assume following the merger, now on Slide
5 63, Carrier A is able to achieve some of the
6 efficiencies from the merger and is able to lower its
7 rate and the rate that Carrier B can charge.

8 This will lower the prop rate that
9 Carrier B can obtain for the Mexico portion of the
10 move from \$400 to \$320, but -- this is important --
11 unless Carrier B can match the rate cut from Carrier
12 A, Carrier A will successfully compete for it and win
13 the traffic as a result of its new lower rate.
14 Carrier A retains the incentive to compete on rates
15 or else it loses the business.

16 CP/KCS's economist, Dr. Majure, argued
17 that a proportional rate mechanism is
18 anticompetitive. This argument and conclusion are
19 subject to two important flaws. CP/KCS starts with
20 a world in which there are no possible competitive
21 problems to be resolved. In Dr. Majure's world there
22 is no need for any sort of fix or constraint on

1 CP/KCS's behavior at the gateway. There would be no
2 need for a commitment to maintain open gateways or
3 commercially competitive rates regardless of how
4 squishy that definition is.

5 In this world, CP/KCS would always do the
6 right thing and any change that alters CP/KCS's
7 decisions would be anticompetitive. But as we've
8 laid out today, that is not the world we're dealing
9 with. The approach in the specific example used by
10 Dr. Majure also assumes that competitors do not
11 compete for traffic. In his example, CP/KCS would
12 raise rates under a proportional rate agreement in
13 order to maintain its profits constant, but his
14 example assumes that railroads are not competing for
15 traffic. Instead of matching CP/KCS's higher rates
16 as Dr. Majure assumed, the competing railroad has the
17 incentive to beat the CP/KCS rate and steal the
18 traffic. That effect is the flip side of what is
19 shown in the slide on the screen. In the slide,
20 CP/KCS -- Carrier A -- wins the business by lowering rates.
21 If, instead, it were to raise its rates the competing
22 Carrier B would win the traffic.

1 Now, I want to turn briefly to BNFS's
2 proposed solution and the specific BNSF prop rate
3 solution is based on the so-called I-5 Agreement
4 between BNSF and UP that was imposed as part of the
5 UP/SP merger. Mr. Nober explained the history of the
6 I-5 agreement. The I-5 Agreement has been in effect
7 and successfully implemented for over 25 years with
8 roughly 25,000 carloads per year moving under the
9 agreement.

10 Under the I-5 Agreement, BNSF over the
11 Portland Gateway is in the role that CP/KCS would be
12 in under BNSF's prop rate proposal for Laredo. I
13 outlined in my reply verified statement how this
14 approach could work based on the I-5 Agreement. In
15 short, it uses an average of actual CP/KCS rates to
16 establish a per mile prop rate south of the Laredo
17 Gateway that can be used by UP and BNSF for
18 interline traffic over the Laredo Gateway.

19 This prop rate is derived from rates
20 negotiated in the marketplace for traffic that
21 actually moves. It varies by commodity, direction,
22 region, car type, and other characteristics the

1 railroads found to be relevant. The BNSF prop rate
2 proposal is pro-competitive. It keeps the Laredo
3 Gateway open using market-determined rates actually
4 paid by shippers, provides incentives for CP/KCS and
5 interline carriers to compete for shipper traffic,
6 it preserves confidentiality of shipper information,
7 and it accounts for differences in rates across
8 traffic types, and it adjusts automatically to
9 changes in market conditions.

10 The fundamentals of this approach is the
11 opposite of rigid. The interline rate for traffic
12 over Laredo adjusts quarterly to recent changes in actual
13 market conditions specific to different commodities,
14 regions, and other characteristics. Importantly, as
15 Mr. Denton emphasized, the BNSF proposal is intended
16 to be a starting point by which the railroads
17 negotiate the specific terms of the mechanism.

18 Within the framework, these terms can
19 account for economic and other issues specific to
20 Mexico traffic over the Laredo Gateway. The specific
21 implementation, like the choices embodied in the I-5
22 Agreement, can decide upon the characteristics, for

1 example, definition of commodities and regions, train
2 size, et cetera that establish what markets are
3 averaged together to determine the applicable prop rate.

4 It is also flexible enough to account for
5 differences in cost between Mexico and the U.S. if
6 those were found to be significant contributors to
7 different levels of rates in the U.S. and Mexico.
8 Likewise, for relatively minor adjustments to
9 formulas, the pure mileage-based rate can be adjusted
10 for differences between short-haul and long-haul
11 portions of a move. These adaptations can account
12 for the issues emphasized by Dr. Majure in CP/KCS's
13 opening and findings in his second report at Figures 7
14 and 8 regarding the length of haul.

15 I would point out that these concerns
16 over prop rates and short hauls apply equally to BNSF
17 as you can see in Dr. Majure's figure. BNSF is often
18 the short haul partner across the Portland Gateway
19 between Washington State and Vancouver with UP
20 locations in California and the U.S. Southwest.

21 These issues have not prevented the I-5
22 Agreement from being effective in preserving

1 competition across the gateway or leading to
2 unacceptable tensions in this long-running agreement.
3 In short, the I-5 Agreement framework provides the
4 flexibility to establish commercially competitive
5 market responsive rates across the gateway in an
6 automatic and durable manner.

7 Now, I'd like to turn to something
8 completely different, something you heard quite a bit
9 about yesterday, the issue of the threat of
10 congestion and service disruption across the Houston
11 Complex from the merger. I'll be quick about this.

12 From an economic perspective, this threat
13 of congestion raises two important and related
14 issues. First, congestion and service disruptions in
15 the shared Houston Complex caused by the CP/KCS
16 merger raises rivals costs, costs incurred by BNSF
17 and UP and their shippers. If Houston becomes
18 congested as a result of merger-induced traffic
19 changes, costs of service delays and service
20 degradation is imposed on shippers using the
21 third-party railroads.

22 Moreover, if additional capital or

1 operational costs are required to alleviate
2 congestion problems caused by the merger, it risks
3 imposing these additional costs on third-party
4 railroads, UP and BNSF. Second, CP/KCS in its
5 decision-making does not fully account for the costs
6 it imposes on others from the merger. CP/KCS gains
7 the full benefit of the merger while shifting costs
8 onto others.

9 CP/KCS has the full incentive to make
10 investments to alleviate congestion on its own tracks
11 and its own shippers, but it lacks the proper
12 incentives to pay to alleviate the congestion the
13 additional traffic causes in the shared Houston area.

14 Economic efficiency and good merger
15 policy calls for CP/KCS to internalize this cost
16 rather than shift them to other railroads and their
17 customers. In short, CP/KCS should incur the costs
18 to receive the benefits of the merger and not shift
19 them on to its competitors and their shippers. And
20 I'm open for questions and otherwise will transfer it
21 back to Peter Denton.

22 CHAIRMAN OBERMAN: Just on this last

1 issue, just a question without getting into the
2 substance. I look a look at the arguments over the
3 striking of the RTC study, did not look at the
4 study, but from the way it was briefed I gathered,
5 and I think I asked this yesterday, but I have a
6 little clearer picture, that the RTC study dealt with
7 conclusions about congestion, but did not propose a
8 specific infrastructure that would alleviate that
9 congestion; is that right?

10 MR. GABRIEL: That's correct. We felt we
11 were lacking some necessary inputs. We only had the
12 inputs from us and Union Pacific. We did not have
13 anything in terms of the merger volume itself, so we
14 didn't feel like it was correct to recommend
15 solutions. We'd like those necessary inputs as part
16 of the outcome of this hearing.

17 MR. DENTON: And just to clarify briefly,
18 we did add the eight additional KCS trains as part of
19 the model, but the other details that Mr. Gabriel was
20 just referencing.

21 CHAIRMAN OBERMAN: Did you ask for that
22 in discovery earlier on in the proceeding? Did you

1 ask for the other inputs that you would've needed to
2 do a study earlier in the proceeding?

3 MR. DENTON: We had a long list of
4 discovery questions. I can't speak to whether each
5 one of those was met or not.

6 CHAIRMAN OBERMAN: Well, if they weren't
7 met and you felt you needed it to do your job, you
8 could've come and asked for it. I don't recall. I
9 don't recall the record enough. One of the reasons I
10 asked the question you know, I have expressed my view in other
11 proceedings, particularly the Gulf Coast proceeding, that
12 regardless of how the litigants litigate the matter,
13 and this is not a hearing on the record, but it is --
14 appears to be a contested matter, we have an
15 obligation to protect the public interest.

16 And what I am frustrated about at this
17 point is that if we accept your concerns about
18 congestion in Houston, even if I looked at your RTC
19 study, I wouldn't have any idea how to solve that
20 problem from anything that's in that study, right?

21 MR. DENTON: Sure.

22 CHAIRMAN OBERMAN: So, we're still in the

1 dark on that question.

2 MR. DENTON: The study identifies the
3 issue, right? And we freely admitted when we
4 submitted the study that there were additional inputs
5 that we need. It showed the need for collaboration
6 and discussion between the three railroads.

7 CHAIRMAN OBERMAN: That I understand.
8 But in my newfound role as an RTC expert, based on
9 everything I heard in the Gulf Coast hearing, you
10 could judge for yourself just how much anybody could
11 become an expert after that hearing, I know that RTC
12 studies say, well, if you put this siding here then
13 the times are better and it gives you an argument to
14 say, yes, this piece of infrastructure is needed.
15 Your study didn't get that far.

16 MR. DENTON: Correct.

17 CHAIRMAN OBERMAN: That's all I was
18 trying to get at. I have a couple of questions going
19 back to this prop rate model. One question I had
20 going back to just a follow up, but when I'd asked
21 about not bringing a rate case when the Robstown
22 segment rate was doubled at the point where the bar

1 chart dropped, did any of the shippers whose
2 freight you were carrying prior to that time -- I
3 assume the point came when KCS doubled the rate and
4 the shippers came to you. You said, well, we have to
5 raise your rates because our rate was just doubled by
6 KCS. Did any of those shippers come to you and say,
7 well, we've got to go in and challenge this. We
8 wanted to stay with BN?

9 MR. HIRSCH: I wasn't there at the time,
10 so I don't know. But what we're showing there is
11 the fact that that rate increases to us it doesn't
12 mean that KCS will have to do the same thing, right?
13 So, they were able to compete. So, if I'm the
14 shipper or the receiver, I may still be able to
15 receiving the same rate I was paying to BNSF, but now
16 I'm paying to KCS, so I'm still getting greater
17 service at the same rate I was paying before but all
18 that freight that was moving on BNSF now move to KCS.

19 CHAIRMAN OBERMAN: You lost me. If KCS
20 is charging the same rate as you were charging, why'd
21 you lose the business?

22 MR. HIRSCH: Because they can manipulate

1 the Mexico side and the U.S. side, as we show in the
2 chart. They can raise and kept that \$1,000 in the
3 example, but on our side it was 1300. We couldn't
4 compete.

5 CHAIRMAN OBERMAN: That's what I'm saying --
6 that overall the interline rate was not the same.
7 It went to 1300 on the example.

8 MR. HIRSCH: Correct.

9 CHAIRMAN OBERMAN: So, your customers
10 said we can go with KCS for a thousand. We can't
11 afford to go with you for 1300. Did any of those
12 customers say we like BN service? We think the 1300
13 is challengeable, let's work on it. Did that happen?
14 I mean, Roger, you said you weren't sure you had
15 standing. I don't opine on that.

16 MR. NOBER: This is going back to 2006
17 and '07, so I just don't know that we could answer
18 that for you.

19 CHAIRMAN OBERMAN: Yeah. But it
20 continued right up to the present date.

21 MR. NOBER: We also can't speak for the
22 shippers.

1 CHAIRMAN OBERMAN: No, I'm asking if they
2 came to you. I'm not asking you to guess.

3 MR. NOBER: We don't know. I mean I
4 don't know that we can answer the question the way
5 you posed it.

6 CHAIRMAN OBERMAN: Well, what do you mean?
7 Pose it a different way?

8 MR. NOBER: Which is to say, did shippers
9 come to -- you asked are we aware of shippers
10 coming to us and saying I'd like to challenge this
11 rate? In the abstract, we're not aware, but we
12 don't know because we weren't there and Paul wasn't
13 there at the time, so I don't know how we can -- we
14 just can't answer that.

15 CHAIRMAN OBERMAN: Well, if the BN
16 service was great, I accept that it was, you would
17 think your customers would be unhappy about being
18 shunted over to somebody else, particularly if they
19 had to stop at Kansas City, so something seems to be
20 missing.

21 Let me ask another -- yeah, go ahead.

22 BOARD MEMBER FUCHS: In discovery, do I

1 read the record correct to stay that BN was unable to
2 produce any discussion between it and a shipper for
3 shipper inquiring about why their rates went up
4 because of Laredo issues? Was there any shipper --
5 and maybe that's posing it a little different way,
6 but I think it's the same question as Marty.

7 MR. DENTON: Yes. And the converse is
8 also true, that we asked KCS for information about
9 their rate setting during this time and they were
10 unable to show us anything. They were also unable to
11 show us any manuals, any discussion about how they
12 set rates in Mexico. They have nothing on the record
13 that establishes that.

14 BOARD MEMBER FUCHS: No. But I mean you
15 all having the burden in this are alleging that
16 they're raising the rates on shippers and what I
17 think shippers would care about is what their
18 overall rate is, right? I understand you all care
19 about is what your proportion is, but for shippers
20 and the overall rate nobody came to you during this
21 massive shift and said my overall rate has gone up.
22 Why is that, BNSF? And you said, well, it's KCS.

1 There's no dialogue like that over 17 years?

2 MR. DENTON: We don't have that. No.

3 BOARD MEMBER SCHULTZ: Just one more
4 question, did any of the shippers avail themselves of
5 the option of arbitration as well?

6 MR. DENTON: Again, we can't speak for
7 the shippers, but we are not aware of that.

8 CHAIRMAN OBERMAN: All right, I want to
9 go back to one more matter and then if we could go
10 back to Slide 53. So, this is the foreclosure slide,
11 right?

12 MR. DENTON: This sums up the foreclosure
13 issue. Yes.

14 CHAIRMAN OBERMAN: Right. So, let's
15 assume that this conduct on the right half of this
16 with the big red "X" happened. Sounds like it did
17 happen. Would that conduct by KCS at the time it did
18 this, and let's assume the increase to \$700 for both
19 carriers for the Mexican portion, would this violate
20 anything that could be considered commercially
21 reasonable, this conduct?

22 MR. DENTON: Yes, I believe so. I mean I

1 think we could try to establish that. Again, the
2 Applicants themselves describe the standard as
3 squishy and without much detail, but I think if we
4 were able to go through what frankly would be a
5 pretty long Board proceeding and get discovery and
6 a couple years later come out with a conclusion,
7 I think that's right.

8 CHAIRMAN OBERMAN: Well, it's not a rate
9 case. I don't know that it takes two years. I don't
10 know how long it takes, but we get a lot of requests
11 for conditions and there's been a lot of argument
12 about how many times we've put commercially
13 reasonable into a merger condition and you're kinda
14 telling me it's all a waste of time. And the way I
15 see it, it certainly appears to be -- I'm not opining
16 because a case may come to us -- that if this kind
17 of manipulation is going on, on page 53, however
18 squishy the overall standard, this case fits and I'm
19 at a loss about if we're trying to look at
20 comparative solutions to preserve competition why
21 this wouldn't do it because it does strike me, Peter,
22 that yes, it may be time-consuming to bring one case

1 and I think that would pretty much end the discussion
2 because you're talking about not only getting the
3 rates right, you're talking about damages and you're
4 talking about gateways all over the country.

5 MR. DENTON: Right.

6 CHAIRMAN OBERMAN: And I'm not aware of
7 any cases that have ever come here under these kinds
8 of provisions. Maybe there have been before my time.

9 MR. DENTON: I think that's fair. Yes.

10 CHAIRMAN OBERMAN: But you're trying to
11 demonstrate what's wrong with this procedure and it
12 sure doesn't meet commercially reasonable as I see
13 it.

14 MR. NOBER: I would just add one
15 amendment to what you said, Mr. Chairman, which is
16 that commercially reasonable gateways are typically
17 in U.S. gateways and I think we've hopefully been
18 able to convince you that there is something that is
19 different about Mexico. So, I don't know that we
20 would agree that imposing a commercially reasonable
21 gateway between two interchanges of U.S. carriers
22 would be the way you've characterized it, but we do

1 think for Mexico it is for some of the reasons we've
2 talked about.

3 CHAIRMAN OBERMAN: Well, we're not
4 finished yet with our discussion about gateways.
5 We're just talking about Mexico.

6 MR. NOBER: Yes. Well, we're here to
7 talk about Mexico.

8 CHAIRMAN OBERMAN: No, I know, but we are
9 going to have a little broader discussion, but I
10 wanted to finish this point. Peter, you wanted to
11 make a conclusion.

12 MR. DENTON: A conclusion, yes,
13 absolutely. Thank you. So, you've heard a lot from
14 us over the course of the last, I guess, two days
15 now. I just want to spend a moment kind of
16 summarizing where we are.

17 So, BNSF believes that end-to-end mergers
18 such as the transaction proposed here are usually
19 pro-competitive and benefit the railroad industry and
20 the public. What you've heard from the last two days
21 from us and our witnesses is that
22 Applicants have entirely failed to address two key

1 facts that distinguish this merger from other
2 end-to-end mergers.

3 Frankly, we would prefer not to be here
4 asking the Board to do what most parties seeking
5 merger approval from this agency have done on their
6 own over the last quarter century, collaborate with
7 stakeholders to address valid merger-related
8 concerns. The first unique issue is that a combined
9 CP/KCS will have the ability and incentive to
10 dominate the critical Laredo Gateway and border
11 crossing by manipulating rates in Mexico and forcing
12 traffic on to their less efficient route that runs
13 directly through downtown Houston.

14 Mr. Hirsch and Dr. Reishus explained that
15 BNSF currently struggles to compete at the Laredo
16 border crossing due to KCS practices and that in the
17 future freezing out competitors at the Laredo border
18 crossing would result in higher costs and worse
19 service for shippers. It would also drive shippers
20 to move their freight from rail to trucks.

21 Access to alternative Mexican gateways
22 like Eagle Pass are not a substitute for Laredo

1 because of the key markets that are accessed only
2 from Laredo. In order to adequately address the
3 issue, this Board must require Applicants to
4 negotiate with connecting carriers to create a
5 market-based, proportional rate remedy and service
6 assurances in order to maintain an open gateway at
7 Laredo, thereby preserving effective interline
8 competition over this critical interchange point.

9 Now, CP itself told this Board in 2003 in
10 the KCS/Tex-Mex proceeding in arguing for enhanced
11 gateway protection that the future competitive
12 viability of interline routes connecting Mexico to
13 the rest of the North American continent via Laredo
14 is simply too important to be left to chance. CP's
15 position was right then and it's the right position
16 now.

17 The second unique issue is that a
18 critical link of the KCS network consists of trackage
19 rights over lines in the Houston area owned by other
20 railroads, largely, UP and used by UP, BNSF, and
21 others.

22 Now, Applicants have the burden of

1 establishing that their operating plan will work,
2 using existing infrastructure or identifying whether
3 additional capacity is necessary. On shared lines in
4 Texas, Applicants simply did not meet that burden.
5 Applicants paid a lot of attention to Chicago, but
6 they failed to do the same for Houston.

7 Now, the reason seems obvious.
8 Applicants have told you that CP/KCS would not be
9 responsible for the cost of any projects on UP lines
10 needed to accommodate their merger traffic, aside
11 from their annual rental payments to UP. They've also
12 told you that CP/KCS could be directly responsible
13 for the cost of projects on UP lines that CP/KCS
14 itself proposes.

15 BNSF has a different arrangement with UP.
16 We would be directly responsible for the cost of
17 CP/KCS's merger projects based on how much BNSF uses
18 the line. If the Board does not intervene here,
19 Applicants by not identifying any projects on these
20 UP lines or even conducting a formal study would
21 successfully externalize the costs of their merger
22 onto their key competitors, UP, BNSF, and their

1 customers.

2 The Board can fix this by requiring
3 Applicants to coordinate with all stakeholders in the
4 Houston area, including local governments and other
5 railroads that share use of the CP/KC route, to study
6 and identify the impact of CP/KC's increased traffic
7 levels and necessary infrastructure improvements.

8 The Board should not let CP/KCS increase
9 KCS traffic levels on shared lines in Texas if such
10 increases would displace existing traffic or
11 compromise fluidity until necessary capital
12 improvements are identified, fully funded by
13 Applicants, and implemented.

14 Specifically, the Board should require
15 Applicants to fully fund any capital improvements
16 that would not be required but for increased CP/KCS
17 traffic on lines where KCS is a tenant. BNSF stands
18 ready to cooperate with Applicants and UP to
19 undertake an RTC study of the shared lines and to
20 inform the Board and parties of any improvements that
21 are necessary to handle Applicants' merger traffic.

22 Both of these proposed remedies are

1 flexible and can be addressed as conditions to be
2 fulfilled after the merger decision is delivered by
3 the Board. The collaboration BNSF is asking for
4 does not require the Board to delay its processes or
5 to undertake additional work before its statutory
6 deadlines.

7 And with that, I thank you all for your
8 time and we're happy to take any final questions.

9 (Pause)

10 BOARD MEMBER HEDLUND: Something that was
11 said yesterday, you're proposing that we could impose
12 a condition with respect to Houston which would have
13 an economic impact on CP/KCS, but one that they would
14 not know until sometime later?

15 MR. DENTON: I'm not sure I would
16 characterize it that way. What I would say is that
17 we're asking for CP/KCS --

18 BOARD MEMBER HEDLUND: Well, you're
19 saying that you don't want us to delay a decision
20 until we know what the infrastructure is that's being
21 proposed, and we determine that that's something that
22 should be built. I think you're saying that this

1 should be, essentially, a condition subsequent but
2 that we would give the approval and then sometime
3 later there would be some agreement as to what
4 infrastructure needs to be built, but at that time
5 the bread's baked.

6 MR. DENTON: Well, the bread is already
7 baked, to be clear.

8 BOARD MEMBER HEDLUND: Well, yes.

9 MR. DENTON: I mean what we're asking for
10 is for the Applicants to have done their job, right?
11 And what we're giving you, the Board, is a way to do
12 this on a post-decision basis. And we think whatever
13 this process comes out with --

14 BOARD MEMBER HEDLUND: But we would be
15 imposing a cost on the Applicants that neither the
16 Applicants nor the Board know today what that is?

17 MR. DENTON: That cost, again, should've
18 been address by Applicants before and --

19 BOARD MEMBER HEDLUND: No, just answer my
20 question. We'd be imposing a cost on them today that
21 neither they nor the Board know what it is.

22 MR. DENTON: I suppose that's correct.

1 BOARD MEMBER HEDLUND: Thank you.

2 CHAIRMAN OBERMAN: So, I want to get back
3 to something, Roger, that you alluded to, and I know
4 it's not part of your presentation. I'm trying to
5 absorb all of this in the context of generally how
6 the regulatory system has dealt with the freight
7 network.

8 So, in this situation because of the Tex
9 -- what was the case called, Tex-Mex, Tex-Mex case at
10 that time when the Board approved the merger there
11 was not enforcement, and I don't know what the issues
12 were at the time, of a bottleneck at that
13 interchange point. In other words, the bottleneck
14 concept was out the window for that merger; is that a
15 fair way to understand it?

16 MR. NOBER: Yes -- well, it's hard to
17 say. I don't know that I would characterize it
18 exactly that way because the Tex-Mex was being
19 absorbed by the KCS, but the interchange with the
20 Tex-Mex was still an independent railroad. So, the
21 TSM South was not part of KCS at the time, so it's a
22 little bit -- it's not a perfect analogy.

1 CHAIRMAN OBERMAN: But it had aspects of
2 that, I guess, because you all had to interchange at
3 Laredo to get into Mexico.

4 MR. NOBER: Yes, you could say that.

5 CHAIRMAN OBERMAN: Yes. And there's a
6 lot of discussion, and I do want to get BN's views on
7 this in this case about places around the country in
8 terms of open gateways and so forth.

9 It appears that for purposes of this
10 merger case, and perhaps previous ones that I haven't
11 presided over, there seems to be a great urgency by
12 the non-merging railroads to make sure that they are not
13 bottlenecked out of business wherever the merger
14 might affect their interchange; is that a fair to
15 understand what's going on here? You're concerned
16 about the rate you would get even with no
17 bottleneck. You certainly wouldn't want the
18 bottleneck rule to be reinstated at Laredo.

19 MR. DENTON: This is not a rate
20 reasonableness issue and that's really where the
21 bottleneck rule and all this comes into. What we're
22 talking about is maintaining an open gateway which

1 Applicants have readily agreed to do.

2 CHAIRMAN OBERMAN: Yes. But an open
3 gateway is the opposite of the bottleneck rule by
4 definition, is it not?

5 MR. DENTON: Again, the bottleneck rule,
6 I think, is specific to rate reasonableness issues.

7 CHAIRMAN OBERMAN: No, I don't think so.
8 It has to do whether you have to quote a rate, as I
9 understand it when you're short hauling yourself, so
10 isn't that a fair way to understand what we're
11 discussing here?

12 MR. NOBER: Again, I don't know that we
13 would agree with that. I'm not sure. I think that
14 for here the way we would frame it, Mr. Chairman, is
15 that in 1996 we were given -- the Board was deciding
16 whether or not -- how to recreate competition to
17 Laredo from the SPM to UP, which was not a vertical
18 merger. It was a horizontal merger.

19 And at the time Tex-Mex was independent
20 and trackage rights to Robstown that was deemed to be
21 sufficient because the Tex-Mex was independent. I
22 don't know that I would -- I'm not sure I could

1 really characterize this particular situation with
2 respect to larger bottlenecks.

3 CHAIRMAN OBERMAN: Well, let me ask the
4 question the other way around. If open gateways are
5 a good idea in this merger, why aren't they a good
6 idea everywhere in the system?

7 MR. DENTON: Open gateways is about
8 preserving competition, right? So, the whole idea of
9 maintaining an open gateway and protecting against
10 vertical competition harm is to preserve competition,
11 which is the heart of your merger policy.

12 When you're talking about some type of an
13 open access regime or forced access regime that is
14 increasing competition. What we're talking about
15 here is there was competition, we want to maintain it
16 and preserve it going forward.

17 CHAIRMAN OBERMAN: I am going beyond
18 this, Peter, intentionally. And because, as you
19 know, I think there should be more competition, so
20 I'm not talking about in the merger context. I'm
21 talking about in terms of having a healthy rail
22 network where everybody benefits, in my view, when

1 there's more competition. Wouldn't open gateways, as
2 a rule of thumb, be a way to accomplish that based on
3 what I'm hearing here?

4 MR. DENTON: That's not what BNSF is here
5 to talk about, Mr. Chairman.

6 CHAIRMAN OBERMAN: I know it's not, but
7 I'm asking you because you're BNSF and you have a lot
8 at stake in gateways all over the country. And if
9 it's good here, why isn't it good in other places?

10 MR. DENTON: I think we are committed to
11 maintaining and preserving competition and that's
12 what our solution shows here.

13 CHAIRMAN OBERMAN: But you're not
14 committed to improving competition in other parts of
15 the country?

16 MR. DENTON: To rewriting the rail
17 network --

18 CHAIRMAN OBERMAN: Yeah.

19 MR. DENTON: -- across the entire
20 country? That's not what we're here to talk about
21 here.

22 CHAIRMAN OBERMAN: Well, I'm trying to

1 figure out where the sauce is for the goose and for
2 the gander, that's all. To me, these issues are hard
3 to separate out and say, well, on this one little
4 place competition is crucial and these all-other
5 places where competition is completely foreclosed
6 because of the bottleneck rule, so be it, because I
7 do think that what we do in these merger cases is
8 part of the overall rail policy for the country.
9 They aren't isolated, as everybody has educated me
10 since I got here, it's a network and it's a network
11 of multiple companies, not just one.

12 So, it's beginning to be blurry in my
13 mind as to where we're supposed to get tough on
14 competition and where we're supposed to let
15 monopolization just rule the day. So, if you had
16 something to say about it, I wanted to hear about it,
17 but if you want to limit it, I can't ask you to go
18 beyond your presentation -- I can ask you, but I
19 can't force you to go beyond your presentation, so I
20 won't.

21 MR. DENTON: I would just say we're here
22 today to talk about a merger and preserving

1 competition over it, a particular gateway, really a
2 narrowly tailored request and problem.

3 CHAIRMAN OBERMAN: Well, if I hear you
4 properly, the only competition you want to preserve
5 is this auto intermodal because you've already been
6 foreclosed by the other competition and you haven't
7 sought relief from that, so that would be adding new
8 competition, at least it hasn't been there since
9 2005. Correct?

10 MR. DENTON: I disagree, frankly, and our
11 papers lay this out in great detail about how the
12 idea of preserving the competitive network that you
13 set up in 1996 is crucial going forward.

14 CHAIRMAN OBERMAN: Well, I didn't set it
15 up, but you know at some point the status in the
16 railroad is the status of what's going on and you've
17 been in a status situation until you over the last
18 few years got an agreement on your intermodal and
19 automobile traffic. So, if we go back to add
20 something that hadn't been there for 12 years, we're
21 increasing competition the way I see it. That's why
22 I ask these questions of why somebody has to come in

1 here to do something about it. Everybody seemed to
2 be living with the situation of double rates at
3 Laredo and whether that was good idea for you to live
4 with it, not contested, or the shippers did not
5 contest it.

6 I'm not suggesting, but that is what
7 happened and now you really want a condition which
8 will take you back to 2005 in terms of what you can
9 do. That sounds to me like adding competition. It's
10 not preserving something that's been there for the
11 last 17 years.

12 MR. DENTON: We appreciate that view and
13 that's why we addressed specifically in our briefs.

14 BOARD MEMBER SCHULTZ: I think you
15 mentioned that the issue is not reasonableness with
16 regard to Laredo. It's about making sure that the
17 gateway remains open and yet, kind of following the
18 questions and the dialogue here today it seems as if
19 rate transparency and rates are somewhat at play. I
20 was wondering if you could address whether or not
21 implementing arbitration as it relates to the Laredo
22 Gateway if that might not alleviate some of those

1 concerns.

2 MR. DENTON: Arbitration, enforcement at
3 the Board, all of these are post-hoc mechanisms that
4 we really believe are largely ineffective and that
5 there is a solution to address this on a going
6 forward basis right now that will eliminate the need
7 to deal with these types of lengthy dispute
8 resolutions issues, whether it's in arbitration at
9 the Board, wherever.

10 MR. NOBER: But I mean we do have
11 arbitration in our other agreements and it's probably
12 -- you know, anything is better than nothing. The
13 distinction that I think you all have argued is that
14 in, say, the Montana arbitration there's greater
15 visibility than perhaps in this situation. So, I
16 understand maybe, Roger, you'd be suggesting that
17 arbitration is better than nothing. Arbitration plus
18 something with enhanced visibility could be even
19 better than what arbitration is. Okay. Yes,
20 correct.

21 CHAIRMAN OBERMAN: Any further questions
22 for BNSF and Northern Southern?

1 (No response)

2 CHAIRMAN OBERMAN: Okay. Thank you all,
3 appreciate your patience. Sorry you had to stay
4 overnight, but then we had to stay overnight. We're
5 going to take a 10-minute recess. As the week has
6 worn on I think we need a little break and we will
7 reconvene at 11:47, thereabouts.

8 (Recess)

9 CHAIRMAN OBERMAN: Robert Girardot, Brian
10 Tisch, Ramsey Shehadeh, and Julie Carey. I'm sure I
11 mispronounced somebody's name. Everybody here? So,
12 Mr. Cunningham, are you the presenter?

13 MR. CUNNINGHAM: Thank you very much.
14 Good morning, Chairman Oberman, Vice Chairman
15 Schultz, Members Fuchs, Primus, and Hedlund. Mr.
16 Primus is not here.

17 CHAIRMAN OBERMAN: Let me say, by the
18 way, he had a personal matter that he needed to
19 attend to. And for the record, as has happened with
20 any Board member who has to step out, shortly or
21 longly, they will be reading the transcript, so they
22 will be fully briefed before any decision in this

1 case is read. I meant to say that when Robert had to
2 duck out.

3 MR. CUNNINGHAM: Thank you, Mr. Chairman.

4 CHAIRMAN OBERMAN: Proceed.

5 MR. CUNNINGHAM: My colleagues and I are
6 honored to be here. I am especially honored as I am
7 celebrating my 50th year in the law, which began as
8 counsel to the Senate Commerce Committee and my 46
9 years as a practitioner before this honored agency,
10 which began when I joined Conrail as special counsel.
11 I will begin by summarizing our presentation. How
12 since 2006 KCS and NS have unlawfully foreclosed
13 competition to, from, and over the Meridian
14 Speedway, how that loss of competition has harmed the
15 public interest, how the CP/KC transaction will
16 exacerbate that harm, why and how the Board should
17 remedy that harm now and why Speedway competition
18 will increase the public interest in the transaction
19 without reducing CP/KC's private benefit.

20 Next, my colleagues will address the
21 effects of the exclusivity arrangements and
22 restricted gateways on Speedway competition from a

1 variety of perspectives. As many have noted here
2 today, what matters is the public interest, the
3 standard governing this proceeding. Before we get to
4 our slides, let me reiterate our answers to three
5 questions posed by Applicants in pleading before
6 the Board in this hearing, answers they continue to
7 ignore.

8 Why are we here? We are here because the
9 Meridian Speedway is an inextricable part of the CP/KC
10 transaction. Unlawful agreements and unreasonable
11 gateway restrictions saddle Speedway shippers and
12 will be exacerbated by the transaction. We believe
13 you have the authority and will protect the public
14 interest by requiring Applicants and NS to remove
15 these barriers to competition.

16 Second, the harms that need a remedy stem
17 from the 2006 NS/KCS joint venture transaction. So,
18 why are we now here, not then? It goes to the nature
19 of business. In 2006, none of the businesspeople at
20 CSX questioned with NS and KCS had done was lawful.
21 Rob Girardot was there. They responded by seeking
22 other ways to do business that did not require the

1 Speedway.

2 No lawyer was commissioned to take a deep
3 dive into what NS told you yesterday is a very
4 convoluted set of agreements. These are the
5 agreements in the public version.

6 Second, KCS and NS did a good job of
7 hiding from the Board, and everyone else, what the
8 Speedway agreements were really about. This
9 transaction led CSX -- and this is the first major
10 merger transaction in this century. Lead CSX to look
11 at the effects on its business. We investigated the
12 change of control provisions in the Speedway
13 agreements.

14 After dozens of hours of wading through
15 the intricacies of these hundreds of pages, again, we
16 realized, and it was to my eyes in the first
17 instance, we realized they contained extraordinary
18 unlawful, anti-competitive provisions that you should
19 remove, and you may only be able to remove in this
20 proceeding.

21 Third, what is implicit needs to be made
22 explicit. These harms to shippers have been going on

1 so long the Applicants and NSS why don't we let them
2 go on longer? From my perspective this question is
3 irresponsible and answers itself. There is no
4 reason to allow these harms to continue. Without a
5 remedy, the Board risks eroding its mandate to
6 protect the public interest.

7 Our goal here is to remove unlawful and
8 --

9 CHAIRMAN OBERMAN: I'm sorry to
10 interrupt. Do you have a slide book for us? It's
11 hard from some of our eyes, mine in particular, to
12 read that on the screen, but I'll try.

13 MR. CUNNINGHAM: We understood that those
14 slides were provided to you by your staff. We have
15 copies.

16 CHAIRMAN OBERMAN: Well, I'm only one of
17 five.

18 MR. CUNNINGHAM: This one is -- I can
19 read most of it to you. Our goal is to remove
20 unlawful and unjustifiable barriers to competition
21 to, from, and over the Speedway. Without these
22 conditions the CP/KCS transaction cannot be consistent

1 with the public interest.

2 Our conditions would remove the unlawful,
3 perpetual NS/KCS exclusivity arrangements that
4 foreclose competition for large volumes that Speedway
5 intermodal traffic over what appears to be the dense
6 and highest volume intermodal corridor to and from
7 the Southeast. And we wish you to remove the
8 anti-competitive restrictions now existing on the
9 interchange over the Speedway Gateways.

10 Restored Speedway competition will
11 improve service, provide competitive prices, grow
12 volumes, and strengthen the U.S. economy, especially
13 in the Southeast. It will also increase CP/KC's
14 competitive opportunities, as Wall Street analysts
15 have attested. Our economists expect CSX's condition
16 will increase the public benefits of the CP/KCS
17 transaction by at least 25 percent.

18 These benefits would occur even if CSX
19 gained no new traffic because we are advocating
20 competition and whether we will benefit from that
21 competition is yet to be seen. Yesterday you heard
22 NS argue at length that the transaction in

1 Applicants' operating plan will harm the public
2 interest because it will harm NS's service and "Many
3 customers will have no choice but to switch back to
4 the highways."

5 That's a very interesting proposition.
6 It raises at least two questions. Why is the only
7 choice for Speedway intermodal shippers to switch to
8 truck if as NS also says shippers have other
9 competitive rail options? As you asked yesterday,
10 Member Fuchs, why won't competitive market forces
11 remedy these issues?

12 The answer is that the Speedway is by far
13 the best route for many shippers. We call them
14 Speedway shippers. And Speedway shippers have been
15 forced by NS to put all their eggs in one basket.
16 Every harm NS identified yesterday has its root and
17 cause in the lack of rail competition on the
18 Speedway. Speedway shippers should no longer be
19 forced to put all their eggs in one basket.

20 Let's explore what the Speedway is. The
21 Speedway runs between Meridian, Mississippi and
22 Dallas, Texas via Shreveport, Louisiana. It has two

1 parts, the KCS line between Dallas and Shreveport and
2 the line owned by the KCS joint venture, Meridian
3 Speedway, LLC between Shreveport and Meridian. Both
4 parts are governed by the unlawful exclusivity
5 arrangement between KCS and NS. They are buried in
6 these hundreds of pages, but once you learn to
7 recognize them, they're pretty simple to see.

8 We agree with the Applicants and NS -- I
9 want to stress this -- that the Speedway is by far
10 the best route for many shippers to and from the East
11 and the fact that it's the best route explains why NS
12 that if they have congestion shippers will have to
13 go to trucks, not to other railroads.

14 Again, CSX's conditions fix two problems,
15 the unlawful, anti-competitive and perpetual
16 exclusivity arrangements are first. NS and KCS have
17 agreed to foreclose competition for two types of
18 Speedway traffic, transcon Intermodal and Dallas
19 intermodal. The definitions are in the slide and I'd
20 be glad to go into them if you wanted further
21 examination.

22 Until 2005, KCS owned the entire

1 Speedway. It could interchange with two in 2005. It
2 could interchange with and grant haulage or trackage
3 to other carriers. KCS has granted NS haulage for
4 transcon intermodal, but KCS could compete for that
5 traffic to the Dallas and Shreveport Gateways. KCS
6 interchanged with CSX at Meridian where CSX and NS
7 competed for all Speedway traffic.

8 In 2005, even more competition with NS
9 for Transco Intermodal was imminent. NS, CSX, and
10 KCS were negotiating to deal to develop a new
11 intermodal service over the Speedway. In response,
12 NS anted up to perpetually foreclose that
13 competition. NS especially feared competition from
14 the imminent, non-exclusive KCS, BNSF, CSX route. NS
15 made a \$308 million investment in a new joint venture
16 railroad, the MS, LLC that now owns the line between
17 Shreveport and Meridian. With that investment, NS
18 also paid heavily, perpetual foreclosure of
19 competition for both Dallas intermodal and transcon
20 intermodal traffic.

21 Slide 13 shows NS bought permanent
22 exclusivity in two areas over the Speedway and east

1 of the Speedway. To make clear how egregious these
2 arrangements were, Slide 14 shows two competitors for
3 transcon intermodal in 2005, plus imminent
4 competition. Then NS paid KCS to reduce the carriers
5 competing for transcon intermodal from two to one.

6 KCS had been in a strong position. It
7 was a classic underlying carrier hosting haulage for
8 NS with the ability to compete with NS and to
9 interchange with CSX. Then KCS sold NS its right to
10 compete using its own line and its right to
11 interchange with CSX. That withdrawal, to our
12 knowledge, is otherwise unheard of in the railroad
13 industry.

14 NS had repeatedly asserted that the
15 affected agreements governed only a narrow category
16 of traffic in their words. We won't reveal here the
17 highly confidential volumes of traffic denied
18 competition by the exclusivity arrangements. They're
19 in the record, but you get the picture. The
20 exclusivity arrangements foreclosed competition for
21 all the intermodal traffic we discussed.

22 First, KCS can move Dallas intermodal

1 traffic over the Speedway only in interchange within
2 asset Meridian unless NS agrees to allow competition
3 at Meridian. NS must agree to the rates for those
4 movements whether they move over NS at Meridian or
5 some other carrier.

6 Did that lock up the market? It sure
7 did. NS bought and paid for exclusivity between
8 Meridian in East, and it has enjoyed the profits for
9 16 years. Second, only NS can handle Transcon
10 Intermodal traffic over the Speedway to and from the
11 East. Does that sound anti-competitive? It is and
12 has been for 16 years.

13 I'm now at perhaps the most -- if we
14 understand the context perhaps the most important
15 part of this presentation. The arrangements were
16 anti-competitive. They were unlawful. They were
17 unlawful because the only approval KCS sought was an
18 exemption for an intra-corporate transaction. Use of
19 that exemption kept the arrangements under the radar,
20 and nobody bothered to look into its
21 meritoriousness.

22 The exemption required no Board scrutiny

1 or approval. However, the MS, LLC agreements were
2 not eligible for that exemption. They required --
3 okay. The MS, LLC agreements were not eligible for
4 an intra-corporate exemption. They required a
5 license after Board scrutiny under Section 11323,
6 just like any other controlled transaction.

7 Why? Because they altered the
8 competitive balance with carriers outside the
9 corporate family and the Board rules only allows
10 exemptions for intra-corporate transactions without
11 this effect.

12 No one disputes the arrangement altered
13 the competitive balance. NS thinks that was a good
14 thing and we think it's a bad thing, but nobody
15 disputes that it altered the competitive balance and
16 that alone is sufficient to render all the MS, LLC
17 agreements void from the beginning. Exemption also
18 did not apply because KCS and NS agreed to a division
19 of traffic that required approval under Section
20 11322.

21 Why did NS and KCS require pooling
22 approval? Because they are competitors taking a

1 common position toward the public in dividing the
2 benefits and costs by agreement rather than according
3 to individual performance and the arrangements
4 restrained competition. They divided the Transcon
5 market by removing KCS as a competitor and they
6 divided the Dallas intermodal traffic by precluding
7 competition east of Meridian. What KCS and NS did in
8 2006 was never approved by this Board, never reviewed
9 by this Board, and is therefore unlawful.

10 Since 1980, the classic rubric in a
11 consolidation case is to be granted condition must
12 first address an effect of the transaction. The
13 Board will not impose conditions to ameliorate
14 longstanding problems not created by the transaction
15 and in other cases I've made that argument against
16 proposed conditions, but that rubric refers to a
17 longstanding lawful arrangement. Here the
18 arrangements are clearly unlawful. Nothing in the
19 Board's precedents or the statute bars conditioning
20 this transaction on removal of unlawful arrangements
21 that harm the public interest.

22 Because the transaction must be

1 consistent with the public interest, the Board should
2 not approve it without the CSX conditions, otherwise,
3 it would perpetuate unlawful harm to the public
4 interest. The transaction would also exacerbate the
5 harms of the arrangements. Applicants operating
6 plans show both increased congestion and
7 intermingling of fast and slow traffic.

8 As NS has demonstrated, this will slow
9 down NS's trains and harm intermodal service over the
10 Speedway. CSX and NS agree on this point. NS,
11 however, says the solution is more NS control of the
12 Speedway. More control? NS lacks control over the
13 Speedway? Not with respect to the traffic at issue,
14 not at all. The harm arises because the shippers
15 have their eggs in one basket.

16 If you restore competition over the
17 Speedway, you will solve this problem. MS, LLC and KCS
18 will be able to fund any investments required to
19 relieve congestion because carriers make investments
20 when traffic can be had. As I demonstrated, the
21 Board has the authority to put the genie back in the
22 bottle.

1 CSX recommends a straightforward surgical
2 remedy, remove only the exclusivity arrangements,
3 preserve the remaining MS, LLC agreements consistent
4 with their severability clauses. While these
5 agreements are mare's nest, it only takes the removal
6 of a few provisions to eradicate their
7 anti-competitive effect. Unwinding the joint venture
8 is not required.

9 The competitive and reasonable economic
10 strategy to recover an investment in line to make a
11 profit is to optimize throughput over that line.
12 This is done by proper pricing to earn a return, not
13 by foreclosing competition. Please recall I opened
14 with two takeaway issues, exclusivity arrangements
15 and gateways. The second barrier to competition over
16 the Speedway is its restricted gateways.

17 Even without the arrangements shippers
18 could not benefit from competition over the Speedway,
19 to, from, and over the Speedway unless the gateways
20 that are now only partially open to some carriers and
21 some traffic are fully opened. NS wants all
22 existing gateways open, but only for NS on the

1 Speedway. Applicants want no fully open gateways on
2 the Speedway or not be required to have them at
3 least.

4 CSX urges the Board to require that all
5 CP gateways be subject to conditions like those
6 imposed by the Board on the PanAm transaction,
7 however, a variation is required to fit the Speedway
8 gateways, Meridian, Shreveport, and Dallas. They are
9 open to some carriers for some traffic, but not
10 others. The Board should remove those restrictions
11 and ensure shippers can enforce this requirement.

12 Among other benefits, opening the
13 Speedway gateways, along with the Laredo Gateway, is
14 the key to attracting Mexico truck traffic from
15 highways to the Speedway. If Meridian is not open to
16 KCS interchange of any traffic with any carrier,
17 Transcon and Dallas intermodal shippers will still be
18 denied a competitive option to and from the East via
19 KCS/CSX. If Shreveport is not open, then UP's route
20 to Mexico will not be available to take trucks off
21 the highways that KCS cannot attract today, and CP/KS
22 would be able to frustrate UP competition and

1 potential BNSF competition for West Coast
2 international traffic so competitive services could
3 not be built as our commercial officers will explain
4 on the Transcon anchor train. If Dallas is not open,
5 there will be fewer options for intermodal shippers
6 between the Dallas area and points West and East.

7 To conclude, the Board should ensure
8 Speedway competitions so the transaction will not
9 perpetuate and exacerbate these silent killer
10 barriers to competition. Doing so will create an
11 opportunity for more than \$50 million in annual
12 public benefits to shippers, consumers, the
13 environment, and the economy.

14 You should act now. If you do not, the
15 Speedway corridor may never be open to competition.
16 We hope you will exercise your authority and
17 demonstrate this agency's willingness to commit and
18 foreclose the exacerbation of unlawful and
19 unwarranted restraints on competition. Thank you
20 very much. I'm glad to answer questions, or I will
21 turn the presentation over to Ms. Kenney.

22 CHAIRMAN OBERMAN: I have a couple,

1 others may, and then we'll proceed. Mr. Cunningham,
2 when did CSX discover the alleged violations of the
3 statute that you recited here?

4 MR. CUNNINGHAM: After the transaction
5 led to commission and investigation of the effects of
6 the transaction on CSX.

7 CHAIRMAN OBERMAN: When was that?

8 MR. CUNNINGHAM: That would have been
9 either late last year or early this year.

10 CHAIRMAN OBERMAN: When was the
11 transaction?

12 MR. CUNNINGHAM: This transaction?

13 CHAIRMAN OBERMAN: No.

14 MR. CUNNINGHAM: When was the supposed
15 exempted transaction, 2006.

16 CHAIRMAN OBERMAN: So, between 2006 and
17 2021, CSX took no steps to investigate the alleged
18 illegality of this transaction?

19 MR. CUNNINGHAM: Not that I'm aware of,
20 and as Mr. Girardot will explain, that's not what the
21 commercial folks do. They commission the lawyers and
22 if they don't see a problem -- they were assuming,

1 and I think from the record they could rightfully
2 assume that KCS had legitimately noticed the
3 exemption. As I said, I had to read these documents,
4 which are painful, several times before I woke up on
5 a Saturday morning and said what in the world's
6 going on here. And I don't think anyone in CSX
7 commercial operations and intermodal operations
8 would've taken the time to make that investigation
9 nor do I think at that time when we assumed everyone
10 was operating in good faith in these matters, they
11 would've had much incentive to look. They went on
12 with their business.

13 CHAIRMAN OBERMAN: You said that prior to
14 the Speedway joint venture there were discussions
15 involving NS and CSX, do I understand that right?

16 MR. CUNNINGHAM: There were two sets of
17 negotiations going on, as MR. Girardot will explain.

18 CHAIRMAN OBERMAN: And NS stepped up and
19 put \$300 million on the table.

20 MR. CUNNINGHAM: As Mr. Girardot will
21 explain, yes, they did that. And called up later and
22 said, we're sorry we cut you out.

1 CHAIRMAN OBERMAN: Right. And did CSX
2 come in and offer 301 million?

3 MR. CUNNINGHAM: They weren't offered the
4 chance. The deal was cut while these other
5 negotiations were going on. Mr. Girardot can state
6 it better.

7 CHAIRMAN OBERMAN: Well, I'm asking you
8 because you made this presentation and Mr. Girardot
9 can come in.

10 MR. CUNNINGHAM: I will be glad to try to
11 answer your questions, Mr. Chairman.

12 CHAIRMAN OBERMAN: So, in this
13 transaction a deal was cut, and CN came in and
14 offered a few billion dollars more after a deal was
15 cut and then another deal was made, so I've been
16 around actually three years longer than you have in
17 the practice of law, Mr. Cunningham.

18 MR. CUNNINGHAM: You're wearing it
19 better.

20 CHAIRMAN OBERMAN: Well, I don't know if
21 I agree with that. You're doing fine, but the people
22 come in and bid on things all the time and you're

1 telling me that CSX was in negotiations, finds out
2 one day they've been priced out of the deal.

3 MR. CUNNINGHAM: That's not what they
4 were told. They were told that the deal was done.

5 CHAIRMAN OBERMAN: Yes. Okay. Whatever
6 it was.

7 MR. CUNNINGHAM: And BNSF, who was
8 leading those negotiations with KCS and the
9 executives.

10 CHAIRMAN OBERMAN: Whatever it was, and
11 then for 15 years being excluded from being able to
12 use this traffic didn't undertake any investigation
13 and apparently it was the proposal of this merger
14 that caused CSX to undertake an investigation, is
15 that it?

16 MR. CUNNINGHAM: That's correct.

17 CHAIRMAN OBERMAN: To your knowledge, and
18 I don't know the answer to this, but I'm going to ask
19 our esteemed lawyers here, but is there a statute of
20 limitations on the claims you're talking about?

21 MR. CUNNINGHAM: Not that I'm aware of,
22 it's an ongoing, unlawful restraint on competition.

1 CHAIRMAN OBERMAN: So, is there a laches
2 problem?

3 MR. CUNNINGHAM: I don't think there is.
4 What's gone is gone, but there's no laches problem
5 and very clearly these are continuing violations.
6 They are not approved, Your Honor -- pardon me -- Mr.
7 Chairman. And they are void ab initio under the
8 Board's rules.

9 CHAIRMAN OBERMAN: Well, that may be.
10 You made an allegation, but I have to say that given
11 the stakes that you are now telling us about is that
12 they've affected CSX and what seemed to be a pretty
13 well known operation of the Speedway, as far as I --
14 and I've been here for three years, three and a half
15 years and I've heard no one complain about the
16 exclusivity of the Speedway until your request here,
17 so it does cause -- it gives me pause. You know our
18 procedures are pretty clear and experienced rail
19 counsel, which I believe you are, and if not, it's
20 really the client's obligation to be on notice and do
21 something about it. I'm having a little trouble
22 hearing allegations of illegalities so great as to

1 render transaction void ab initio. That's pretty
2 strong --

3 MR. CUNNINGHAM: Well, it's not the
4 violation -- pardon me, Mr. Chairman, that renders it
5 void ab initio. It was the only approval you gave it
6 was an exemption that your rules precluded being
7 applied.

8 CHAIRMAN OBERMAN: Well, that's what
9 you're saying, that the violation of the statute in
10 our rules in your view renders this void ab initio.
11 That's a fairly strong claim to sit on for 16 years.
12 That's what I'm talking about.

13 MR. CUNNINGHAM: It's not a claim that
14 was known and with all due respect, I don't think
15 anybody understood this set of legal arrangements.
16 It was accepted as a business practice that the Board
17 had been given notice of and everybody went on about
18 their business. I do not believe that the Board
19 should abandon its duty to the public interest
20 because a harm has been going on for 16 years. It
21 never should've gone on in the first place. The
22 Board has a responsibility to the public interest.

1 CSX, as I said in the beginning, doesn't know whether
2 it's going to get any traffic from competition. What
3 we do know is the competition puts pressure on
4 prices, improves service, and gives shippers more
5 options and creates the opportunity to take a lot
6 more trucks off the road than anybody is proposing to
7 do otherwise.

8 This is an opportunity to meet the goals
9 that this Board has stated consistently under your
10 chairmanship that it wishes to pursue. This is not
11 something that should be waved away. It's egregious.
12 I'm sorry. I've been here many times and I don't
13 use terms like that. I'm a very conservative person,
14 but this is a very serious violation of the
15 principles that this Board stands for, competition,
16 open gateways, and more trucks off the road, and
17 more economic development, and more employment I
18 would state because if there's more throughput over
19 the Speedway does now have the opportunity to move it
20 will mean more trains and more train employees.

21 The trains that we're talking about, as
22 my colleagues will explain, are not trains that are

1 going to go over the hump to Memphis and down to
2 Atlanta.

3 CHAIRMAN OBERMAN: Let me pursue this a
4 little further. It's not being litigated here, but I
5 am quite familiar with the concepts of notice and
6 constructive notice and when an aggrieved person is
7 held to know that they should investigate whether
8 they have a claim and I'm not so sure that your
9 conclusory statements that they had no reason to look
10 into this apply, but I'm not making any judgment on
11 it, only raising the question.

12 But let me ask you this question, as I
13 understand CSX's concern here, if this merger were
14 disapproved you would still contend that the initial
15 transaction was illegal and should be remedied, would
16 you not?

17 MR. CUNNINGHAM: We might, but that's not
18 here. That's another place.

19 CHAIRMAN OBERMAN: I'll tell you why it's
20 here. There is no way of knowing what transaction
21 was going to go through for much of last -- I don't
22 know what month last year your clients discovered

1 this alleged violation, but for much of last year no
2 one knew that there was going to be a CP deal because
3 CN had a deal. And it is now almost October of 2022
4 and for what you allege is a dramatic violation of
5 our laws, one that NS spent \$300 million to gain
6 you've still not taken any action, other than to ask
7 us for a condition and I'm having trouble
8 understanding why, without knowing whether this or
9 any other merger because I'm not sure that CN
10 would've had the same repercussions had they
11 succeeded in acquiring KCS, I'm hearing a situation
12 that begin 16 years ago, no action was taken until
13 you filed your objections here. The violation was
14 discovered no later than last year, whether it
15 should've been discovered earlier, and still no
16 formal lawsuit, petition before this Board, or other
17 actions taken to undo what you claim is a huge bar to
18 competition. I'm just having trouble with it.

19 MR. CUNNINGHAM: Well, I'll be very
20 frank.

21 CHAIRMAN OBERMAN: I hope so.

22 MR. CUNNINGHAM: I was not directed to

1 this task until after CP rebid and won and we began
2 work to really understand this transaction. We tried
3 to understand it from CN, but we hadn't gotten -- no
4 one had pointed to Meridian Speedway, but there was a
5 concern about change of control with respect to the
6 Wiley Terminal. I had never worked for CSX, well,
7 not since the Staggers Act. I had not worked for CSX
8 up until last year on a merger case and I don't know
9 what went on before, but the only person who does is
10 Mr. Girardot.

11 But I do know that this is the place
12 where you can find that if the aspects of the
13 transaction you approved are necessary to the
14 transaction they're forever barred from legal
15 scrutiny as to the things that are approved.

16 CHAIRMAN OBERMAN: Not if they're void ab
17 initio as you suggest. I don't think the obligation
18 is necessarily yours, Mr. Cunningham, particularly,
19 if you hadn't been retained until last year. The
20 obligation and the notice usually fall on the client,
21 particularly, where the client's sophisticated. And
22 in the case of all of these Class 1 railroads, they

1 have very large legal departments and, in my
2 experience, first-rate general counsels, as CSX has
3 had over the years, and I'm having a lot of trouble
4 with this. That's all I'm saying.

5 MR. CUNNINGHAM: Well, if I may, I find
6 it odd that an agency as esteemed as this one whose
7 charter is to protect the public interest would not
8 ask if something like this is raised, whenever it's
9 raised. If somebody had flipped a piece of paper
10 over the transom you wouldn't look into it and decide
11 whether it should go on or not. I don't think that
12 the ultimate decision-maker here is not the
13 railroads. It's not the lawyers. It's you. You
14 carry that mantle. You're dedicated public
15 servants. This is in your wheelhouse, and you can
16 only fix one part of the problem, the gateway problem
17 here because there is no other relief for that and
18 this transaction would perpetuate these unlawful
19 arrangements and you would sanction them. Whether
20 they could then be pulled apart or challenged is
21 another question which is for another day.

22 CHAIRMAN OBERMAN: I take it your

1 position is if we were to agree with you that the
2 penalty on NS for having engaged in an allegedly
3 invalid transaction is that they lose all or part of
4 the value of the \$300 million they spent, is that the
5 penalty?

6 MR. CUNNINGHAM: They should only lose
7 the part that results from restraints on competition.
8 They don't lose their interest in MS, LLC.

9 CHAIRMAN OBERMAN: But do you not think
10 that their determination to spend \$300 million was
11 relied on the nature on the transaction they entered
12 into?

13 MR. CUNNINGHAM: We certainly do, and MR.
14 Tish will be addressing that a bit later as a part of
15 the competition.

16 CHAIRMAN OBERMAN: All I can tell you I'm
17 having a lot of trouble with it, but let's -- go
18 ahead.

19 BOARD MEMBER FUCHS: And I want to
20 respond directly to your broader point, Mr.
21 Cunningham, which I understand. But just on the
22 Chairman's line of questioning about what CSX knew

1 and when, what happened in the Louisville, Indiana
2 railroad transaction?

3 MR. CUNNINGHAM: I don't know.

4 BOARD MEMBER FUCHS: Does anybody at the
5 table know? I understand that was a joint use
6 transaction and there were a number of repetitive
7 restrictions that were in play. I'm not saying they
8 were the same restrictions that you all are taking
9 issue with, but one of the things that I noticed in
10 that transaction, and this was from -- I think it was
11 filed in '13. It might've been ultimately
12 adjudicated in like a '15 range, is that CSX cited
13 the exemption in support of its joint use
14 application.

15 MR. CUNNINGHAM: They may have.

16 BOARD MEMBER FUCHS: So, the way you
17 describe it is Meridian happens in '06, the lawyers
18 and the operating people and marketing people aren't
19 talking to each other and then we wake up with this
20 merger, but it's a little bit more complicated than
21 that because it seems as those CSX's filing in
22 Louisville and Indiana that CSX looked at the

1 Meridian exemption, looked at those contracts and
2 drew from those contracts for its own joint use.

3 MR. CUNNINGHAM: That may be the case.

4 BOARD MEMBER FUCHS: That's a little bit
5 different than what you described.

6 MR. CUNNINGHAM: No, it is not.

7 Louisiana and -- I don't know about that case, was
8 that an exemption proceeding?

9 BOARD MEMBER FUCHS: I actually -- I
10 could tell you in a minute. I think it was a minor
11 transaction.

12 MR. CUNNINGHAM: A minor transaction?

13 BOARD MEMBER FUCHS: It was.

14 MR. CUNNINGHAM: There was all sorts of
15 activity going on, I'm assuming, as there is normally
16 with respect to a minor transaction.

17 BOARD MEMBER FUCHS: True, most
18 certainly.

19 MR. CUNNINGHAM: And you reviewed it, and
20 you gave it whatever blessing or lack of that you did
21 because I'm not familiar with because I'm not
22 familiar with the case.

1 BOARD MEMBER FUCHS: And so, what CSX
2 said in that case, and there are differences in terms
3 of what's in that contract for just what you're
4 talking about is in other transactions involving a
5 significant capital investment by a railroad to
6 improve lines that it does not own or fully control
7 the Board has permitted certain restrictions similar
8 aimed at protecting that investment citing the
9 Meridian Speedway exemption.

10 MR. CUNNINGHAM: Right.

11 BOARD MEMBER FUCHS: And then the Board
12 embraced that in its ultimate decision and I'm not
13 getting into the broader public interest and the
14 appropriateness of raising it here. I'm only
15 addressing the contention that CSX was in the dark
16 for all these years and didn't look at it when it
17 seems as though you're actively citing the exemption,
18 you're drawing from the contracts to inform your own
19 joint use agreements.

20 MR. CUNNINGHAM: Well, I can't speak to
21 that, but I can say that no one I've spoken to at CSX
22 had a memory of ever looking at the anti-competitive

1 restraints in this document.

2 BOARD MEMBER FUCHS: Well, take a look at
3 that, and I might be misreading, but it does seem
4 like you are citing -- CSX is citing the very
5 exemption that you claim is illegal.

6 MR. CUNNINGHAM: Well, they're not citing
7 the exemption. You're saying they're citing the
8 documents.

9 BOARD MEMBER FUCHS: No, no, in your
10 filing you are citing the exemption decision.

11 MR. CUNNINGHAM: The exemption decision
12 itself, however, did not address these -- there was
13 never any mention in that exemption proceeding of
14 these vertical restraints and horizontal restraints.
15 They did not say we are affecting competition. They
16 knew they couldn't be there under the Board rules if
17 they were affecting competition.

18 BOARD MEMBER FUCHS: But you're also
19 citing the restrictions.

20 MR. CUNNINGHAM: Pardon me. LLC
21 agreements, membership agreements have lots of
22 restrictions.

1 BOARD MEMBER FUCHS: Yes.

2 MR. CUNNINGHAM: They are very similar
3 across a wide range of transactions, not just
4 railroads, but everything else and the minority party
5 seeks to restrain certain actions from the majority
6 that would harm them, but I don't know that in that
7 transaction there was a proposal to shrink
8 competition from two to one or to foreclose gateway
9 competition.

10 BOARD MEMBER FUCHS: There are key
11 differences and I'm only responding to the question
12 that I heard, and you raised broader points in this
13 and I'm also springing this on you right here and I
14 don't think this is --

15 MR. CUNNINGHAM: No, I think that's
16 entirely fair. I should've known, but --

17 BOARD MEMBER FUCHS: No, no, no, it's
18 okay and I might be misreading it.

19 MR. CUNNINGHAM: Here's the point --
20 pardon me. I don't believe they said we are citing
21 this because we're about to restrain competition, did
22 they?

1 BOARD MEMBER FUCHS: They certainly said
2 that the Board permitted competitive restrictions in
3 order to protect their investment. Now, that's not
4 the same thing and there are differences in these
5 things.

6 MR. CUNNINGHAM: Indeed, there are.

7 BOARD MEMBER FUCHS: But I'm responding
8 to the dialogue that you all had, and you all have
9 not had the -- well, you all have not reviewed these
10 decisions it doesn't sound, so how about we address
11 it in final briefs and move on?

12 MR. CUNNINGHAM: We'll do that.

13 BOARD MEMBER FUCHS: Okay.

14 BOARD MEMBER HEDLUND: I have one
15 question.

16 MR. CUNNINGHAM: Yes, Ms. Hedlund.

17 BOARD MEMBER HEDLUND: Since I'm new to
18 the Board, can you cite any precedent for the Board
19 taking an action similar to what you are asking us to
20 do?

21 MR. CUNNINGHAM: I cannot because the
22 Board's precedent, which I have relied on from the

1 other perspective several times is about longstanding
2 legal arrangements. I'm not aware of a case in which
3 a party came to the Board in a merger case and said
4 this will perpetuate an unlawful competitive
5 restraint. There may be them, be out there, and
6 others certainly are smarter and have better memories
7 than I do, but in my research over the years I've
8 never encountered that situation, is that helpful?

9 BOARD MEMBER HEDLUND: This is,
10 essentially, a case of first impression, but we have
11 never --

12 MR. CUNNINGHAM: Absolutely, as far as I
13 know.

14 BOARD MEMBER HEDLUND: -- have done
15 anything that would have this kind of far-reaching
16 effect based on something that was alleged to be
17 illegal that had been sitting in place for 16 years.

18 MR. CUNNINGHAM: Right. And if it's
19 illegal now, it was illegal then, it's illegal today.

20 BOARD MEMBER HEDLUND: But you can't cite
21 a case where we made that determination and upset a
22 transaction on that basis.

1 MR. CUNNINGHAM: I don't know because
2 this is a very extraordinary -- we've never seen
3 anything like this before and I didn't recognize it
4 at first. I have to plead guilty.

5 BOARD MEMBER FUCHS: Real quick, I mean
6 just for that initial point. You view it more -- and
7 I don't know if you argued this, but you view it more
8 appropriate to deal with it in a merger than going in
9 and attacking the exemption directly.

10 MR. CUNNINGHAM: If it's necessary to
11 direct it directly, we might have to do that, if
12 we're able to and you haven't sanctioned it. But
13 more importantly, we're not trying to unwind the
14 whole set of agreements that are nominally void.
15 We're only asking you to remove particular
16 restrictions on competition that are contained in
17 those agreements.

18 BOARD MEMBER FUCHS: I understand.

19 CHAIRMAN OBERMAN: Mr. Cunningham, if
20 you're contention is correct that all times, broad
21 principle, which I agree with that we are here to
22 protect the public interest, and in my view, promote

1 competition, what justification would we have if you
2 have convinced us that the arrangement was void ab
3 initio to not undo it completely? I mean how could
4 we say it's only half illegal? I mean I don't get
5 that. You may not be asking for more, but it seems
6 to me it would be a pretty cynical move on our part
7 to say, you know, there's a completely illegal
8 arrangement, but CSX shows up 16 years later and
9 would like part of that illegality to stay in place.
10 It just wants to get in on the deal and so we'll
11 leave the rest of the illegal arrangement in place.
12 I mean that sounds like what you're asking.

13 MR. CUNNINGHAM: No. I would like to
14 contend, first, with one part of that. We don't want
15 to get in on the deal. If there is money to be
16 spent, if there's traffic to be had once the
17 Speedway is open to competition, we will pay for
18 anything that is required to serve that traffic up to
19 the point that it's no longer profitable.

20 CHAIRMAN OBERMAN: Yeah. But you want to
21 make money on it, in that sense you want to get in on
22 the deal. That's the only reason you're here.

1 MR. CUNNINGHAM: We want to eliminate
2 these barriers of competition. They affect a lot of
3 shippers that aren't being served today, as we will
4 explain, and they permit the investment that NS has
5 been inadequate to prevent the congestion they
6 predict from the transaction. That's absolutely
7 correct.

8 CHAIRMAN OBERMAN: So, are you trying to
9 suggest that CSX is here in an altruistic mode to
10 protect a lot of traffic that it's not going to get
11 itself?

12 MR. CUNNINGHAM: It is not altruistic,
13 but we don't know whether we'll get it or not, but
14 we will provide competition and competition is not
15 present for this traffic today, Mr. Chairman.

16 CHAIRMAN OBERMAN: Well, it would be
17 naive, would it not, for us to conclude that you're
18 anything other than that you're here, not only so you
19 could compete, but that you expect to win enough to
20 make it worth your client's --

21 MR. CUNNINGHAM: You'll have to ask Ms.
22 Kenny about that. I don't know what she expects.

1 CHAIRMAN OBERMAN: Well, I've yet to see
2 any railroad come before this Board in the role of
3 private attorney general, but maybe you're
4 establishing a first.

5 MR. CUNNINGHAM: It wasn't where we
6 started, I can assure you. Thank you, Mr. Chairman.

7 CHAIRMAN OBERMAN: Are there any
8 questions for the moment?

9 MS. KENNEY: Good morning. My name is
10 Mary Clare Kenney and I'm CSX's Vice President of
11 intermodal and automotive. CSX comes before you
12 today for one simple reason. We want to compete. We
13 want to be able to compete to provide the services
14 that our customers and the communities we serve have
15 persistently asked us to provide, efficient
16 intermodal service to and from points in the
17 Southeast for traffic originating or terminating in
18 the Southwest and Mexico. We cannot do this without
19 Board action.

20 We cannot compete effectively to provide
21 those services today because NS and KCS have locked
22 up the only efficient rail artery to and from the

1 Southeast in perpetuity. As you have heard from NS
2 itself, the Meridian Speedway, which connects
3 Meridian, Mississippi to Shreveport, Louisiana and
4 Dallas, Texas is by far the shortest and fastest
5 route capable of providing time-sensitive intermodal
6 shippers with service that is competitive against
7 trucking and over which service to and from a host of
8 destinations can efficiently be aggregated.

9 Due to sheer geography from movements
10 from the Southwest and Southeast there's nothing else
11 like it. NS and KCS eliminated competition for
12 effective Southwest to Southeast service when they
13 agreed that nobody but NS could carry
14 transcontinental intermodal traffic over the Speedway
15 and nobody, but NS could interchange Dallas
16 intermodal traffic that moves over the Speedway and
17 their agreement is perpetual. They didn't just lock
18 the door to effective competition, they threw away
19 the key forever and the effects of their doing so
20 will only get worse as a result of the CP/KC
21 transaction.

22 Today we are asking the Board to allow

1 that competition by removing the parts of those
2 agreements that harm competition and ensuring the
3 Shreveport and Meridian Gateways are open. I'd like
4 to offer my insights on how this will benefit shippers
5 and take trucks off the road in the following steps.

6 First, I will explain how the NS/KCS
7 exclusivity agreements harm competition for
8 Transcontinental and Dallas intermodal traffic.
9 Second, I will explain why that has even further
10 reaching effects to prevent efficient intermodal
11 service for a range of customers and locations that
12 are clamoring for it and why open gateways are needed
13 to provide that service. And finally, I will address
14 NS's statements that its agreement to eliminate
15 competition in perpetuity is really just a way to
16 recoup its investments.

17 As Mr. Cunningham explained, the Meridian
18 Speedway agreements between NS and KCS govern two
19 critical types of traffic. For Transcontinental
20 Intermodal traffic, only NS may transport the
21 traffic between Shreveport and Meridian. And because
22 NS never hands off the traffic to other carriers at

1 Meridian, in practice, NS is also the exclusive
2 carrier for Transcontinental Intermodal traffic
3 between Meridian and points East.

4 For Dallas Intermodal traffic, only KCS
5 may transport the traffic over the Speedway, but KCS
6 and NS have to agree on the rate charged and KCS may
7 not interchange it at Meridian with anyone but NS
8 unless NS refuses to carry it, which they never have.
9 With this agreement, NS and KCS have prevented CSX
10 from participating in any way in movement of
11 transcontinental intermodal traffic and Dallas
12 intermodal traffic that passes over the Meridian
13 Speedway.

14 Why does this prevent CSX from competing
15 effectively? Because when it comes to intermodal
16 service your routing matters. It matters a lot. My
17 role as CSX's Vice President, intermodal and
18 automotive, has taught me that delivering a
19 competitive, intermodal service requires
20 understanding what shippers need in order to
21 increase their use of intermodal rail transportation.

22 Shippers need economically sustainable

1 options that meet their specific requirements for
2 delivery speed, reliability, volume, and shipping
3 costs. For most shippers, moving containers up to
4 500 miles within North America an all-truck move is a
5 natural choice. For most of those shorter moves,
6 trucks can deliver door to door with greatest
7 flexibility, reliability, lowest costs, and highest
8 speed.

9 For longer haul and higher volume moves,
10 as well as shorter, international shipments to inland
11 ports from on-dock port facilities, rail intermodal
12 can offer cost and capacity advantages for shippers.
13 For shippers that want those advantages, competition
14 between rail carriers depends on speed, reliability,
15 capacity, and costs, but each of those features
16 varies with how direct your route is.

17 If your route is significantly longer and
18 slower than another railroad's, that other railroad
19 will be better at meeting the customer's needs. And
20 all else equal, if your route is circuitous enough,
21 and even over long distance, your intermodal train
22 service is not competitive against trucking, which

1 brings me back to the Meridian Speedway.

2 The restrictions NS and KCS placed on the
3 Meridian Speedway eliminate effective competition for
4 the types of traffic subject to those agreements.

5 Why is this the case? Because as Applicants and NS
6 have explained, the Speedway offers the shortest,
7 fastest route from points in Mexico and the
8 southwestern U.S. to points in the southeastern U.S.
9 and vice versa. Other potentially competitive
10 intermodal services are handicapped. They must
11 detour around the Speedway.

12 When NS and KCS prevented CSX from
13 participating in the movements of traffic over that
14 route, CSX's only option was to work with BNSF to
15 transport traffic via a line that goes through
16 Memphis to Birmingham and then via haulage over CSX
17 to Atlanta. We've worked hard to make this route as
18 fast and efficient as possible and through this
19 arrangement BNSF carries significant volumes of
20 intermodal traffic between LA and Atlanta.

21 For those customers for which this route
22 meets their needs, CSX and BNSF have fought to

1 compete against NS, but this route can take more than
2 two days longer than Transcontinental service over
3 the Meridian Speedway. For time-sensitive shippers
4 for whom delivery speed is a key priority, and that
5 describes a lot of intermodal shippers, this route
6 will never be a suitable alternative to the Meridian
7 Speedway and this BNSF/CSX traffic is not growing
8 with the southeastern economy nor in line with
9 intermodal growth elsewhere.

10 Our volumes today over this route are not
11 much larger than when the service was initially
12 established. For more time-sensitive
13 transcontinental shippers only the Speedway provides
14 a direct enough routing to meet their needs, but for
15 them there is only one carrier option. They and many
16 more shippers would benefit if the Speedway were open
17 to competition to serve their needs.

18 And for Dallas intermodal customers, we
19 cannot even begin to overcome the difference between
20 going to Atlanta via Shreveport and going to Atlanta
21 via Springfield, Missouri. The NS/KCS agreement
22 locks us out of this market completely.

1 (Discussion off the microphone)

2 MS. KENNEY: But the effect of this
3 restriction does more than eliminate competition for
4 transcontinental and Dallas intermodal traffic. It
5 effectively prevents anyone but NS from offering a
6 host of services between the Southeast and a range of
7 other points west and south of Dallas. Why? Again,
8 because of how an intermodal service must be
9 constructed in order to sustainably meet customers'
10 needs.

11 A basic intermodal service requires a
12 regular trainload volume of at least 200 containers
13 between two railroad terminals to be sustainable.
14 That trainload might be formed at an on-dock
15 terminal for international traffic or by drain from a
16 port or inland shipper to an air-modal terminal.
17 Once this service, which we will refer to as the
18 anchor volume, is established less than trainload
19 blocks can be added on the back of an anchor train.

20 The ability to add these less than
21 trainload blocks allow this core intermodal service
22 to serve shipments in many other geographic markets

1 that only support the movement of less than
2 trainload blocks of container traffic. I'll give an
3 example to illustrate what is at stake. American
4 automotive manufacturers have plants throughout the
5 Southeast, but unlike in the Detroit area, these are
6 not concentrated in a way that can be served via
7 single intermodal hubs.

8 These manufacturers source many of their
9 parts from plants in Mexico that are also not
10 concentrated in a single place. These are some of
11 the customers that have come to us looking for an
12 intermodal rail solution because today they rely
13 heavily on trucking, even for over long distances.
14 But to sustainably serve their needs, we must
15 aggregate their less than trainload shipments onto a
16 West/East anchor train.

17 As I have said, the Los Angeles/Atlanta
18 service we operate today, while suitable for some
19 customers, is too slow for time-sensitive shippers
20 and does not have the geography that would allow us
21 to aggregate Mexico traffic onto the anchor train.
22 NS's exclusivity over the Speedway prevents us from

1 having an West to East anchor train and it prevents
2 us from serving these customers.

3 There is a critical component of this
4 service that I don't want to overlook. I earlier
5 referred to aggregating shipment in interchange with
6 a combination of western carriers and KCS. That
7 aggregation can only occur at an efficiently located
8 interchange point and only if that interchange point,
9 the gateway, is open.

10 For the Meridian Speedway, the natural
11 gateway where this aggregation would occur is at
12 Shreveport, Louisiana, where KCS, UP, and the MS, LLC
13 all meet. If that gateway is not open to efficient
14 interchanges, none of these additional services are
15 possible. It is for that reason we are asking the
16 Board to ensure that the Shreveport Gateway is open.

17 I understand that MS's economist has
18 suggested that CSX cannot have been shutout of
19 southeastern markets because it could compete in them
20 by carrying traffic by truck to and from all points
21 in the Southeast. This is based on the idea that one
22 can efficiently use truck service to serve points

1 within a 500-mile range, then one can simply add
2 500-mile truck movements to the beginning and end of
3 an intermodal rail movement.

4 This is simply not the case. Most
5 intermodal train service between two inland points
6 requires trucks to haul containers to or from a rail
7 terminal. This is called drayage. Intermodal rail
8 is most competitive when rail miles are maximized,
9 and dray miles are minimized. And the cost of
10 drayage in terms of truck costs and delays
11 overcrowded highways is almost always higher than
12 marginal rail costs for movements over 150 miles.

13 A simple analogy demonstrates why. When
14 I go from Jacksonville to New York for business, I
15 have a choice between driving, which takes about 14
16 hours or taking a about a two-hour flight. I usually
17 fly. But when I go to Charleston, which is about a
18 four and a half to an hour drive or an hour and a
19 half-long flight, I often drive. Why? Because the
20 entire airline trip includes the drive to the
21 airport, getting through the airport, flying, getting
22 through the airport again, waiting for a driver or

1 rental car and another drive. It is over a long
2 distance that the shorter flights overcome the
3 disadvantages of flying.

4 The direct and indirect cost of drayage
5 are the intermodal equivalent of all the extra steps
6 involved in flying. An intermodal move is more
7 efficient than truck movements if the drayage costs
8 do not overcome the efficiency of moving large
9 volumes by rail. That is why railroads have so many
10 terminals in highly populated areas so they can get
11 containers as close to their destinations as possible
12 by train rather than rely so heavily on trucking that
13 the advantages of intermodal rail service evaporate.

14 Finally, I believe you heard yesterday
15 the idea that NS's exclusivity, including de facto
16 exclusivity for traffic between Meridian and points
17 east is necessary of NS to recoup its investment. We
18 at CSX are constantly investing in improving the
19 lines we use, and I have to say that is not how we
20 think of recouping those investments.

21 That is when we invest in a rail line, we
22 expect to make a profit by charging for the value

1 provided by that investment; namely, the service
2 provided over that line, not by preventing
3 competition on one side of the line or the other.
4 Here NS's and KCS's joint venture, the MS, LLC, owns
5 an advantageous West/East corridor between the
6 Southwest U.S. and points east.

7 It would make the most money by
8 maximizing the volumes that traverse the MS, LLC's
9 line and differentially pricing that traffic. This
10 is the ordinary business of railroading, and those
11 profits are the ordinary way to recoup investments.
12 But what NS has done here is to agree with KCS to
13 limit the MS, LLC's volume by limiting competition
14 to, from, and over the Speedway.

15 NS has sought to extract the most profit
16 possible, not over the line, but downstream of it in
17 eastern railroad markets where absent restrictions on
18 competition NS would otherwise have to compete
19 head-to-head. NS's strategy to recoup its investment
20 departs from the norm, to say the least. It is not
21 monetizing the line it invested in. It is trying to
22 protect itself from competition east of that line.

1 I'd like to close by saying that we at
2 CSX are passionate about providing the best possible
3 intermodal service to our customers. We therefore
4 strongly urge you to remove the unwarranted barriers
5 to competition to, from, and over the Meridian
6 Speedway. We see no reason removing these obstacles
7 would frustrate investments in the Speedway. On the
8 contrary, removing those obstacles will result in the
9 most efficient and competitively priced services for
10 shippers best served over the Speedway, the most
11 sustainable options over more service lanes for
12 shippers, more economic development, more trucks
13 taken off the highways, and more railroad volumes.
14 Thank you for your attention. Happy to take
15 questions now or hand the presentation over to Mr.
16 Girardot.

17 CHAIRMAN OBERMAN: Let me interject, this
18 is the time -- I don't know if he's here -- we were
19 to hear from the representative from Congressman
20 Omar. Not here yet? Okay. All right, so let's
21 proceed with this presentation and when that person
22 shows up, I promised him we would try to accommodate

1 them because of the congressional schedule.

2 So, does anybody have any questions for
3 Ms. Kenney?

4 (No response)

5 CHAIRMAN OBERMAN: I have one that may
6 actually relate to Mr. Cunningham. In order to
7 impose the condition that you're asking for, do we
8 have to find, as you allege, that the entire
9 arrangement was void?

10 MR. CUNNINGHAM: It's actually not the
11 arrangement that's void. It's the exemption. I
12 misspoke.

13 CHAIRMAN OBERMAN: That the exemption
14 proceeding was void, do we have to do that in order
15 to grant the condition that you're seeking?

16 MR. CUNNINGHAM: Well, I think you'll
17 otherwise be told that this is not the time because
18 it's been around for so long, but that finding is
19 only necessary to get over that hump. It has no
20 legal consequence from our particular standpoint. We
21 are not trying a backwards looking case. We are
22 seeking a forward opening of competition.

1 CHAIRMAN OBERMAN: But do we have the
2 authority to grant the condition you're asking for
3 without ruling one way or the other on the initial
4 exemption?

5 MR. CUNNINGHAM: If you find as we
6 believe is the case and NS seems to believe is the
7 case, the application as its operating plan has been
8 presented, the Applicants' plan has proposed a
9 transaction that would exacerbate these existing
10 conditions and therefore if you find them to be
11 anti-competitive you can impose a condition that
12 requires their removal.

13 CHAIRMAN OBERMAN: Well, you already
14 don't have access to the Speedway, so to give you
15 access would be providing a new competitive option,
16 not remedying the removal of an old one, if I
17 understand.

18 MR. CUNNINGHAM: Well, it would be
19 restoring competition that was present until these
20 agreements were reached. And I don't know if I can
21 answer your question. You might save that for brief
22 as to whether you have to find that the exemption

1 was void in order to do this, but I think you should
2 know that the exemption under your rules was void and
3 I think that you should recognize that this is a
4 continuing harm to competition that shouldn't be
5 perpetuated. That's really important here. It's not
6 about them --

7 CHAIRMAN OBERMAN: That's why I asked the
8 question today because just as in the last
9 presentation within an alleged foreclosure that
10 happened 16 years ago at Laredo, at some point does
11 that become the state of competition which we're not
12 supposed to be remedying old harms in a merger and
13 I'm not strongly I adhere to that doctrine, but it
14 has been the practice of this Board and the ICC time
15 in memorial, as I understand it. And so, I'm trying
16 to put aside for the moment of voidness. There has
17 been no competition here for 16 years is what you're
18 saying and now you're asking us to put in a condition
19 to add competition and that's why I asked the
20 question is there is some legal authority to do that,
21 assuming we fully litigated your contention and we
22 found that the initial exemption was not void, do we

1 still have the authority to grant you the relief
2 you're seeking?

3 MR. CUNNINGHAM: If you found that these
4 are unreasonable restraints on competition, you can
5 condition the transaction on the removal of that in
6 order to protect the public interest, particularly,
7 since, as we believe, the transaction will
8 exacerbate those conditions.

9 Harm to competition is not something that
10 the Board has previously had to deal with in this
11 sense. You did not have vertical and horizontal
12 foreclosure together by agreement between two
13 railroads that previously were competitors and
14 foreclosed competition at the gateways.

15 That's a very different case. I think I
16 agree with Member Hedlund that this is a case of
17 first impression in that sense, but if you feel
18 constrained to not rely on the exacerbation
19 doctrine, but you can find that these are not lawful
20 agreements because they were never exempted or
21 approved by this Board.

22 The difference would be if you had

1 approved merger conditions and they turned out to be
2 not as satisfactory as they were expected to be, you
3 might say I'm not going to change those conditions or
4 I will look into them again in that merger doctrine,
5 but this is not -- pardon me. I have a highly
6 radiated throat apparently gives up on me -- not
7 apparently, it actually gives up on me every now and
8 then because I want to talk too much.

9 The point is that these are restraints on
10 competition that were never sanctioned by the Board.
11 They were never examined by the Board, and they are
12 ongoing and they are causing a great deal of public
13 harm and they're foreclosing tremendous
14 opportunities, as Ms. Kenney just explained, for the
15 development of markets that have not been developed
16 because of this.

17 Your conditioning authority is to ensure
18 that a transaction is consistent with the public
19 interest and if you do not find that carrying them
20 forward is consistent with the public interest,
21 notwithstanding that your general predilection and I
22 think wise predilection of the agency not to reopen

1 anything anybody can complains about, you are
2 entitled under the law to condition the transaction
3 on the removal of those harms and we'll be briefing
4 this as well. I'm very confident of that legal
5 proposition.

6 CHAIRMAN OBERMAN: Is what you're asking
7 for something different from the opening gateway
8 commitments that others are asking for?

9 MR. CUNNINGHAM: Yes. Because these are
10 agreements between parties to restrain competition.
11 Typically, gateway restrictions, which would also
12 need to be eliminated here in order to make the
13 removal of the exclusivity arrangements effective,
14 are imposed as they are in this case, I believe is
15 one exception, not by agreement, but by one carrier,
16 KCS.

17 CHAIRMAN OBERMAN: All right. I think
18 the witness that we had talked about is here.
19 Michelle has one question.

20 BOARD MEMBER SCHULTZ: Real quick. If
21 the transaction is approved without your requested
22 condition what, if anything, would prevent you from

1 seeking up to revoke the 2006 exemptions.

2 MR. CUNNINGHAM: Well, we'd be seeking,
3 but it's not clear once you find that a transaction
4 as proposed -- and remember these agreements are part
5 of the proposal -- they're cited approving by Mr.
6 Obensmeyer, by Mr. Brooks. NS thinks they should be
7 continued, obviously, and extended.

8 If they are necessary to the transaction,
9 then they are immune from all other law, which means
10 they'd suddenly be immunized from antitrust attack,
11 which I don't believe they are today because they
12 were never -- they are today exempt because you have
13 jurisdiction, but if you were to find that they were
14 exempted, then the antitrust laws would apply to them
15 and that's a nest that nobody had to sort out in one
16 of these cases yet.

17 CHAIRMAN OBERMAN: Well, not to overuse
18 your own image, but it sounds to me like CSX has put
19 all of its eggs in this basket and will rise or fall
20 on whether the merger is approved --

21 MR. CUNNINGHAM: We're not asking that at
22 all.

1 CHAIRMAN OBERMAN: -- as distinguished
2 from filing a separate piece of litigation last year
3 before this merger was even considered.

4 MR. CUNNINGHAM: Well, we weren't aware,
5 to my knowledge, of these distinctions.

6 CHAIRMAN OBERMAN: No, here you said when
7 I --

8 MR. CUNNINGHAM: Yes, this is the place
9 where you can fix both. You have the power.

10 CHAIRMAN OBERMAN: But as I said, you're
11 putting all the eggs in this basket.

12 MR. CUNNINGHAM: No, I haven't said that.
13 I said I would seek --

14 CHAIRMAN OBERMAN: You seem to be.

15 MR. CUNNINGHAM: But we are very
16 concerned that you would sanction these and
17 perpetuate them.

18 CHAIRMAN OBERMAN: All right. Let's
19 break here for a moment, don't go far.

20 All right, we are going to hear now from
21 Mr. Gbadamosi. You are here. Please have a seat.
22 Okay. Proceed Mr. Gbadamosi.

1 MR. GBADAMOSI: Good afternoon. Yes.
2 Hello. My name is Akolade Gbadamosi. I am a Senior
3 Community Representative for Congresswoman Iihan
4 Omar, and I am here to testifying on her behalf.
5 Unfortunately, Congresswoman Omar was unable to be
6 today and ask that I relay this statement to you all.

7 I want to thank the Surface
8 Transportation Board for taking testimony on this
9 important topic. This proposed merger between
10 Canadian Pacific and Kansas City Southern has
11 generated a lot of alarm from my constituents and for
12 the State of Minnesota.

13 If the proposed merger moves forward
14 Canadian Pacific Headquarters will move out of my
15 district in Minneapolis to Kansas, Missouri. This
16 will result in a direct loss of 207 jobs and an
17 estimated \$15 million of wages will be lost and
18 transferred out of Minnesota.

19 Concerned residents and local elected
20 officials in my district have been actively
21 considering what could be done to make up for these
22 economic losses. They have asked me to bring their

1 ideas to the STB. My colleagues across the
2 Mississippi River, Congresswoman Betty McCollum of
3 St. Paul has done the same and we both share a common
4 message for you.

5 The best opportunity for the STB to
6 mitigate jobs loss and spur economic growth in
7 Minneapolis and St. Paul is also the easiest for the
8 railroad to say yes to. I'm referring to the four
9 corridors of Canadian Pacific Rail right-of-way,
10 which could be repurposed in ways that benefits
11 hundreds of thousands of our constituents.

12 Minneapolis is very proud for its record
13 in maximizing the economic benefit of Rails to
14 Trails projects far beyond the public health
15 benefits, which are already substantial. In my
16 district, the Midtown Greenway is a nationally
17 recognized bike and pedestrian corridor which boasts
18 not just incredible recreational and commuting use
19 but delivers a direct economic impact that is an
20 unparalleled development tool.

21 More recently, our neighbors in St. Paul
22 have developed the New -- Trail which is just over

1 the Mississippi River from the Midtown Greenway.
2 These two trails could be connected by unused
3 railroad right-of-way. Doing so would greatly
4 enhance the utility of both trails and better serve
5 both Betty McCollum's constituents in St. Paul and my
6 constituents in Minneapolis.

7 There's never been a time more right than
8 this to connect these two trails that will connect
9 the two largest cities in the State of Minnesota far
10 beyond a recreational amenity these unconnected
11 trails have become a key transportation corridor that
12 create important access for thousands of people every
13 day. The opportunity must be seized.

14 Our challenge is not a physical one. The
15 bridge over the Mississippi River was built for two
16 railroad tracks and now only has one. It has plenty of
17 space for a bike pedestrian trail, the primary
18 impediment to make the crucial connection between
19 Minneapolis and St. Paul has been the inability to
20 motivate CP Rail.

21 The filing I submitted to the STB
22 included a letter from nearly two dozen elected

1 officials in Minneapolis and St. Paul articulating
2 these concerns and highlighting the desire to
3 preserve the four Canadian Pacific rail corridors for
4 public use. Transitioning these corridors to public
5 entities would be one way to help offset the impact
6 this proposed merger would have in lost jobs.

7 Preserving these corridors for public use
8 would be great opportunity to generate proven
9 economic development that future generations of
10 Minnesotans will be able to benefit from. Thank you
11 for your time and attention to this very important
12 issue and I hope you will take these testimonies
13 you've heard over the past three days and many more
14 days now into great consideration. Thank you.

15 CHAIRMAN OBERMAN: Thank you and we
16 appreciate your coming here and I think a
17 representative of the Sierra Club was here also
18 talking about the same issue and cited the work
19 they've done with Congresswoman Omar on this concern, so
20 thank you very much.

21 MR. GBADAMOSI: Thank you.

22 CHAIRMAN OBERMAN: Any questions?

1 (No response)

2 CHAIRMAN OBERMAN: All right. Appreciate
3 it. Give the Congresswoman our regards.

4 MR. GBADAMOSI: Will do. Thank you.

5 CHAIRMAN OBERMAN: Thank you. All right,
6 if we could ask CSX to come back up. My hungry
7 colleagues have reminded me I said we were going to
8 break for lunch, 1:15, we'll break for half an hour,
9 be back at 1:45.

10 (Whereupon, at 1:15 p.m., a lunch recess
11 was taken.)

12 CHAIRMAN OBERMAN: Could you tell me as
13 concisely as possible what are the facts that you say
14 render the exemption void ab initio? What is it that
15 rendered it void?

16 MR. CUNNINGHAM: The exemption was
17 rendered void ab initio because the transaction
18 presented did not qualify for that exemption,
19 principally, because it changed the competitive
20 balance in the industry. And as I said in my
21 prepared remarks, whether you look at it the way NS
22 does, it enhanced a changed competition positively or

1 as we do it changed it negatively, it had an effect.

2 CHAIRMAN OBERMAN: Is it your contention
3 that the Applicants for the exemption mislead the
4 Board?

5 MR. CUNNINGHAM: I'm not making any
6 contention if they did. I'm saying what did not
7 qualify as presented.

8 CHAIRMAN OBERMAN: Well, I'm trying to
9 get at how this came about. Was it the Board simply
10 underperforming its duties completely erroneously on
11 its own without any help from anybody or was it
12 something that the Applicants failed to disclose or
13 deceived the Board about? That's usually the kind of
14 allegation when somebody argues that an action was
15 void.

16 MR. CUNNINGHAM: They characterized it as
17 an intra-corporate transaction, and it did not
18 qualify as an intra-corporate transaction.

19 CHAIRMAN OBERMAN: They?

20 MR. CUNNINGHAM: They, being KCS. Only
21 KCS got the exemption. They did not apply for that.

22 CHAIRMAN OBERMAN: So, you're saying they

1 submitted a false statement to the Board, is that
2 what you're saying and that's a separate question
3 whether you --

4 MR. CUNNINGHAM: I think --

5 CHAIRMAN OBERMAN: Well, let me be clear.
6 I'm separating out the question of whether something
7 was done intentionally. The first question is, is it
8 your contention that what was submitted to the Board
9 was false. Second question is, do you contend that
10 it was intentionally false, I guess.

11 MR. CUNNINGHAM: I can say having only
12 stumbled into these provisions myself, not having set
13 out to find them, that they were well hidden as to
14 their effect.

15 CHAIRMAN OBERMAN: What was hidden?

16 MR. CUNNINGHAM: The restraints, the
17 vertical and horizontal restraints were not obviously
18 in a --

19 CHAIRMAN OBERMAN: Well, I'm having --
20 this is the reason I asked the question.

21 MR. CUNNINGHAM: Okay.

22 CHAIRMAN OBERMAN: Let me be clear here

1 so you can answer it because I tried to remember what
2 you had told us while I was having lunch. You say
3 that it was characterized as an intra-corporate
4 transaction and it wasn't, but that was false or not
5 correct. Now, you're also saying that restraints on
6 trade were not disclosed, is that a separate
7 allegation?

8 MR. CUNNINGHAM: No. That's a fact that
9 they were not focusing on the competitive impact.

10 CHAIRMAN OBERMAN: Wait. I'm trying to
11 get basic facts, Mr. Cunningham.

12 MR. CUNNINGHAM: The basic facts --

13 CHAIRMAN OBERMAN: What was wrong that
14 leads you to say that it was void ab initio, can you
15 be very specific.

16 MR. CUNNINGHAM: Yes.

17 CHAIRMAN OBERMAN: Okay.

18 MR. CUNNINGHAM: They did not qualify for
19 an exemption and second --

20 CHAIRMAN OBERMAN: That's a legal
21 conclusion. The facts I'm asking you, what was filed
22 with the Board that was wrong on paper that was sent

1 to this Board.

2 MR. CUNNINGHAM: They asserted that it
3 qualified for an exemption that could not be granted
4 through a transaction that changed competitive
5 balance.

6 CHAIRMAN OBERMAN: What did they say?

7 MR. CUNNINGHAM: They said this is a
8 intra-corporate transaction totally within KCS.

9 CHAIRMAN OBERMAN: And you're saying that
10 is a false statement.

11 MR. CUNNINGHAM: Yes. Because it did
12 change the competitive balance, just like this --

13 CHAIRMAN OBERMAN: Well, now, wait a
14 minute. That's two separate points. It's either
15 corporate, intra-corporate or it's not.

16 MR. CUNNINGHAM: It's intra-corporate,
17 but it does not qualify --

18 CHAIRMAN OBERMAN: Was that a true
19 statement that it was an intra-corporate transaction?

20 MR. CUNNINGHAM: No, it was not.

21 CHAIRMAN OBERMAN: Well, I'm trying to
22 get somewhere.

1 MR. CUNNINGHAM: That's a long step way
2 down. That's what I'm getting at.

3 CHAIRMAN OBERMAN: I'm just trying to get
4 fact by fact. The legal conclusions I will worry
5 about in a moment, if ever, but I need to know what
6 the facts are that you are saying caused this to be a
7 void ab initio transaction, so please tell us with
8 specificity.

9 MR. CUNNINGHAM: The facts are that it
10 changed the competitive balance and did not qualify.

11 CHAIRMAN OBERMAN: No, that is a
12 conclusion, sir. I want to know the facts of what
13 was filed here.

14 MR. CUNNINGHAM: This is what was filed,
15 this pile of paper. This is the public record.

16 CHAIRMAN OBERMAN: And you're referencing
17 a three-inch stack of documents.

18 MR. CUNNINGHAM: I am.

19 CHAIRMAN OBERMAN: Okay. What is it
20 about that that was false or inaccurate or lead to a
21 void ab initio.

22 MR. CUNNINGHAM: I'll read this to you,

1 Mr. Chairman. I'm sorry. I'm too slow. I'm not
2 grasping your question.

3 CHAIRMAN OBERMAN: Let me say this, read
4 something. I'm not going to let you read 300 pages.

5 MR. CUNNINGHAM: No, no, no, I think the
6 Notice of Exemption -- KCS, the Kansas City Southern
7 Railway Company and the newly formed Meridian
8 Speedway, LLC, parties, hereby submit this notice
9 pursuant to 491180.2(d)(3) for an exemption on the
10 prior approval and authorization requirements of the
11 Surface Transportation Board of a transaction within
12 a corporate panel.

13 BOARD MEMBER FUCHS: What's the date on
14 that?

15 MR. CUNNINGHAM: That date is -- it was
16 filed, I believe, it was received January 17, 2006.

17 BOARD MEMBER FUCHS: All right, I'm
18 looking at that and that notice has an extensive
19 discussion last year NSR approached KCSR. Next
20 paragraph, KCSR and NSR announced an agreement for a
21 series of transactions. NSR will be the sole
22 provider. Next paragraph, duh-duh-duh-da. I mean NS

1 is documented throughout the notice.

2 MR. CUNNINGHAM: It is not documented as
3 changing.

4 BOARD MEMBER FUCHS: Please.

5 CHAIRMAN OBERMAN: Let's let Mr.
6 Cunningham talk.

7 BOARD MEMBER FUCHS: There you go.

8 CHAIRMAN OBERMAN: Go ahead.

9 MR. CUNNINGHAM: So, they submitted this
10 and on its face, it changes the competitive balance
11 and did not qualify.

12 CHAIRMAN OBERMAN: What does it say that
13 you say is false?

14 MR. CUNNINGHAM: That it qualifies for an
15 intra-corporate transaction exemption under
16 1182(d)(3).

17 CHAIRMAN OBERMAN: And you're saying it
18 didn't qualify.

19 MR. CUNNINGHAM: It does not qualify,
20 yes.

21 CHAIRMAN OBERMAN: And the reason you say
22 that it doesn't qualify is because -- ?

1 MR. CUNNINGHAM: It changed the
2 competitive balance.

3 CHAIRMAN OBERMAN: By?

4 MR. CUNNINGHAM: By the series of
5 arrangements changing who gets to handle traffic and
6 who doesn't.

7 CHAIRMAN OBERMAN: All right. And all of
8 those arrangements --

9 MR. CUNNINGHAM: Pardon me.

10 CHAIRMAN OBERMAN: Are all of those
11 arrangements described in that thick book that was
12 filed with the Board?

13 MR. CUNNINGHAM: Well, the thick book
14 describes them if you can find them.

15 CHAIRMAN OBERMAN: Are all of the
16 arrangements that you say changed the competitive
17 balance part of that book --

18 MR. CUNNINGHAM: Yes.

19 CHAIRMAN OBERMAN: -- that you say was
20 filed?

21 MR. CUNNINGHAM: Yes.

22 CHAIRMAN OBERMAN: It's in there?

1 MR. CUNNINGHAM: Yeah.

2 CHAIRMAN OBERMAN: So, nothing was
3 withheld from the Board as to the nature of the
4 transaction.

5 MR. CUNNINGHAM: Except that they
6 presented it --

7 CHAIRMAN OBERMAN: Please answer the
8 question I put, otherwise, we're going to be here for a
9 very long time.

10 MR. CUNNINGHAM: I don't know whether
11 it's withheld. We'd have to go through --

12 CHAIRMAN OBERMAN: I thought you said
13 when you discovered all of this you or somebody at
14 CSX investigated it. Somebody read the book.

15 MR. CUNNINGHAM: I read the book, yes,
16 and that's how I determined that it was so
17 restrictive of competition.

18 CHAIRMAN OBERMAN: That's my questions.

19 MR. CUNNINGHAM: Pardon?

20 CHAIRMAN OBERMAN: Is what's in the book
21 the arrangements.

22 MR. CUNNINGHAM: They were all there.

1 CHAIRMAN OBERMAN: They were all
2 disclosed to the Board.

3 MR. CUNNINGHAM: They were published.

4 CHAIRMAN OBERMAN: What you say is false,
5 I take it, is the descriptive language by the
6 Applicant of what they were filing.

7 MR. CUNNINGHAM: And -- yes.

8 CHAIRMAN OBERMAN: So, that's what you're
9 saying.

10 MR. CUNNINGHAM: Right.

11 CHAIRMAN OBERMAN: So, you're saying they
12 described what they filed inaccurately, but they
13 filed the actual stuff.

14 MR. CUNNINGHAM: Filed the actual stuff,
15 that's how we found it.

16 CHAIRMAN OBERMAN: Well, we have a very
17 professional staff here and I can assure you one of
18 the reasons our cases take so long is that we have
19 people who read and study that stuff and I have no
20 reason to think they didn't read and study it in '06.
21 They might not have. I wasn't here. But based on
22 the experience I've had here I fully expect that

1 someone or more people on this staff reviewed this
2 before the Board acted.

3 MR. CUNNINGHAM: They may have, we don't
4 know.

5 CHAIRMAN OBERMAN: Well, I'm going to
6 assume it until somebody tells me that the people
7 here weren't doing their job. I've never seen that
8 happen.

9 MR. CUNNINGHAM: I don't know whether
10 they were doing their job or not, sir. A member of
11 the Bar before this Board said that this was a
12 transaction that qualified.

13 CHAIRMAN OBERMAN: I understand that, but
14 you -- if it didn't qualify.

15 MR. CUNNINGHAM: It didn't qualify.

16 CHAIRMAN OBERMAN: If it did not qualify,
17 Mr. Cunningham, let me finish please, all of the
18 information to determine that it did not qualify was
19 filed with the Board in that book because that's all
20 the information on which you conclusion that it
21 didn't qualify.

22 MR. CUNNINGHAM: I did.

1 CHAIRMAN OBERMAN: And the Board had all
2 of that information at the time.

3 MR. CUNNINGHAM: It did.

4 CHAIRMAN OBERMAN: So, (A) other than
5 what you describe as an inaccurate conclusory
6 description of the filing, I am not hearing that the
7 Applicants did anything to mislead the Board with
8 the underlying papers of what the nature of the
9 transaction was; is that a fair statement because
10 they filed it all.

11 MR. CUNNINGHAM: Well, I don't know
12 whether -- the fact that they filed it may or may not
13 have mislead the Board.

14 CHAIRMAN OBERMAN: Well, let me say this,
15 they filed -- you're telling me that they filed every
16 piece of paper that described the underlying
17 transaction which you say resulted in a restraint of
18 trade.

19 MR. CUNNINGHAM: I don't know.

20 CHAIRMAN OBERMAN: They didn't leave
21 anything out as far as you know.

22 MR. CUNNINGHAM: Well, they were

1 redacted, so they did leave some things out.

2 CHAIRMAN OBERMAN: Well, there's a public
3 and a confidential filing, but -- well, I think you
4 said that everything that's in the filing that's in
5 front of you was sufficient information for you, as
6 an experience lawyer, to conclude that the cover
7 paper was not accurate; is that a fair statement?

8 MR. CUNNINGHAM: Yes, that is a -- .

9 CHAIRMAN OBERMAN: Is that a fair
10 statement, okay.

11 MR. CUNNINGHAM: -- as -- my
12 determination.

13 CHAIRMAN OBERMAN: Yes. So, assuming
14 that the Board staff is just as smart as you.

15 MR. CUNNINGHAM: Probably, yes.

16 CHAIRMAN OBERMAN: I'm going to make that
17 assumption for purposes of this question. I haven't
18 given you or anybody else an IQ test. The Board
19 staff presumably could have figured out what you
20 figured out.

21 MR. CUNNINGHAM: Might have, I don't
22 know.

1 CHAIRMAN OBERMAN: Yeah. But they had
2 the same material in front of them. Correct?

3 MR. CUNNINGHAM: Yes. This went into
4 effect three days earlier.

5 CHAIRMAN OBERMAN: But then,
6 nevertheless, the Board acted or approved the
7 exemption, however you want to describe it.

8 MR. CUNNINGHAM: Pardon me, sir. No one
9 approves an exemption. As you stated in a later
10 case, this is not precedent.

11 CHAIRMAN OBERMAN: No, no, they allowed
12 the exemption to go into effect. I can tell you --

13 MR. CUNNINGHAM: Yes, they did.

14 CHAIRMAN OBERMAN: -- when that happens in
15 my experience, we have to decide are we allowing
16 exemptions to go into effect, so in effect, we are
17 acting perhaps by enacting, but it doesn't just
18 happen out in the ether. Somebody has to say this is
19 or does not qualify for an exemption.

20 MR. CUNNINGHAM: They don't release it.

21 CHAIRMAN OBERMAN: I'm just telling you
22 how things work around here.

1 MR. CUNNINGHAM: Okay. I don't know how
2 they worked in '06. I'm sorry.

3 CHAIRMAN OBERMAN: Well, I don't know how
4 they worked in '06 either. Here's one thing I can
5 tell you, this Board's been here a long time. If I
6 have any frustrations with the Board and its staff is
7 that we do things the same way all the time, so I
8 have to believe we're still doing that.

9 MR. CUNNINGHAM: I understand.

10 CHAIRMAN OBERMAN: And by the way, I
11 don't mean to disparage the staff. They do a good
12 job at it. It's a lot of things we do there's good
13 reason to keep doing them the say way. There are
14 some that I'm sure staff will tell you the Chairman's
15 disrupting the apple cart, but that's not in these
16 proceedings.

17 So, I'm just trying to get at what
18 happened here.

19 MR. CUNNINGHAM: That's what happened.
20 They filed this and 30 days later it went into
21 effect.

22 CHAIRMAN OBERMAN: Yeah. I got it.

1 MR. CUNNINGHAM: All right.

2 CHAIRMAN OBERMAN: So, you are saying --
3 you haven't yet told me anything other than a
4 superficial descriptive statement of what the
5 transaction was that the Applicant did wrong.

6 MR. CUNNINGHAM: Pardon me, sir. There's
7 a presumption that when someone files a Notice of
8 Exemption that is a class exemption as this is, that
9 it qualifies because you'll rely on the
10 representations of counsel that they do qualify. On
11 the face of it, it's clear to me from what the
12 investigations I've been able to conduct that that
13 was assumed across a broad range, and I happen to
14 have been there at the time for another client who
15 didn't care about the competition, but wanted their
16 problem looked at. We never looked into
17 arrangements, and we never second-guessed the
18 proposition that it qualified for an exemption.

19 CHAIRMAN OBERMAN: Well, you're trying to
20 second-guess it now and I'm trying to get at the
21 bottom of it.

22 MR. CUNNINGHAM: I am.

1 CHAIRMAN OBERMAN: So, I'm still trying
2 to figure out who did what, but as far as I can tell
3 the Board had all the information it needed to
4 determine whether this qualified for an exemption and
5 the Board's action, in effect, was to allow the
6 exemption to take effect, so the Board must have
7 concluded that it did and all I am getting at I'm
8 trying to get the essence of your claim is that the
9 Board would have to decide that the Board itself on
10 the basis of having all the information it needed
11 made a wrong decision. I'm not saying that that's
12 true or not true. I'm really trying to dissect the
13 nature of your claim.

14 MR. CUNNINGHAM: The Board itself in the
15 Michigan Central case said that this did not stand as
16 precedent for justifying restrictions.

17 CHAIRMAN OBERMAN: That's not what I'm
18 talking about. I'm trying to find out what the claim
19 is so I can then figure out what, if anything, we're
20 going to do about it.

21 MR. CUNNINGHAM: The claim is--

22 CHAIRMAN OBERMAN: Your claim is, is that

1 the Board should not have granted this exemption.

2 MR. CUNNINGHAM: It doesn't grant
3 exemptions.

4 CHAIRMAN OBERMAN: Well, should not have
5 allowed the exemption to go into effect. That's what
6 your claim is and as to whether anybody did anything
7 that was malignant your claim is the filers
8 misrepresented in their cover language the nature of
9 the transaction, but they actually provided the Board
10 with the actual facts of the transaction so the Board
11 could figure out for itself whether it was
12 misdescribed; wouldn't that be a fair statement?

13 MR. CUNNINGHAM: No. Because that's not
14 the point. The point is --

15 CHAIRMAN OBERMAN: I'm sorry. I'm not
16 asking you what the point is.

17 MR. CUNNINGHAM: Your Honor, if I
18 could --

19 CHAIRMAN OBERMAN: I am asking you --
20 (Parties talking over each other)

21 No, I'm sorry. I want you to respond to
22 what I ask you.

1 MR. CUNNINGHAM: I can't answer that
2 question.

3 CHAIRMAN OBERMAN: Well, then tell me you
4 can't answer it, don't make an argument.

5 MR. CUNNINGHAM: I'm not making argument.

6 CHAIRMAN OBERMAN: Yes, you are.

7 MR. CUNNINGHAM: I'm pointing out, as the
8 Board later said in a decision referring back to
9 this, something is reviewed by the Board.

10 BOARD MEMBER FUCHS: Marty, I just have
11 to jump in here.

12 CHAIRMAN OBERMAN: Go ahead, Patrick.

13 BOARD MEMBER FUCHS: I just want to make
14 sure we're all working off the same set of facts.
15 The intra-corporate transaction that you're referring
16 to is a continuance in control, right? And that's a
17 continuance in control because that was just one of
18 the three exemptions in this case because it's KCS
19 and the Meridian Corporation, but there were two
20 other exemptions, right?

21 MR. CUNNINGHAM: Yes, trackage rights.

22 BOARD MEMBER FUCHS: And NS was one of

1 the trackage rights and KCS was one of the trackage
2 rights.

3 MR. CUNNINGHAM: That's not what we're
4 complaining about.

5 BOARD MEMBER FUCHS: I understand. I'm
6 only saying that the whole intra-corporate and that
7 whether or not NS was poorly disclosed the entire
8 agreement was filed in the Notice of Exemption on the
9 continuance of control. If it says intra-corporate
10 it's not because anyone was hiding that NS was
11 involved. The agreement was filed, NS was documented
12 throughout, NS had its own separate proceeding
13 getting trackage rights, but here's why I have to
14 jump in is because Mr. Cunningham, you're making it
15 seem like it just took effect after 30 days, but
16 that's not what happened, is it?

17 MR. CUNNINGHAM: I don't know.

18 BOARD MEMBER FUCHS: It's not because CN
19 came in and asked for an extension of time. You
20 represented CN.

21 MR. CUNNINGHAM: I did. That's what I
22 said. We came in and asked to protect CN's rights at

1 Jackson.

2 BOARD MEMBER FUCHS: So, the exemption
3 was going on, CN during the initial 30-day period
4 petitioned for a stay. CSX didn't.

5 MR. CUNNINGHAM: No, it's CN.

6 BOARD MEMBER FUCHS: CN did. CSX didn't.
7 So, it's not like there's this automatic exemption
8 process, there's this fast-moving thing. When
9 someone has concerns during our notice and exemption
10 process, they come in. That's why it's noticed. And
11 CN came in, CSX didn't. And when CN came in, the
12 Board granted CN and all of the parties more time to
13 work out their issues.

14 MR. CUNNINGHAM: They did, and we worked
15 it out.

16 BOARD MEMBER FUCHS: You worked it out.

17 MR. CUNNINGHAM: Operationally.

18 BOARD MEMBER FUCHS: And then there was a
19 separate process on the environmental and it wasn't
20 completed until many months later. The point is that
21 it's not this unstoppable force for the exemption
22 where nobody has any recourse.

1 MR. CUNNINGHAM: We're not claiming that.

2 BOARD MEMBER FUCHS: It's not that anyone
3 claimed that NS wasn't involved. It's not that
4 nobody could find --

5 CHAIRMAN OBERMAN: Slow down. We can't
6 hear you.

7 BOARD MEMBER FUCHS: Sorry, Keith. So,
8 it's not that nobody could've seen any of these
9 provisions.

10 MR. CUNNINGHAM: I'm not saying they
11 couldn't.

12 BOARD MEMBER FUCHS: But it's just to the
13 point that there was this false and misleading
14 statement. The way our exemption frameworks works is
15 that there is a presumption on notices, but that
16 presumption is not -- the nature of the presumption
17 is not absolute. Someone can come in and say the
18 framework by which you said that the Notice of
19 Exemption satisfies the RTP just doesn't apply in
20 this case. It happens all the time. Usually, what
21 people pled is that there's something non-routine or
22 controversial. I mean you see a 400-page document

1 filed, you've got the binder right there, so CSX
2 could've come in and said this is non-routine or
3 controversial and they didn't and so I'm only saying
4 that of course they could've made a case under the
5 RTP. Several of the factors reference effective
6 competition that it did not qualify for an exemption.
7 Just because it's a notice process does not foreclose
8 that opportunity. Obviously, it did not foreclose
9 that opportunity for CN. So, I just want to say that
10 the proceeding is a little bit more complex than was
11 being discussed. CSX had a lot more opportunity than
12 you're leading on.

13 MR. CUNNINGHAM: I didn't suggest anybody
14 CSX and opportunity.

15 BOARD MEMBER FUCHS: But it's not handled
16 in a false and misleading -- if CSX doesn't argue
17 competition when everything is disclosed that doesn't
18 make an Applicant's claim that something is
19 pro-competitive false or misleading. It just means
20 it's an uncontested assertion.

21 MR. CUNNINGHAM: May I read the provision
22 at issue here?

1 BOARD MEMBER FUCHS: Which one, in the
2 exemption?

3 MR. CUNNINGHAM: 232 --

4 CHAIRMAN OBERMAN: Sure. Go ahead.

5 MR. CUNNINGHAM: All right. This is what
6 qualifies, "transactions within a corporate family
7 that do not result in adverse" --

8 BOARD MEMBER FUCHS: That's what was
9 cited for the continuous of control and then D7 was
10 from the trackage rights, but did you read -- read
11 the final rule that implemented that and there's an
12 extensive discussion of the recourse of what happens
13 when something ought not qualify as an exemption.
14 The Board made an assumption that things that met
15 that criteria were categorically okay, but just
16 because they're in that category doesn't mean they
17 have to stay in that category forever.

18 I've been a part of many decisions in
19 which people said, well yes, you narrowly fit that
20 category, but this is non-routine or controversial.
21 That doesn't make what the person cited misleading.

22 MR. CUNNINGHAM: May I finish?

1 CHAIRMAN OBERMAN: Yes, please.

2 MR. CUNNINGHAM: Thank you.

3 "Transactions within a corporate family that do not
4 result in adverse changes in service levels,
5 significant operational changes, or a change in the
6 competitive balance with carriers outside the
7 corporate family." Leaving aside the first two
8 clauses, second of which might apply about changes in
9 operating levels, there was a definite change in the
10 competitive balance with carriers outside the
11 corporate family. The Board at no time addressed
12 those changes. Whether they were ignored or not by
13 other parties they were not addressed, and no
14 scrutiny was given to them. The reason this
15 provision is here is that if there is going to be an
16 effect in the competitive balance it requires
17 scrutiny in a process like this one under 11323. The
18 Board did not at any time conduct that scrutiny. We
19 didn't say that CSX didn't have a chance. We said
20 they didn't.

21 CHAIRMAN OBERMAN: We're going to move,
22 and we aren't going to finish here. I'm just go to

1 -- go ahead, Patrick.

2 BOARD MEMBER FUCHS: Can you give an
3 example of a continuous and controlled transaction,
4 that transaction itself that was not processed under
5 the exemption notice process?

6 MR. CUNNINGHAM: I'm not looking for one,
7 this one was not, and it clearly had an effect on the
8 competitive balance. The Applicants said so.

9 CHAIRMAN OBERMAN: Well, I'm just going
10 to make one more observation, then we're going to
11 move on. And I'm going to give you a chance to brief
12 this. We will not finish.

13 MR. CUNNINGHAM: That's fine.

14 CHAIRMAN OBERMAN: But I will say this,
15 Mr. Cunningham, based on what you've reported to us
16 this morning about how this transaction came to be,
17 the notion that CSX was trying to be part of this
18 deal and got aced out, those are my words, because NS
19 made the deal and NS wasn't told about it, didn't get
20 a chance to participate, and then for 16 years didn't
21 raise a description that this changed the competitive
22 balance when it knew full well it was being excluded

1 from this traffic strikes me as a little bit hard to
2 accept, but I'm going to give you the chance, because
3 everybody will have a chance to write a final brief
4 here, to brief this issue and both fact and law, but
5 I think we've got to move on or we will not finish.

6 MR. CUNNINGHAM: May I, Mr. Chairman, one
7 thing.

8 CHAIRMAN OBERMAN: Yes.

9 MR. CUNNINGHAM: They also did not seek,
10 as I noted in my opening presentation, authority
11 under 11322 for a pooling, which this clearly was, a
12 division of traffic and that is mandatory. They must
13 seek it. If they're going to do it, they must seek
14 authority.

15 CHAIRMAN OBERMAN: Well, you know there
16 were other railroads involved here. I didn't know
17 about CN's asking for time. If people with a lot
18 more at stake, more than Board staff, which has no
19 personal stakes in this, don't see the issue and
20 don't bring it to us to come in 16 years later and
21 say this was all done incorrectly, but I'm going to
22 let you brief it. We've got to move on. We have

1 other witnesses we want to hear from.

2 MR. CUNNINGHAM: Great. Thank you. Mr.
3 Girardot.

4 MR. GIRARDOT: Good afternoon, Chairman,
5 Members. My name is Bob Girardot. I'm CSX's
6 Director of Network Strategy and Analytics. I hope I
7 can contribute to your understanding of how the
8 NS/KCS exclusivity agreements have affected
9 intermodal rail transportation in the United States.
10 Have we got any slides going?

11 CHAIRMAN OBERMAN: Why don't you just
12 tell us the page number because we all have a copy?

13 MR. GIRARDOT: Okay, so page 47.

14 CHAIRMAN OBERMAN: Tell us, Mr. Girardot,
15 how long you've been at CSX.

16 MR. GIRARDOT: I've been at CSX a little
17 over 39 years.

18 CHAIRMAN OBERMAN: How long in your
19 present position?

20 MR. GIRARDOT: In my present role,
21 approximately five years.

22 CHAIRMAN OBERMAN: And before that?

1 MR. GIRARDOT: Well, I've had an awful
2 lot of positions.

3 CHAIRMAN OBERMAN: Well, what was your
4 job in 2006?

5 MR. GIRARDOT: In 2006, I was the
6 Director of Service Design.

7 CHAIRMAN OBERMAN: All right. And since
8 that time what titles have you had?

9 MR. GIRARDOT: I've had Director of
10 Service Design, Director of Port and Rail Relations,
11 and then this title Director of Strategy and
12 Analytics.

13 CHAIRMAN OBERMAN: All right, proceed.

14 MR. GIRARDOT: So, I'd like to make four
15 basic points. First, in 2005, CSX was close to
16 reaching agreements with KCS and BNSF to bring new
17 competition between the Southwest and Southeast
18 using the Meridian Speedway. Second, the NS/KCS
19 agreements foreclosed that opportunity and all the
20 competition, new service lanes, and investment that
21 would have come with it.

22 Third, the Meridian Speedway is a

1 one-of-a-kind asset and the best Southwest/Southeast
2 route. And fourth, addressing this issue would
3 increase competition, bring new service lanes, take
4 trucks off the highway, and benefit the public.

5 To address these points, I'd like to
6 begin with the situation in 2005. Norfolk Southern
7 has had haulage rights over the Meridian Speedway
8 since 2000. As of 2005, though, there were no limits
9 on KCS's own ability to provide service over the
10 Meridian Speedway, an interchange with carriers of
11 its choice on either end.

12 KCS was also free to allow additional
13 carriers to operate over the Speedway via haulage and
14 at the eastern end CSX could connect with KCS at
15 Meridian via haulage arrangement with the MMBR. This
16 brings me to my first point. Yesterday you heard the
17 Meridian Speedway arrangement caused CSX to
18 collaborate with BNSF to carry transcontinental
19 traffic. That's not just wrong, it's backwards.

20 In 2004 and 2005, we at CSX were in
21 active negotiations with KCS and BNSF to increase
22 competition over the Meridian Speedway. That

1 increased competition was not theoretical. CSX's
2 participation in the Meridian Speedway movements was
3 not theoretical. It was imminent.

4 CHAIRMAN OBERMAN: Were you personally
5 involved in those?

6 MR. GIRARDOT: Yes, I was.

7 CHAIRMAN OBERMAN: Okay. Go ahead.

8 MR. GIRARDOT: In 2004 and 2005, by 2004,
9 BNSF was already running multiple Los Angeles/Atlanta
10 trains in interchange with Norfolk Southern via the
11 Speedway. IN 2004, BNSF approached us to handle one
12 or more of these Meridian Speedway trains. The idea
13 was that BNSF would use KCS haulage over the Speedway
14 to reach CSX. This would allow BNSF to pitch CSX and
15 NS against each other to compete for its business
16 head-to-head.

17 We loved that idea. Over the course of
18 2005, I was engaged in intense, highly productive
19 negotiations among KCS, BNSF, and CSX to develop the
20 new joint service that I've just described. That
21 service would have dramatically increased competition
22 by giving shippers more rail options using the

1 fastest and most direct routing between the Southwest
2 and the Southeast.

3 I'll reiterate here that the whole point
4 of the strategy was head-to-head competition between
5 CSX and NS. We did not ask for, BNSF did not want,
6 and we would've never envisioned somehow permitting
7 Norfolk Southern from competing. We just flat out
8 wanted to be able to interchange trains. Further, as
9 Marie Clare just explained, the key to building
10 efficient intermodal service for both trainload and
11 lessen trainload traffic is an anchor volume that
12 will support at least one daily end-to-end run
13 through train. BNSF's LA/Atlanta service would've
14 provided exactly that. Thus, the arrangement would
15 not only enhance competition for transcontinental
16 traffic, but would also permit BNSF, KCS, and CSX to
17 serve a portfolio of smaller volume markets.

18 While volumes between many locations in
19 the Southwest and Southeast, such as Dallas and
20 Florida, are too small to justify a whole train. We
21 could service traffic by adding it onto the
22 underlying BNSF run through train already going

1 between Los Angeles and Atlanta. Similarly, as the
2 train passed through Shreveport, we could add blocks
3 from Mexico destined to other CSX points like
4 Charlotte.

5 Once on the CSX network, the Charlotte
6 and Florida box would be put onto other trains and
7 the anchor train would continue on to Atlanta. This
8 aggregation process allows reliable truck
9 competitive movement of smaller blocks without
10 undermining the service and efficiency of the anchor
11 service.

12 All that was needed to support these
13 synergistic products was to establish the underlying
14 BNSF, KCS, CSX service that we were in the process of
15 negotiating. Simply put, the open Speedway made many
16 competitive options possible through many
17 combinations of interlining and haulage services.
18 We, BNSF, and KCS were actively pursuing these
19 throughout 2005. Then much to our surprise these
20 negotiations were abruptly terminated when NS and
21 KCS announced their MS, LLC joint venture.

22 This is my second point. The NS/KCS

1 agreements foreclosed an immediate increase in
2 competition and quashed any opportunity to develop
3 the additional services to, from, and over the
4 Meridian Speedway that we had been planning.

5 CHAIRMAN OBERMAN: Let me just ask you a
6 question.

7 MR. GIRARDOT: Yes, sir.

8 CHAIRMAN OBERMAN: The statement you just
9 made, quashed any opportunity for competition, when
10 did you become aware of that fact?

11 MR. GIRARDOT: I received a phone call
12 from the gentleman that I was negotiating with and
13 making trains plan with KCS, my counterpart, Waldon
14 Hargate. He called me shortly after the public
15 announcement of the Speedway.

16 CHAIRMAN OBERMAN: What year?

17 MR. GIRARDOT: It was December of 2005.

18 CHAIRMAN OBERMAN: Okay. Thank you.

19 MR. GIRARDOT: So, shortly after the MS,
20 LLC announcement, my counterpart at KCS, Waldon
21 Hargate, called and apologized because the NS/KCS
22 agreement meant that BNSF could no longer connect its

1 LA/Atlanta trains with CSX across the Meridian
2 Speedway. The arrangement we'd spent so much time
3 negotiating would not be allowed under the new
4 agreement. Most of the competitive options that you
5 see up on this slide became impossible overnight.

6 As commercial market developers, we at
7 CSX intermodal recognized that KCS and NS had
8 frustrated our effort to connect with western
9 carriers over the Speedway, although we had assumed
10 they had done so lawfully. This was disappointing
11 for our intermodal business. It was very complex,
12 and I moved on in solving the problem of connecting
13 western carriers with our Southwest network some
14 other way.

15 CHAIRMAN OBERMAN: Let me ask you a
16 question. You said you assumed it was done lawfully.
17 You weren't the only person at CSX who was working on
18 this project before you got this news.

19 MR. GIRARDOT: No.

20 CHAIRMAN OBERMAN: Were any other lawyers
21 from the Counsel's Office working with you?

22 MR. GIRARDOT: No. I know that the

1 president of intermodal at that time, a gentleman by
2 the name of Jim Hurtwick, he was at an executive
3 level working with BNSF and his KCS counterparts. I
4 was working at a lower level. I wasn't working with
5 any attorney on any of this.

6 CHAIRMAN OBERMAN: Did anybody talk to
7 the attorneys after you got this news and say, well,
8 the deal's over? We assume it's legal, any
9 discussion inside CSX?

10 MR. GIRARDOT: I mean I kind of had my
11 nose to the grindstone, which was find the best way
12 to connect with western carrier again.

13 CHAIRMAN OBERMAN: Well, why do you say
14 you assumed it was legal?

15 MR. GIRARDOT: Well, I worked with the
16 KCS folks for many years, and I had a very good
17 relationship with them and felt that they were very
18 straight up people. We did a lot of work together at
19 Kansas City, for example, and so I really didn't have
20 any -- I mean they had been working with me very hard
21 all year long, so I had no reason to imagine that
22 what they were doing was unlawful.

1 CHAIRMAN OBERMAN: Well, nobody else at
2 CSX thought about it or talked about it, to your
3 knowledge?

4 MR. GIRARDOT: No.

5 CHAIRMAN OBERMAN: Go ahead.

6 MR. CUNNINGHAM: He's been working for an
7 entity separate from CSX.

8 CHAIRMAN OBERMAN: Pardon me?

9 MR. CUNNINGHAM: He's been working for an
10 entity separate from CSX.

11 CHAIRMAN OBERMAN: I thought he just told
12 me he had a title at CSX at the time.

13 MR. GIRARDOT: At that time, CSX
14 Intermodal was a separate, independent operating
15 company from CSX Transportation.

16 CHAIRMAN OBERMAN: Well, it was part of
17 the corporate family, wasn't it?

18 MR. GIRARDOT: Yes.

19 CHAIRMAN OBERMAN: It was called CSX
20 something. I mean it wasn't out there in left field.
21 Go ahead with your presentation.

22 MR. GIRARDOT: So, I've been working on

1 that problem ever since, Chairman. This is because
2 of my third point. We agree with Norfolk Southern
3 and the Applicants that the Meridian Speedway is the
4 best route, especially, for intermodal traffic
5 between North American points west of Shreveport and
6 the Southeast. BNSF still wanted to be able to
7 interchange with its choice of Eastern carrier, NS or
8 CSX, but the Meridian exclusivity arrangements meant
9 it could never do so over the Speedway. Instead,
10 BNSF ranged the northern route that you see up on the
11 slide to carry its traffic via Springfield, Missouri,
12 Memphis, Tennessee, the interchange with CSX in
13 Birmingham, Alabama and then operate over haulage via
14 haulage over CSX to Atlanta, Georgia.

15 This route was not what we had planned.
16 NS told you yesterday the Meridian Speedway route
17 takes about 74 hours to get from LA to Atlanta. The
18 Memphis route you see up here on the screen takes
19 about 130 hours and it's less reliable and more
20 costly. As a result, it can only serve a limited set
21 of transcontinental traffic where directness and its
22 advantages are not essential.

1 BNSF diverted one LA/Atlanta train to
2 this route in late 2006. After investments in the
3 route by CSX and BNSF, BNSF diverted a second train
4 in 2007, but unfortunately, that Memphis route could
5 not serve as the anchor route for the integrated
6 services CSX and KCS had planned for smaller markets.
7 It was too circuitous, and it detours around the
8 logical aggregation points of the Meridian Speedway
9 route like Dallas and Shreveport. Without the
10 ability to route transcon traffic over the Meridian
11 Speedway this strategy of linking other smaller
12 markets west of Shreveport with Southeast markets was
13 abandoned.

14 That leaves the BNSF CSX alternative the
15 handicap one trick pony. It provides service between
16 LA and Atlanta, but that service is too sequitur from
17 any customers, and it offers no opportunity to
18 aggregate additional Southwest/Southeast traffic.

19 My fourth point is the consequence of
20 what's happened. The truck markets into which we
21 wanted to introduce intermodal rail competition in
22 2005 have continued to grow. We could've have had

1 many opportunities to take trucks off the highway in
2 those markets, but that will only work if the Board
3 takes down the barriers to effective rail competition
4 that NS and KCS have created.

5 I would like to illustrate with two
6 specific geographies where we see tremendous
7 opportunities that cannot be effectively served by
8 rail because of NS's and KCS's agreement. One
9 intermodal service between Dallas and the Southeast
10 and two, intermodal service for the automotive
11 industry between Mexico and the Southeast.

12 You heard the BNSF testimony earlier
13 today about the Golden Triangle in Mexico where
14 there's this concentration of automotive
15 manufacturing in Mexico. Well, there's a similar
16 concentration of automotive manufacturing that's
17 moved to the southeastern states of Alabama,
18 Tennessee, Georgia, and South Carolina and there are
19 many automotive plants that are there, new
20 automotive plants that are locating there. You just
21 heard the Ford/Volvo Project, for example, locating
22 in Tennessee.

1 So, they have just called out for
2 solutions between Mexico and that automotive
3 production area because there's parts and materials
4 flowing back and forth between those regions in both
5 directions. Unfortunately, it's all moving by truck.

6 CSX's filings and my fellow panelists
7 addressed the closing competition with Dallas and the
8 Southeast by NS and KCS. What I hope jumps out about
9 this is that these are large markets and there's only
10 one rail product serving them, KCS/NS. The reason
11 for this that the same circuitousness of the Memphis
12 route that hamstrings our ability to compete for
13 transcontinental traffic becomes prohibitively
14 inefficient when connecting the much closer cities of
15 Dallas and Atlanta.

16 I think the best illustration of that was
17 Marie Clare's other map which was on Slide 36. The
18 same problem applies elsewhere in Southeast between
19 the Southeast and Atlantic Seaboard. Even though we
20 get many requests for service between the Port of
21 Savannah and Dallas, we cannot provide an effective
22 rail solution via Memphis. This leaves international

1 shippers three options. They can pay for an NS rail
2 service that faces no real competition. If they want
3 the benefit of competing rail carriers, they can send
4 their products all the way to ports on the West Coast
5 or of course they can use truck service, which is
6 what most domestic traffic does.

7 As a result, there's a large, untapped
8 set of markets where we could offer efficient port to
9 intermodal rail service for international traffic and
10 convert domestic volumes off the highway, but only if
11 the Speedway is open through competition. There is
12 great demand to link American auto manufacturers with
13 plants in Mexico by rail.

14 To illustrate, we move tens of thousands
15 of containers of intermodal traffic every year
16 between Mexico and Detroit, but we move virtually
17 zero containers between Mexico and the Southeast.
18 It's all truck. That should give us a sense of the
19 size of the untapped market.

20 We've made many efforts since 2005 to
21 work with KCS, with UP and with FXE to change that
22 fact. The auto industry is desperate for this

1 service, but we cannot provide it unless the Board
2 acts. The problem is twofold. First, without a
3 Speedway routing for transcon trains, we do not have
4 an anchor volume on which to aggregate the Mexico
5 services. With an underlining transcon train over
6 the Speedway, we could construct efficient services
7 between Mexico and the Southeast that would take
8 trucks off the highway.

9 Second, KCS, which has a small amount of
10 Mexico Southeast intermodal traffic seemed to have
11 closed the Shreveport Gateway to UP. UP has a much
12 more tuck competitive route between Shreveport and
13 both Eagle Pass and Laredo. The KCS route from
14 Laredo is roughly a day slower than the UP route and
15 requires long dredge from FXE served points in
16 Mexico.

17 If the Shreveport Gateway were open, we
18 could create services with KCS, FXE, and UP that
19 would convert large volumes of Mexico Southeast
20 automotive traffic off the highway. CSX seeks the
21 opportunity to offer customers a competitive
22 alternative railroad option for movements between the

1 Southeast and the West Coast, Dallas, and Mexico.

2 CSX's vision today is the same vision it
3 had in 2005 and the same one we thought we were about
4 to achieve before NS and KCS agreed to foreclose that
5 possibility. That competition would've greatly
6 benefited the public and it still would today, but
7 this opportunity can never be realized unless the
8 barriers to competition to, from, and over the
9 Speedway are removed. Thank you.

10 CHAIRMAN OBERMAN: Let me ask you, Mr.
11 Cunningham, you have three other people up here. It's
12 a quarter to 3:00. Is there testimony cumulative of
13 what we've already heard?

14 MR. CUNNINGHAM: It's quite different.
15 (Speaking off mike)

16 CHAIRMAN OBERMAN: I mean we've taking
17 all of time questioning you and others, but we have
18 because you've made some pretty serious charges here,
19 but this has gone way beyond what we anticipated for
20 CSX. We have to still hear from Union Pacific, and
21 we have other witnesses, and we have to be out of
22 here at about 5:30, quarter to 6:00, so maybe I can

1 ask the remaining two witnesses to try to briefly
2 summarize.

3 You have statements and there'll be final
4 briefs, so we will have everything you want to tell
5 us.

6 MR. TISCH: Are we able to submit
7 statements in the record?

8 CHAIRMAN OBERMAN: Well, you're able to
9 submit a final brief. If you have written statements
10 that you brought with you and you don't finish them,
11 you can submit them.

12 MR. TISCH: I'll be brief, Mr. Chairman.

13 CHAIRMAN OBERMAN: Okay. All right,
14 proceed.

15 MR. TISCH: My name is Ryan Tisch. I'm a
16 partner at Crowell Morning, LLP and I'd like to
17 explain just a little further how the KCS/NS
18 exclusivity arrangements run afoul of applicable
19 competition principles, as informed by the Federal
20 antitrust laws.

21 The STB considers whether a transaction
22 is consistent with the public interest, including

1 whether the proposed transaction would have an
2 adverse effect on competition among rail carriers.
3 It may also ask whether a proposed division of
4 traffic will not unreasonably restrain competition.

5 The Federal antitrust laws provide an
6 analytical framework the STB regularly applies when
7 asking these questions. Assess under that framework
8 the exclusivity arrangements manifestly and
9 unjustifiably restrain competition for the following
10 reasons.

11 For transcontinental intermodal traffic,
12 the exclusivity arrangements reduced the number of
13 competitors from two to one. And bad as that would
14 be on its own, the arrangements also impose a
15 separate vertical limitation governing the Meridian
16 Interchange. The exclusivity arrangements also
17 ensure NS is the only railroad able to serve
18 transcontinental and Dallas intermodal traffic east
19 of Meridian unless it consents to consents to
20 competition. It never has.

21 You'll hear briefly from Professor Carey
22 and Dr. Shehadeh, these horizontal and vertical

1 limitations on competition have harmed shippers and
2 the public interest gravely, but it didn't have to be
3 this way. The exclusivity we're talking about was
4 not reasonably necessary to secure an investment in
5 the Meridian Speedway that you heard about yesterday.

6 NS's supposed justification that other
7 carriers would free ride on any investment they made
8 is not a magic word. It's a factual claim and it
9 does not withstand scrutiny. What actually happened
10 was that NS knew that competition was imminent, and
11 it paid a large amount of money to avoid that
12 competition. And as I'll explain, again briefly, I
13 promise, it's neither in the public interest nor is
14 it consistent with long-established antitrust
15 standards.

16 So briefly, I'd like to remind the Board
17 the MS, LLC transactions included two related, but
18 distinct elements and this is important. On the one
19 hand, KCS granted MS perpetual exclusivity for
20 transcontinental intermodal traffic and a right of
21 first refusal to carry Dallas intermodal traffic east
22 of Meridian.

1 On the other hand, NS invested \$300
2 million which was used primarily for the improvement
3 of the MSLLC line. One of these elements plainly
4 limits competition, one seeks to expand output. How
5 under prevailing antitrust law and policy do we
6 analyze a transaction that does both? The antitrust
7 law provides a clear answer.

8 If the exclusivity arrangements were
9 reasonably necessary to achieve the output expanding
10 investments NS touts, only then can the investment
11 even purport to justify those restrictions. The
12 analysis is factual. Reasonable necessity cannot be
13 assumed as NS seems to want to do. NS does not
14 engage with the standard at all. It simply calls the
15 MSLLC joint venture pro-competitive because of its
16 investment and the great results, but without an
17 analysis of whether the exclusivity arrangements
18 were reasonably necessary to secure such an
19 investment that is irrelevant.

20 In fact, if you skip the question of
21 reasonable necessity, as the NS is encouraging this
22 Board to do, the logical conclusion of that argument

1 is simply as long as you invest in a line you are
2 allowed to restrict competition in any way that you
3 want, both on and off that line. That is not what
4 the law says. Instead, antitrust law applies the
5 well-established rule of reason.

6 Now, under that framework, first, the
7 component of a given competitive restriction must
8 show it may harm competition, then it's proponent
9 must show that the restriction has a procompetitive
10 justification. And finally, the opponent has the
11 opportunity to show that a less restrictive
12 alternative approach would have accomplished the same
13 procompetitive justification.

14 Each of those is a factual claim that
15 requires examining the evidence and I'll walk through
16 each one in turn. The exclusivity arrangements harm
17 competition for three reasons. The first is the most
18 obvious. In 2005, NS already had haulage rights for
19 transcontinental intermodal traffic and KCS owned the
20 underlining line between Shreveport and Meridian.

21 Either could readily provide the relevant
22 service and at Meridian each could interchange with

1 their choice of carrier. The exclusivity
2 arrangements reduced the number of carriers offering
3 the relevant service over the relevant line from two
4 to one. In antitrust terms, this is a horizontal
5 reduction of competition.

6 NS claims that because KCS had no volumes
7 of transcontinental intermodal traffic at the time NS
8 and KCS "did not compete" for it and the exclusivity
9 arrangements could not harm competition. That is an
10 egregious misstatement of the law. KCS certainly did
11 carry traffic on the Speedway prior to 2006 and KCS
12 was free and able to carry transcontinental
13 intermodal traffic at any time or to grant a third
14 carrier the right to do so, making KCS interline or
15 third-party haulage service, at a minimum, a
16 potential competitor and an important competitive
17 constraint on NS.

18 And in fact, as Mr. Girardot told you, at
19 the time of the agreement KCS was imminently about to
20 do exactly that via an arrangement with CSX and BNSF.
21 Exclusivity was so valuable to NS specifically
22 because it eliminated that imminent competition. The

1 antitrust laws fully recognize this real-world
2 dynamic. And as the Supreme Court held in *Palmer v.*
3 *BRG*, a case where a regional competitor agreed not to
4 enter its joint venture partners other markets,
5 market allocation agreements are anticompetitive
6 regardless of whether the parties split a market
7 within which both do business, however, they merely
8 reserve one market for one and the other for another.

9 NS ignores this law. Instead, it claimed
10 in its briefs that the Supreme Court ruled in the
11 case of *United States v. Topco* that an agreement not
12 to compete is only illegal if it is between two
13 businesses actively competing in the same market.
14 That only underscores NS's error of law. As the
15 Supreme Court later explained in *Palmer*, *Topco*
16 literally says the opposite of that. That is, the
17 agreement in *Topco* was illegal even though the
18 defendants in *Topco* had never competed in the same
19 market. In effect, NS is asking the Board to
20 overrule the Supreme Court in that regard.

21 The second reason the exclusivity
22 arrangements harm competition is, one, NS itself

1 stresses. The Speedway is by far the shortest and
2 most efficient route between the Southwest and the
3 Southeast and indeed the only route that is
4 competitive against trucking. By blocking other
5 carriers' ability to interchange with the more direct
6 Speedway route, NS ensured they could not compete
7 effectively against NS's services over the Speedway.

8 NS responds to that argument with a
9 supposed principle of economics and law. So long as
10 CSX has the ability to provide Los Angeles to Atlanta
11 intermodal services forbidding them from
12 interchanging with the Speedway cannot harm
13 competition. This is simply not the law either.
14 Antitrust law does not that a company may foreclose
15 something the rival needs to compete so long as
16 there's any alternative no matter how disadvantaged,
17 competitively unappealing, or costly. As the D.C.
18 Circuit held in the Microsoft case, it is no defense
19 that a competitor is not completely blocked from all
20 means of serving customers if the defendant has
21 barred them from the cost-efficient ones.

22 The third and final reason that

1 exclusivity arrangements harmed competition you will
2 hear from the other witnesses. Since the exclusivity
3 arrangements were entered prices for services over
4 the Speedway are higher than they would otherwise
5 be, output over the Speedway is lower than it would
6 otherwise be, and services for which there is
7 tremendous demand are impossible deliver.

8 Antitrust law recognizes each of these as
9 proof of harm to competition. So, what does NS say
10 justifies those harms? NS claims that the
11 exclusivity arrangements are justified because they
12 are "narrowly tailored to protect NS's investment."
13 The only substance they provide for this claim is to
14 quote KCS's 2006 statement that NS did not want to
15 invest in the Speedway "unless it could be assured
16 that other carriers would not use the capacity NS's
17 investment would help create."

18 What NS says this 2006 statement referred
19 to is a well-developed concept in the antitrust law
20 called freeriding. Here's how it works. One, NS
21 improves the lines facilities by investing in the
22 MSLLC. Two, that improve confers a benefit to

1 anyone who serves traffic that passes over the line,
2 including third-party carriers that interchange
3 Speedway traffic or have haulage rights. And three,
4 those third-party carriers then charge customers for
5 the improved service, taking the supposed freeride on
6 the NS's investment.

7 So far, sounds so logical, but there's
8 just one problem. That's not how railroads actually
9 work. In reality, the MSLLC would and could charge
10 any interlining customer a factor and any haulage
11 customer a fee and those payments would pass through
12 in Part 2 NS as the MSLCC's co-owner. It is what the
13 MSLLC would, like any owner of an advantaged asset
14 naturally do to maximize the profits of its owners,
15 KCS and NS.

16 And remember NS has management rights to
17 insist that its investment in the MSLLC is
18 appropriately rewarded. Simply put, freeriding is
19 not a magic word. It's a finding of fact and in the
20 real world there's no reason whatsoever that NS would
21 not get paid when carriers interchange Speedway
22 traffic or receive haulage over the line.

1 Now, as courts have explained, when
2 payment is possible freeriding is not a problem
3 because the ride is not free. Freeriding is really
4 only a risk for benefits you can't charge for like in
5 intangibles or complimentary customer assistance.
6 From an antitrust perspective, this is the extreme
7 opposite case and an exceptionally literal one.
8 There is a literal ride, and the ride is literally
9 not free.

10 But faced with this bleak landscape, NS
11 presents to this Board that it actually is res
12 judicata that the exclusivity arrangements are
13 justified because in 2006 the Board considered and
14 approved of the narrow restriction on MSLLC
15 operations to protect NS's significant investment.

16 And as the Board itself has explained, it
17 did no such thing. One year after the Meridian --

18 (Response off mike)

19 MR. TISCH: Happy to. As the Board
20 itself has explained it did no such thing. One year
21 after the Meridian Speedway exemption proceedings the
22 Board explained that the Speedway proceedings could

1 not be relied upon as a precedent because they did
2 not result in a reasons decision. That is, when a
3 party notices an intra-corporate transaction, the
4 transaction is automatically permitted unless
5 objectives are received and trigger an after-the-fact
6 Board review.

7 Because the Meridian Speedway notice was
8 unopposed it simply became effective, no in dept
9 review occurred. To reiterate, the Board has stated
10 definitely that it has never assessed the
11 competitive effects of the Meridian Speedway
12 arrangements at all, so no, the Board has never
13 deemed them justified.

14 BOARD MEMBER FUCHS: Mr. Tisch, I will
15 not reopen our discussion. I will just say that
16 you've pinpointed a couple areas of frustration that
17 I've had with the class exemption framework, which is
18 sometimes the Board says we only do after-the-fact,
19 but then, as in this case, there's a petition for
20 stay and we extend it and the exemption never even
21 takes effect, right?

22 So, if you look at the implementing rules

1 of those regulations, they say, well, come in for a
2 revocation, but in practice oftentimes the exemption
3 doesn't take effect, we just delay it and how that
4 fits under the regulator structure amorphous. Same,
5 Mr. Cunningham with your points about some of the
6 judgment calls that are embedded in regulation, how
7 much weight should the director of proceedings give
8 to judgment calls versus should the Board intervene
9 if it's -- so all I'm saying is that you can pick
10 after-the-fact, but in practice it's not always
11 after-the-fact.

12 MR. TISCH: Right. And I appreciate that
13 point. I don't think it takes anything away from the
14 point I'm trying to make about NS implying that
15 there's been a real consideration of the pro and
16 anticompetitive factors that I'm talking about and
17 those have been sifted all the way through, if you
18 catch my drift, but I do appreciate that input.

19 CHAIRMAN OBERMAN: I've got to urge
20 everybody along. We're not going to finish.

21 MR. TISCH: I'm sorry I'm fighting you
22 here, but two more minutes. I promise.

1 CHAIRMAN OBERMAN: Okay.

2 MR. TISCH: Thus, there's no evidence
3 that the exclusivity arrangements protect NS's
4 investment at all, but even if they did our July
5 comments identified numerous, less restrictive
6 arrangements that NS and KCS could have used to fully
7 protect and ensure a return on their investment. I
8 will not go into them in detail here. I will simply
9 explain that once again NS does not engage with the
10 relevant legal principles at all.

11 NS says first that its investment makes
12 the MSLLC transactions per competitive as a whole, so
13 no less restrictive alternative needs to be
14 considered. This is both circular and a
15 mischaracterization of the law which says that if the
16 exclusivity arrangements are anticompetitive.
17 Considering less restrictive alternatives is part of
18 that analysis. NS's rejection of that framework
19 pretends that more than 100 years of case law doesn't
20 exist.

21 NS says second that because the Meridian
22 Speedway investment was so big these industry

1 standard tools were not practical. This is another
2 factual claim and NS doesn't back it up but follow
3 that claim to its logical end and we're back where we
4 started. If you cut a big enough check any
5 restriction on competition is allowed, regardless of
6 the alternatives. Again, that is not the law.

7 NS makes one more argument, on that is a
8 pure smoke screen. NS argues many carriers use some
9 form of exclusivity to protect their investments, so
10 CSX has nothing to complain about. Here's what NS is
11 referring to, let's remember what a haulage
12 agreement is, it's a host railroad agreeing to carry
13 another railroad's traffic using the host railroad's
14 crews over the host line and traveling in the second
15 railroad's account.

16 That means when a new haulage agreement
17 is reached its effect is typically to increase the
18 number of carriers offering service over the relevant
19 line, usually from one to two. It is not unusual for
20 that kind of agreement to say thou shall not increase
21 this further from two to three. In that situation
22 competition is still increased which is the opposite

1 of what happened on the Meridian Speedway.

2 There is NS's so-called exclusivity
3 directly reduced the number of carriers able to offer
4 the relevant service from two to one. None of the
5 instances of so-called exclusivity that NS referred
6 to in its briefing did that.

7 So, let me sum this up because I don't
8 think anything will make the Board happier at this
9 point, but if none of NS's explanations for the
10 exclusivity arrangements make sense, then what is
11 really happening here? I would close by calling your
12 attention to two key documents from the record. We
13 discussed them in our July comments, and they will
14 appear again in our brief.

15 Because they are highly confidential, I
16 cannot display them here, but they contemporaneously
17 document a very simple answer to the question of
18 what's happening here. NS knew competition over the
19 Meridian Speedway would hurt it, so NS purchased
20 exclusivity specifically to prevent that competition.
21 Dr. Mayo offered you his conclusions about the
22 contemporaneous documents regarding what motivated

1 the Meridian Speedway transaction. It may be
2 instructive that Dr. Mayo told us in his deposition
3 that he did not review these documents. I have 10
4 copies here if the Board would like to review them
5 now or later today. I won't mince words. These are
6 some of the clearest smoking gun documents I've seen
7 in many years as an antitrust practitioner. I urge
8 the Board to look at them closely.

9 In closing, NS has provided no viable
10 justification for these exclusivity arrangements in
11 the course of these proceedings. They knew their
12 business over the Meridian Speedway was at risk and
13 that competition for that business was about to
14 intensify. They could've competed to keep it and
15 bargain to make sure their investments benefited
16 them. Instead, they reached an agreement that
17 excluded competition and did so forever. And unable
18 to defend their anticompetitive arrangements NS
19 offers a grab bag of reasons why this Board cannot
20 reach them.

21 As we have shown, none of those arguments
22 hold up to the barest scrutiny. In fact, they don't

1 engage with the relevant legal principles at all.
2 The only possible conclusion is that NS is counting
3 on the Board to ignore this problem. We urge you not
4 to.

5 CHAIRMAN OBERMAN: Thank you. Mr.
6 Cunningham, what are the other two witnesses going to
7 address?

8 MR. CUNNINGHAM: They're going to address
9 the harms that were created, the economic harms in
10 terms of (off mic) and other harms to the public
11 interest.

12 CHAIRMAN OBERMAN: Because of the amount
13 of time you have been sitting here I am inclined to
14 ask you to step aside so we can hear UP before the
15 day expires and we have several other witnesses who
16 have been moved around and waited patiently and then
17 come back the end of the day and we'll hear as much
18 as we can before we have to leave, unless you tell me
19 it is a very short time.

20 MR. CUNNINGHAM: That's entirely
21 acceptable to us lawyers and I believe to the
22 economists, but our folks from Jacksonville have a

1 great need to take the planes that they have to get
2 them back -- so what's left after the hurricane.

3 CHAIRMAN OBERMAN: So, who are those
4 people?

5 MR. CUNNINGHAM: Those would be the
6 Jacksonville --

7 CHAIRMAN OBERMAN: The people who have
8 already testified.

9 MR. CUNNINGHAM: Right.

10 CHAIRMAN OBERMAN: So, they don't have to
11 stay if they want. I'm not insisting on that, but
12 I'm just really conscious of the fact that you guys
13 have been up here for hours. We've asked a lot of
14 questions, so I'm not saying you're delaying, but we
15 really have a lot of people to hear from. How long
16 are your presentations?

17 MR. SHEHADEH: Well, with your
18 instruction and your citation to the care of staff,
19 I'm happy to do it in five minutes.

20 CHAIRMAN OBERMAN: All right, and the
21 other?

22 MS. CAREY: An I can work until 10 or

1 under.

2 CHAIRMAN OBERMAN: Ten tonight or ten
3 minutes?

4 MS. CAREY: Ten minutes.

5 CHAIRMAN OBERMAN: Okay. Let's try to
6 keep it within that limit, if we can. Go ahead.

7 MR. SHEHADEH: Thank you. So, to keep it
8 short I'm only going to address a few issues that
9 have been raised in the context of the hearing and
10 again rely on my slides and my verified statement for
11 the remainder of my testimony.

12 The core issue that I'm evaluating is
13 whether or not harm to a competitor rose to harm to
14 competition, whether foreclosure of competing traffic
15 over the MSLLC harmed competition. That's what my
16 statement addresses, that's what my slides address.
17 I'll rely on staff for that review. But here I'd
18 like to take a moment to discuss the standard
19 employed by NS in its comments yesterday and if we
20 can go to the next slide.

21 There was repeated citation to what
22 happened in 2005 versus what was going on today.

1 That's a before/after standard. That's not the
2 relevant standard to evaluate the competitive
3 effects of the exclusivity arrangements. The correct
4 standard, as reflected in economics, as reflected in
5 things like the DOJ guidelines, whether the horizontal
6 merger guidelines, vertical merger guidelines.

7 Collaboration among competitor guidelines
8 is to look at what would happen in the absence of the
9 conduct. In the absence here of the exclusivity
10 arrangements, not before/after. So, when we heard
11 Professor Mayo cite to the fact that intermodal
12 traffic had increased from 2005 or '06 to more recent
13 years that is not evaluating the competitive effects
14 of the exclusivity arrangements.

15 Likewise, when we heard citation to the
16 lack or scale of CSX activity in 2005 that's not the
17 right economic standard. What matters and what Mr.
18 Girardot described in detail is the fact that
19 competition was imminent and that those plans related
20 to significant competition. And as Mr. Tisch
21 described, that there was anticipation of the effect
22 of that competition on NS.

1 When one applies that correct standard,
2 that "but for" standard, so when I say "but for" I
3 mean the competition in the absence of the
4 exclusivity arrangements what a proper economic
5 analysis demonstrates is that output was reduced
6 relative to what it would have been with competition.
7 Harm to a competitor, exclusion of a competitor rose
8 to harm to competition.

9 That's my principal conclusion and
10 Professor Mayo's analysis hasn't changed that. In
11 fact, even adopting Professor Mayo's proposal that
12 the entire Southeast should be treated as one
13 geography, even adopting that, the method properly
14 applied demonstrates that there's been a reduction in
15 competition.

16 So, another point that I wanted to raise
17 is how does this -- from an economic perspective only
18 I'm addressing this. How does this relate to the
19 transaction before you, the CP/KCS transaction? NS
20 has already stated that it anticipates the CP/KCS
21 transaction will significantly increase congestion.
22 Now, that's its own anticipation. What does that

1 mean? Well, that anticipation and the anticipation
2 alone increase the likelihood that it will exercise
3 its option for the Dallas intermodal terminal, the
4 Wiley Terminal.

5 Likewise, it increases the likelihood,
6 and likelihood is what matters here because
7 transaction reviews and competition reviews are
8 necessarily predictive. Increases the likelihood
9 that it will exercise its contingent trackage rights,
10 whether those be the contingent trackage rights that
11 it has on the MSLLC line or the requested contingent
12 trackage rights if you grant those as part of its
13 requested remedy.

14 All of those, the exercise of the option,
15 the exercise of those contingent trackage rights
16 cements the anticompetitive effect of the exclusivity
17 arrangements and that's the anticipation as NS has
18 described itself. And the cement, changing that
19 right of first refusal into ownership, exercising
20 those trackage rights would cement that exclusion of
21 competition that arises under the exclusivity
22 arrangements.

1 Again, with that, I will throw myself at
2 the mercy of staff or a review of the slides.

3 CHAIRMAN OBERMAN: I just have one
4 question.

5 MR. SHEHADEH: Sure.

6 CHAIRMAN OBERMAN: All day long I've
7 heard that the 2006 deal was in perpetuity. How can
8 you cement something that's already perpetual?

9 MR. SHEHADEH: That's a great question.
10 So, two things, one in the context of the Dallas
11 intermodal terminal ownership would provide different
12 rights in terms of the ability to expand that, for
13 example, and chose not to expand it than would the
14 right of first refusal that they currently have.

15 Likewise, they do not have today the
16 trackage rights that they're seeking on the Wiley to
17 Shreveport section and if those were granted those
18 would create new rights if they were exercised, at
19 least as my understanding of the NS proposal is that
20 those trackage rights would also be contingent on the
21 exercise of the terminal option.

22 CHAIRMAN OBERMAN: If we reject this

1 merger, CSX is still not getting on this line unless
2 we throw out the entire transaction, the exempt
3 transaction, is it?

4 MR. SHEHADEH: On the DIT Terminal they
5 could have access under the right of first refusal
6 result and the traffic that is covered by that DIT
7 Terminal, for example.

8 CHAIRMAN OBERMAN: Who could have it.

9 MR. SHEHADEH: If under the right of
10 first refusal, NS didn't exercise it, then KCS could
11 provide that service to CSX or to BNSF.

12 CHAIRMAN OBERMAN: But CSX has no right
13 to get it.

14 MR. SHEHADEH: That's correct.

15 CHAIRMAN OBERMAN: That's all I'm saying.

16 MR. SHEHADEH: Right. If I implied that
17 they had a right, this would be KCS providing that
18 service in competition. I apologize if I --

19 CHAIRMAN OBERMAN: So, in terms of
20 worsening CSX's access to any of this, whether this
21 transaction goes through or not is not going to
22 change the current legal restrictions that you're

1 all complaining about unless we find that the whole
2 initial transaction was void.

3 MR. CUNNINGHAM: Or if you found that
4 they unlawfully divided traffic and didn't get
5 approval under 11.

6 CHAIRMAN OBERMAN: Well, that's what I'm
7 talking about. You're going to the initial
8 transaction.

9 MR. CUNNINGHAM: Well, it's a current
10 state. They're still dividing the traffic.

11 CHAIRMAN OBERMAN: I understand. All
12 right. Thank you. Any questions? Proceed, Ms. --
13 say your name for us.

14 MS. CAREY: Julie Carey.

15 CHAIRMAN OBERMAN: Oh, it's Julie Carey.
16 I'm sorry I was looking at the wrong person, but go
17 ahead.

18 MS. CAREY: Good afternoon to all
19 esteemed Board Members. I'm Julie Carey, an
20 economist for NERA Economic Consulting, the
21 substantial railroad economic experience and also an
22 adjunct professor at Georgetown University.

1 My discussion will focus on the public
2 interest ramifications of the CP/KC transaction in
3 the context of the uncommon, perpetual exclusivity
4 arrangements in the MSLLC/JV that create harm to
5 competition and for which substantial benefits are
6 achievable by removing those barriers to competition.

7 Really just setting the stage, the CP/KC
8 transaction, as others have discussed before and will
9 continue after us, has a unique ability to foreclose
10 its competitors related to traffic in Mexico. You
11 combine that challenge of harm of competition which
12 needs commercially reasonable terms and rates, along
13 with very few savings to shippers in the terms of
14 lower rates. So, 81 percent of the public benefits
15 put forth by the Applicants are private benefits,
16 incremental profits in their pocket.

17 With that context, the additional public
18 benefits analysis that I've done associated with the
19 MSLLC/JV in removing the exclusivity arrangements and
20 opening the relevant gateways on the Meridian
21 corridor would add substantially to the public
22 benefits of the transaction.

1 So, turning to the uncommon and harm to
2 competition of immediately shutting the door of
3 substantial competition and denying southeastern rail
4 customers competition, aside from only NS, on the
5 advantaged East/West route have a material impact.

6 Just to clarify the record in a couple
7 ways, here's a slide that show contemporaneous 2005
8 CSX, the merchandized carloads over the MSLLC line
9 interchanging at Meridian between KCS and CSX is
10 evidence that CSXT was historically using the line
11 which is directly contradicted by MS.

12 This slide shows the historical
13 intermodal traffic over the MSLLC line pre-JV,
14 post-JV, and post-JV with Dr. Shehadeh's estimate of
15 what output would've been without the exclusivity
16 arrangements. And I will also note that this slide
17 shows growth, but much less growth than the over 300
18 percent that MS represented yesterday, more along the
19 lines of 30 percent growth from 2006 to 2019.

20 So, my work in this case was to look at
21 the nature of the MSLLC/JV exclusivity arrangements.
22 And to do that this is an underlining haul service,

1 so I did detailed research for examples of haulage
2 service, I looked at analyzing actual traffic flows
3 over those segments, and through all of my work I
4 identified no examples of a host railroad removing
5 itself from competition, i.e., no longer providing
6 that underline/interline railroad service, none in
7 existence.

8 So, with that effect resulted in NS being
9 the only option for shippers needs for traffic
10 movements over this important and advantaged line.
11 My opinion is confirmed by CSX, as you heard from,
12 and notably, NS identified no like-for-like examples.

13 So, to respond to NS's claim of
14 procompetitive benefits and to justify the perpetual
15 exclusivity arrangements, I looked at the economic
16 efficiencies associated with that JV transaction and
17 found them lacking. They had the same type of
18 service and similar service requirements post-JV as
19 they did before.

20 There were no cost reductions from the
21 new JV haulage versus the pre-JV haulage that would
22 reduce the markup over variable costs and spur lower

1 rates to shippers. Therefore, I concluded the type
2 of efficiency gains often anticipated for vertical
3 transactions are absent in this case.

4 Other claims by NS's experts of
5 procompetitive benefits similarly are misplaced.
6 It's written on the slide. I'll let you read that at
7 your leisure.

8 Now, turning to the resulting competitive
9 harm, the perpetual exclusivity arrangements were
10 substantially detrimental to shippers in the
11 Southeast railroad market for traffic over the
12 advantaged route. These shippers had no opportunity
13 to negotiate with the railroad that we know applies
14 competitive pressures to the benefit of the shippers,
15 even if they don't get that traffic.

16 I conducted a railway rate benchmark
17 analysis that shows that the shippers using the
18 NS/Meridian route today have less competition and
19 less competitive rates than alternative CSX or NS
20 routes for the same origin/destination move. As I
21 will discuss shortly, my rigorous econometric rail
22 rate analysis reaffirmed my rate benchmarking

1 analysis. NS's expert provides no quantitative
2 analysis that otherwise explains the substantial
3 premium of the NS/Meridian rates.

4 To further evaluate competitive harm, I
5 also conducted market share analysis for the relevant
6 Dallas and transcontinental intermodal traffic moves.
7 The analysis shows high proportions for NS and raises
8 concerns of market power. I used a railroad specific
9 market share to compare like-for-like competitors
10 that are best able to constrain each other on these
11 long-haul intermodal traffic moves.

12 In response, NS raises two particular
13 issues. First, arguing that I should not treat BNSF
14 as a distinguished single-line competitor separate
15 from CSX/TSNS. The BNSF traffic into Atlanta from
16 the West Coast is in BNSF's waybill account as a
17 single move.

18 BNSF has economic control of this traffic
19 with the ability to restrict output and influence
20 price. CSXT is simply a service haulage provider and
21 a single-line service in this context is a distinct
22 rail service and competitor because it's compared to

1 CSXT and NS.

2 Second, NS's expert argued for rail and
3 truck combined market shares. That approach
4 artificially understands market shares by assuming
5 that any and all trucks compete with rail. And as
6 you've heard earlier, there are a myriad of best
7 possible conditions that are required for rail to
8 compete with a subset of trucks. That highlights the
9 importance of understanding the rail-only market
10 shares which is commonly used and presented in
11 analysis such as I've conducted.

12 This slide presents a summary depiction
13 of my historical analysis of substantial NS earnings
14 on its exclusivity intermodal traffic movements for
15 shippers in eastern railroad network. My economic
16 analysis includes a conservative estimate of NS's
17 contribution margin and demonstrates that NS's 300
18 million initial investment has been well recouped.

19 Based on my financial analysis and other
20 work, no procompetitive economic rationale existed to
21 justify the MSLLC exclusivity arrangements in the
22 past, and even if there was some reason it existed in

1 2006, there's no reason today, tomorrow, and
2 certainly not perpetually into the future.

3 There are tremendous potential public
4 benefits available from opening the Meridian corridor
5 and removing exclusivity arrangements. I conducted a
6 detailed analysis. I quantified those total benefits
7 from shippers receiving competitive rail rates and
8 more trucks off the road.

9 Other factors on the slide before were
10 not all incorporated. I conservatively estimated as
11 high as 50 million annually to shippers from
12 increased rail competition over the line from trucks
13 off the road, including Mexico. The opportunity of
14 benefits is conservative, it's a 2019 study, volumes
15 have increased, and I haven't included all of the
16 eastern railroad market opportunities that exist in
17 unserved or underserved markets.

18 My public benefits estimate is based on a
19 rigorous regression analysis of rail competition and
20 quantify the shipper benefits from removal of the
21 exclusivity arrangements and opening the corridor. I
22 used a large and comprehensive set of actual

1 intermodal moves. I presented six different
2 scenarios of my analysis to ensure my conclusions
3 were economically reliable and robust. I evaluated
4 the impact of railroad competition under numerous
5 scenarios, including various number of routes,
6 carrier alternatives, as well as number of railroad
7 competitors at interchange locations.

8 I countered and included a myriad of
9 railroad economic factors and under ally scenario
10 studied the consistent and reliable conclusion
11 emerged that Meridian shippers would benefit from
12 more rail competition and routes and interchanges.

13 To be clear, I'm not advocating
14 competitive access or open access to the last mile
15 solution. I'm focusing my work on removing the
16 barriers of unlawful, closed advantaged East/West
17 corridor and the reduction in competition that raises
18 alarming economic concerns.

19 In response to my analysis, NS's expert
20 appears to misunderstand or misconstrue it as single
21 scenario, which it's not. I did six scenarios.
22 Also, since my regression analysis takes into

1 account additional route options, i.e., any and all
2 pathways between an origin and destination, NS's
3 experts claim that Memphis is good enough and no
4 public benefits will be foregone by continuing with
5 the exclusivity arrangements is flatly contradicted
6 by my detailed analysis. I specifically isolated and
7 quantified that the shipper benefits and lower rates
8 from additional route options.

9 And with that, I'll conclude my remarks
10 and turn it back over for a summary to Paul or answer
11 any questions that arise.

12 CHAIRMAN OBERMAN: I take it that if I
13 listen to your praise for the benefits to shippers
14 for more competition, is it fair to say NS is
15 comfortable with foreclosing competition that
16 currently is deemed lawful. You just don't like this
17 foreclosure or competition; is that a fair summary of
18 CSX's position?

19 MS. CAREY: Well, I'm not a lawyer. I'm
20 not speaking to the --

21 CHAIRMAN OBERMAN: No, I understand, but
22 you talked about unlawful foreclosure. There's lack

1 of competition throughout the entire country,
2 including places where NS -- CSX has the opportunity
3 to open its gateways and they came forward in the
4 PanAm transaction, but only there because they were
5 asking for our approval, so it was a rhetorical
6 question.

7 Mr. Cunningham, I can't conceive that you
8 have anything more to add, so we'd like to conclude.

9 MR. CUNNINGHAM: I have a request, if I
10 may.

11 CHAIRMAN OBERMAN: Make it please.

12 MR. CUNNINGHAM: The request is that all
13 parties who have signed the Protective Order be
14 entitled to see any highly confidential materials
15 that have been submitted by other parties' teams.

16 CHAIRMAN OBERMAN: Well, I don't think we
17 could respond to that off the top of our heads, so
18 we'll take it under advisement.

19 MR. CUNNINGHAM: Thank you very much.

20 CHAIRMAN OBERMAN: All right. Thank you.
21 And I particularly want to note that the CSX
22 employees from Jacksonville braved through the

1 elements to get here, and we really appreciate the
2 fact that you did and were able to get here and to
3 hear from you. And I didn't mean to rush everybody,
4 but as you can see, we're having trouble getting
5 through this proceeding, so we really need to hear
6 everybody else, but thank you much all of you for
7 being here and for your presentation.

8 MR. CUNNINGHAM: And if you'll allow my
9 concluding remark. Thank you very much for you
10 giving us the time to make this case.

11 CHAIRMAN OBERMAN: You're welcome, sir.

12 MR. MEYER: Rather than burdening
13 the record with written correspondence, I thought
14 just a response to what Mr. Cunningham said a moment
15 ago about opening up the entire highly confidential
16 record to anyone who signed the Protective Order
17 implies that every internal relevant person who
18 signed the Protective Order would see all of
19 Applicant's highly confidential material and we
20 strenuously object. A Protective Order protects
21 that material and there's a procedure within the
22 Protective Order for declassifying if that were

1 required.

2 CHAIRMAN OBERMAN: Make a more formal
3 request, Mr. Cunningham.

4 MR. CUNNINGHAM: I shall.

5 CHAIRMAN OBERMAN: Ten-minute break and
6 we'll ask UP to be ready to go. We're going to be
7 out of here and so we're not going to get done.
8 Thank you.

9 (Recess)

10 MR. ROSENTHAL: Good afternoon, Chairman
11 Oberman and Members of the Board. My name is Michael
12 Rosenthal. I'm outside counsel for Union Pacific
13 Railroad Company. I'm here today with John Turner,
14 Union Pacific's Senior Vice President of the Herman
15 Dispatch Center Network Planning.

16 Union Pacific opposes an unconditioned
17 merger of CP and KCS. I'm going to provide a brief
18 overview of Union Pacific's position and a more
19 detailed discussion of Union Pacific's
20 competition-related concerns. Mr. Turner will then
21 discuss UP's service-related concerns.

22 So, Union Pacific opposed an

1 unconditioned merger of CP and KCS for two reasons.
2 First, an unconditioned merger would likely cause a
3 significant loss of competition, particularly, for
4 traffic moving via the Laredo Gateway between the
5 United States and Mexico.

6 Applicants have acknowledged this is a
7 valid concern and they've tried to address it here by
8 promising to keep existing gateways open on
9 commercially reasonable terms, but they admit that a
10 simple promise would be essentially unenforceable
11 because no standard exists for determining whether
12 gateway rates are commercially reasonable. And he
13 quote up there is what they told us when we sought
14 discovery trying to find information to see whether
15 they discriminated.

16 The Board didn't define commercially
17 reasonable in its 2004 Tex-Mex decision. There are
18 no metrics, no dollar caps, no rule by which we could
19 determine at this later date and with full hindsight
20 where a particular rate is commercially reasonable
21 without wild speculation, so UP is asking the Board
22 to impose a simple rule for setting commercially

1 reasonable gateway rates as a condition if it
2 approves the merger.

3 If a shipper asks, KCS must allow it to
4 use a mileage-based pro rate of its single-line rate
5 to create an interline rate. The calculation would
6 be straightforward and transparent so there would
7 never be any disputes for the Board to resolve. And
8 to ensure that the remedy protects competition and
9 not CP/KC's competitors, shippers will control the
10 decision to request a gateway rate and information
11 about the rate and it's really the same remedy that
12 was requested by the National Industrial
13 Transportation League, the American Chemistry
14 Council, and the Fertilizer Institute.

15 Our second concern is that Applicants
16 haven't committed to fund investments in all the new
17 capacity needed to implement their proposed merger,
18 particularly, where they'd operate over UP's lines
19 between Robstown and Beaumont, Texas, which includes
20 the Houston Terminal. These lines are critical to
21 the Applicants' plans for cross-border traffic, but
22 the Applicants failed to analyze operations over

1 those lines in their application.

2 After UP highlighted the omission, the
3 Applicants tried to fill the gap in their reply,
4 leaving n opportunity under the procedural schedule
5 to address their new evidence and Mr. Turner will
6 address some of the problems with the Applicants'
7 reply evidence here, but what Applicants really seem
8 to be saying is that capacity on those lines is UP's
9 problem, not theirs.

10 Now, UP isn't going to ask the Board to
11 resolve disputes over needed investment. UP is
12 asking the Board to require the Applicants to bear
13 responsibility for the cost created by their merger
14 and to do that so that UP, BNSF, and the customers we
15 serve aren't required to subsidize their merger.

16 Specifically, we're going to ask the
17 Board to require Applicants to work with UP to
18 identify the investments needed to accommodate their
19 planned traffic growth, to fund the investment, and
20 not to increase operations until sufficient capacity
21 is in place.

22 So, let me turn back to the competition

1 issues. As I've said, Applicants have acknowledged
2 the concern over the rates CP/KC would charge for
3 traffic that would move over existing gateways is a
4 valid one. If the Board follows precedent, it will
5 impose a condition intended to keep gateways open on
6 commercially reasonable terms. The question is
7 whether the condition will be concrete and
8 enforceable.

9 No one disputes the public interest in
10 protecting competition at existing gateways. In this
11 case parties have focused in particular on the Laredo
12 Gateway, and I don't think anyone disputes the
13 importance of the Laredo Gateway to the economic, in
14 general, or the success of the proposed merger, in
15 particular.

16 There's also no dispute that CP/KC will
17 be under significant pressure to divert Laredo
18 traffic from UP, KCS, and BNSF/KCS interlining
19 service to single-line CP/KC service. If CP/KC
20 succeeds by offering better service or rates that
21 would be procompetitive, but if they capture traffic
22 by foreclosing competition from BNSF and UP north of

1 Laredo that would be anticompetitive and contrary to
2 the public interest.

3 Now, Applicants say their vague,
4 unenforceable promise to keep gateways open on
5 commercially reasonable terms is fine because there's
6 no genuine risk of competitive harms. They say that
7 UP's evidence presented only an abstract theory of
8 harm, but the Applicants are really the ones here who
9 are relying on a abstract theory. The Board calls it
10 the one lump theory. And applied the Laredo Gateway
11 the theory is that KCSM, KCS's Mexican affiliate,
12 already squeezed every last drop of monopoly profit
13 from cross-border business, so CP/KC can't extract
14 anymore.

15 Dr. Steven Salup, an economist who
16 submitted testimony for UP, explained that the one
17 lump theory doesn't apply in the situation here where
18 the upstream monopolist, KCSM, and the downstream
19 rivals, for example, CP and UP, lack full information
20 about each other's costs and prices, or when the
21 rivals provide service that shippers view as
22 qualitatively different. Again, conditions that we

1 see here.

2 He explained that in these circumstances
3 the monopolists generally can't extract the full one
4 lump, so the shipper retains a surplus and the
5 existence of that surplus gives the monopolist an
6 incentive to engage in anticompetitive conduct to
7 capture the surplus.

8 Now, Dr. Salup didn't just talk about
9 theory, he took the Applicants actual data and
10 analyzed it using an approach that the Department of
11 Justice talks about in their vertical merger
12 guidelines, and he used that to show that foreclosing
13 competition would be a profitable strategy for a
14 merged CP/KC.

15 UP's Chief Marketing Officer, Kenny
16 Rocker, provided evidence that substantial volumes of
17 traffic that the Applicants plan to divert have no
18 alternative to Laredo, that truck, water, and other
19 gateways aren't a realistic alternative. So, UP's
20 evidence showed that CP/KC would have both the
21 incentive and the ability to foreclose competition
22 north of Laredo.

1 Now, the Applicants really don't address
2 UP's evidence, apart from noting a few situations
3 where shippers could use alternative gateways. Apart
4 from that, they really don't analyze the facts in
5 this case. They don't address the vast amounts of
6 traffic that don't have alternatives. Their evidence
7 is almost entirely focused on KCS's acquisition of
8 Tex-Mex back in 2004.

9 Dr. Salup explained that the Applicants'
10 analysis of the KCS/Tex-Mex data is inconclusive, at
11 best, because it doesn't address what shares would've
12 been in the absence of a merger. He also explained
13 that the analysis really isn't just inconclusive,
14 it's also irrelevant because a CP/KC transaction
15 would create greater incentives to engage in
16 anticompetitive conduct than a KCS/Tex-Mex
17 transaction. Again, the Applicants really don't
18 address the facts in this case.

19 In the end, we don't think that the Board
20 needs to resolve the dispute between economists or
21 among economists in this case. The Applicants
22 proposed a gateway condition. The Board has

1 generally committed to protecting competition at
2 gateways. So, the real question is whether
3 Applicants' promise is sufficient or whether more
4 must be done to make a gateway condition effective.

5 So, UP has proposed a remedy. It's a
6 simple rule really for making Applicants promise to
7 charge commercially reasonable rates concrete and
8 effective. The point is where a CP/KC single-line
9 route competes with an interlining route that
10 includes a former CP, KCS, or KCSM segment, and where
11 the shipper asks, then CP/KC must provide a Rule 11
12 rate that reflects a mileage-based pro rate of the
13 single-line rate so the customer can use that to
14 create a competitive interline alternative.

15 The feature we think is important here
16 about UP's proposal is that all the control is placed
17 in the hands of the shippers which ensures again that
18 the condition protects competition and not
19 competitors. So, shippers decide whether to request
20 gateway rates from CP/KC, shippers receive the
21 gateway rate from CP/KC, the railroad UP or BNSF or
22 whoever wouldn't get that rate. Shippers can easily

1 check whether the rate is calculated correctly. It's
2 a mileage-based rate. Shippers have access to tools
3 like PC Miler.

4 And then, ultimately, it's the shipper
5 that decides whether to come to UP or another carrier
6 and ask us to quote a rate that can be used to form
7 an interline rate. Again, it's essentially the same
8 remedy proposed by NIT League, ACC, and TFI.

9 So, Applicants, of course, criticized
10 UP's proposal. They say it would benefit UP and hurt
11 shippers, but I don't think that NIT League, ACC, and
12 TFI would be pressing for a condition that they
13 thought would hurt their members. The Applicants'
14 main criticism seems to be that divisions in the
15 marketplace aren't strictly mileage based and there
16 are three problems with that criticism.

17 First, Mr. Rucker's verified statement
18 and other evidence in the record show that railroads
19 do use mileage pro rates in their commercial
20 dealings, not always, but they use them in
21 agreements, and you've heard about the I-5 Agreement,
22 which is essentially a large mileage pro rate system.

1 Second, the Applicants own data shows what looks to
2 me like a strong relationship between a railroad
3 share of mileage and its share of revenue.

4 They put up those highly confidential
5 charts that I can't show you because my witness can't
6 see them, but if you look it looks like a pretty good
7 linear relationship to me. It's not perfect, right,
8 but it comes to my third point, which is that
9 Applicants don't offer a better solution.

10 They also claim that UP's proposal would
11 transfer revenue to UP where the current KCSM
12 division is greater than the KCSM milage share and
13 that criticism is misguided for several reasons.
14 First, it's a distraction from the main issue. The
15 main issue is that absent a remedy CP/KC will have
16 the incentive to raise rates on the KCSM segment
17 which would allow it to divert traffic to CP/KC's
18 single-line routes and raise its single-line rates.
19 UP's remedy is designed to preclude this tactic and
20 protect customers, allowing them to benefit from
21 competition on the merits between UP, BNSF, and
22 CP/KC.

1 Second, the Applicants' claim ignores the
2 nature of the remedy. They talk about taking money
3 from KCS, KCS had been putting in Applicants'
4 pockets, but UP's remedy isn't affecting pre-merger
5 rates and pre-merger arrangements. It's affecting
6 new rate quotes.

7 And then, third, the Applicants' claim
8 relies on the faulty assumption that UP would know
9 when the use of a mileage based pro rate would
10 require KCSM to reduce the divisions it would
11 otherwise charge. As Mr. Rucker testified, UP almost
12 never knows KCSM's pre-merger divisions. They're
13 Rule 11 confidential rates, so UP isn't going to know
14 when the application of the pro rate might cause KCSM
15 to reduce its division.

16 So, what's really going to happen in a
17 post-merger world? In a post-merger world that
18 includes this remedy UP would expect CP/KC to set
19 low, competitive, single-line rates to try to divert
20 traffic to new CP/KC single-line service. That
21 competition is going to prevent UP from raising its
22 division.

1 Shippers will benefit from the
2 competition, rates will be lower, CP/KC also is very
3 easily able to benefit from its transaction because
4 if its single-line service is superior to our
5 service, as they claim it will be, then CP/KC isn't
6 going to collect just this KCSM division. It's going
7 to collect the whole rate. It's going to make more
8 money at the end of the day.

9 The Applicants' economist also tries to
10 attack UP's proposed remedy by claiming it would
11 create an incentive for CP/KC to raise rates to
12 offset some potential reductions in KCSM's
13 divisions, but that claim is inconsistent with the
14 Applicant's reliance on the idea that KCSM is already
15 squeezing every last drop of profit out of a
16 transaction. So, if Applicants are abandoning that
17 position now, well, that's all the more reason to
18 worry and to adopt a concrete gateway remedy.

19 Ultimately, Applicants real concern with
20 UP's proposed remedy appears to be that it would
21 defeat their ability to exploit market power gained
22 through this transaction to raise rates above

1 pre-merger interlines rates or to divert traffic to
2 their single-line service, even if shippers would
3 prefer an interline service that would hurt customers
4 and that's what UP's proposal protects against.

5 Before turning it over to Mr. Turner, I
6 was going to say a few words about the Laredo Bridge,
7 but if you want to --

8 BOARD MEMBER FUCHS: I'm wondering if
9 before we get into the Houston portion of the
10 presentation whether or not it makes sense to stop
11 and ask about gateways.

12 MR. ROSENTHAL: If I could go to the
13 Laredo Bridge because it's a gateway issue. UP has a
14 request for a condition affirming its right to use
15 the new international railroad bridge that KCS has
16 announced for Laredo. We think our right to use the
17 new bridge on equal terms with CP/KC flows from the
18 Applicants commitment to abide by the conditions
19 imposed on the KCS/Tex-Mex merger.

20 In approving that merger, the Board
21 required the Applicants there to abide by a number of
22 promises KCS regarding KCSM and KC's operation of the

1 bridge. That it won't change the basic structure in
2 operations of KCSM, except through negotiations and
3 all carriers will be treated fairly at the bridge and
4 that it won't make unilateral changes in the way the
5 bridge is dispatched and operated. And the Board
6 imposed all these promises as conditions to guarantee
7 that traffic will continue to flow fairly and
8 efficiently at the Laredo Bridge and through the
9 gateway. So, we think UP's access to the new bridge
10 is essentially upholding the guarantee that traffic
11 will continue to flow freely and fairly through the
12 gateway.

13 UP thought it had an understanding with
14 KCS that UP would have access to the new bridge under
15 the same terms as the existing bridge. Applicants
16 are now saying something different, and we think the
17 Board can help avoid future disputes by affirming
18 here CP/KC's obligations under the KCS/Tex-Mex
19 conditions or simply ruling as a way to protect
20 gateways that UP should have equal access to the
21 bridge.

22 BOARD MEMBER FUCHS: Thank you. I'm

1 wondering, particularly, to UPSP, but in past mergers
2 does Union Pacific have newly created bottlenecks out
3 of those mergers that were not conditioned?

4 MR. ROSENTHAL: UPSP was generally a
5 different type of merger. It was more of a
6 horizontal merger. I think there were some
7 bottleneck-type issues raised with respect to some
8 individual coal facilities where SP served the plant
9 and UP served the mine, and it became UPSP. I don't
10 think there was anything of the sort that we're
11 looking at here where the two carriers were the only
12 two carriers or one carrier was the only carrier on
13 one side of the gateway and merged with SP. I think
14 there were alternatives in those situations, so I
15 think the general answer is nothing like what we've
16 seen here.

17 BOARD MEMBER FUCHS: It seemed to me just
18 in reviewing the record in past mergers, and I'll
19 just use UPSP, but I think here are others in other
20 mergers. I think International Paper in that merger
21 suggested that there were a number of gateways,
22 particularly, actually on KCS that then connected to

1 SP and then Union Pacific had other routes that
2 created vertical foreclosure. And it seemed to me
3 that Union Pacific had a bit of the opposite
4 position in that proceeding.

5 So, the first question is, factually,
6 whether or not that's accurate and I know there are a
7 lot of conditions flying around in that proceeding,
8 so it could be that some of those gateways were
9 addressed in other conditions. But based on my look
10 at it, it did seem that there are a number of
11 unconditioned, newly created bottlenecks across your
12 mergers, and I'm guess I'm sort of wondering because
13 you raised the empirical question whether or not UP
14 foreclosed those gateways.

15 MR. ROSENTHAL: So, as I said, I mean I'm
16 trying to remember. International Paper I remember
17 having an issue with access maybe to short lines who
18 were connecting to some roads or another. I don't
19 remember all their issues, but as I said, the coal
20 shippers do stand out. And I will say what Dr. Salup
21 says, and I don't want our position to be taken
22 wrong.

1 One, we're not saying that there are
2 always going to be problems with vertical
3 transactions. What a lot of Dr. Salup's work was,
4 was to say, hey look, you shouldn't have a
5 presumption that just because you have vertical
6 merger, you're fine, there are no anticompetitive
7 problems. And he did his analyses and a bunch of
8 computer program model simulations and so there's a
9 range of results. And there's certain things that
10 matter to the results.

11 So, one thing he found important, if you
12 look at the pattern of results he set up, is a lot of
13 times it matters what the share is of the railroad on
14 the other side of the transaction where you have low
15 shares, low pre-merger market shares by one of the
16 competing railroads.

17 So, like CP doesn't really do much of the
18 Chicago auto area, the Chicago intermodal area,
19 that's a cause for concern. Another very important
20 thing is what sort of efficiencies is the merger
21 creating that could offset the anticompetitive
22 incentives to raise rates. And so, you look at

1 something like UPSP where when you look at the
2 benefits -- and maybe you can argue -- I don't want
3 to get into a fight about UPSP, but there was
4 consolidation. There was route consolidation, there
5 were savings, there were operational efficiencies
6 through shorter routes.

7 There were a lot of, I think,
8 undisputable public benefits or at least what the
9 Board would count as a public benefit and those sort
10 of merger-specific benefits, the existence of those,
11 make the foreclosure pressures less because they help
12 you lower your costs and compete.

13 So, if you look at these sort of one-off
14 shipper situations, it's not that there's one carrier
15 with a lot of competition and then two on the other
16 hand. It's a real one-to-one and it's kind of 100
17 percent/100 percent. So, it's not a difference in
18 market share.

19 Now, like I said, there were a lot of
20 efficiencies that went along with the UPSP merger,
21 and we did rate studies for years afterwards show the
22 savings and what actually happened at the two-to-one

1 locations.

2 This merger, on the other hand, has
3 really very low efficiencies and we've got a
4 statement in there by Tom Hailey who goes through
5 that and that's another reason to be concerned. So,
6 part of it is the market shares of the railroads.
7 Another is the real, what we think a lack of
8 merger-specific efficiencies that makes us concerned
9 about this transaction where you might not be
10 concerned about something like UPSP.

11 BOARD MEMBER FUCHS: No, I appreciate
12 that. I'm yet to hear -- because I do see these
13 vertical foreclosure issues being raised merger,
14 after merger, after merger, and then the same theory
15 is being relied on and I'm yet to see a railroad ever
16 in the empirical analysis admit to foreclosing. So,
17 it could be that maybe the five or six gateways that
18 were mentioned by International Paper were never
19 foreclosed, but in terms of empirical analysis, it
20 never seems to make its way to the people who
21 benefited from not having a proper mechanism not
22 applied to them and so what I'm cognizant of, of CP's

1 claims being like, well, we've got our own
2 regulatory regime just for us, right?

3 Now, that's in the context of rates
4 overall, but it's also that it's just for their
5 particular gateways, not to say that that undermines
6 the merits. It's just to say that how you UP
7 performed when they had the opportunity to vertically
8 foreclose something might be indicative of how CP
9 might. But you're right, individual gateways are
10 different, depending on the circumstances.

11 MR. ROSENTHAL: And again, I think Dr.
12 Salup was careful to say he's not saying all vertical
13 transactions are one way or another way. It does
14 depend on the evidence. It does depend on the facts.
15 And as I said, I don't remember -- I feel bad. I
16 was probably there. I probably responded to their
17 concerns.

18 BOARD MEMBER FUCHS: No, it's okay.

19 MR. ROSENTHAL: But I don't think we had
20 -- and John would know the network better. I don't
21 think we had anything like this sort of situation
22 where -- again, there are places where a shipper may

1 have had SP and UP combined, but not in the same way
2 that --

3 (Parties speaking over each other)

4 BOARD MEMBER FUCHS: I think an example
5 would be like I think there was a Mansfield plant in
6 IP that could go directly to St. Louis or could go
7 over to Shreveport onto KCS and then on SP up to St.
8 Louis, but that could be wrong. It's a decision that
9 was a long time ago, but that's an example. Where
10 all of a sudden now, the Shreveport to St. Louis
11 route that's foreclosed IP claimed because UP can get
12 you directly to St. Louis.

13 MR. ROSENTHAL: Except I think in the
14 UPSP merger, if we had UP coming in one way and SP
15 coming in another way that would've been a two-to-one
16 location and there would've been a remedy as part of
17 the UP merger. So again, I'm not sure what the IP
18 situation was, but in that kind of situation where
19 one route out was on UP, one route out was on SP that
20 was actually addressed by conditions in the UPSP
21 merger. That was the two-to-one condition, so they
22 may have gotten relief. I just don't remember IP at

1 this point.

2 BOARD MEMBER FUCHS: That would be great
3 if past performance of UP in vertical foreclosure
4 situations might shed light on the issue. The one
5 other thing I wanted to mention was just I wanted to
6 give you an opportunity to respond to my questions
7 of BN about whether or not the prop rate mechanism is
8 really appropriate for traffic that is higher on the
9 competitive spectrum, let's say.

10 If CP/KC is constrained by the
11 marketplace in their topline interline rates whether
12 or not it's really appropriate for the Board then to
13 break out that on a mileage basis for revenue
14 divisions.

15 MR. ROSENTHAL: So, I mean I think it's
16 difficult to really sit and parse traffic, right? I
17 mean their promise was a broad-based gateway
18 protection promise and what we've tried to do is come
19 up with a broad-based solution. I think even when a
20 rate is constrained by the market, assuming it's
21 constrained by the market, as I think their expert,
22 Dr. Reicher said, it's not like you go a dollar

1 higher and something goes to truck, right? There's
2 a range of motion, so I'm not sure that a dollar
3 higher it goes to truck, so you don't need to worry
4 about rail.

5 Even if that existed, even if there were
6 rates that rail rate goes up a dollar it goes to
7 truck, so you don't need to worry about UP. KCS's
8 rates are being constrained by truck, by water, by
9 something else. It would be really hard to identify
10 those and try to carve those out of a solution. So,
11 the question is what's the harm of our remedy and I
12 don't think there is a harm, and I don't think that
13 NIT League and ACC and TFI would be in here if they
14 thought there was a harm.

15 What may happen is, again, maybe KCSM's
16 division goes down, but that money is going to go to
17 a shipper, right?

18 BOARD MEMBER FUCHS: No, I don't think so
19 because -- so if there's the market rate and that's
20 the topline interline rate, what strikes me is that
21 there could be situations where the rate would go
22 down if there were vertical foreclosure, but you

1 don't have that opportunity if you're not a
2 monopolist if the underline rate is constrained by a
3 lot of competition in the marketplace.

4 So, all that would happen is you all
5 would be subsidized by CP/KC. I'm not saying that it
6 can't go the other way, but without getting into
7 highly confidential information, you raised the point
8 that the correlation isn't perfect, so there will be
9 situations where a mileage-based rate does not
10 reflect a market-based reality of revenue division.
11 And I don't think anyone is claiming that revenue
12 divisions are only based on mileage or else the
13 correlation would be 100 percent, okay.

14 So, if that's the case and CP/KC doesn't
15 have pricing power, when that error rate is under the
16 line graph, all of that variation in the revenue
17 division between what the market would do and what
18 the mileage-based rate would be would just be pure
19 subsidy to UP because the topline rate wouldn't
20 change, just the revenue divisions would.

21 MR. ROSENTHAL: I guess I don't
22 understand how it's subsidy to UP. It's only a

1 subsidy to UP if UP is going to make some extra money
2 on this and UP is never going to know when it can
3 make extra money, right? Because we're never going
4 to know that, oh, they've had to reduce their rates
5 so now we can increase our rate.

6 BOARD MEMBER FUCHS: If this mechanism
7 gives UP a higher revenue division, then UP could
8 otherwise bargain with CP/KC on a competitive move
9 then that is giving money to UP, isn't it?

10 MR. ROSENTHAL: So, the mechanism is
11 never going to give UP a higher revenue division.
12 The mechanism is only going to affect the KCSM
13 division, which UP is not going to see unless a
14 shipper decides to share it and they're not going to
15 share it because they want to negotiate, so UP
16 doesn't get anything.

17 UP is left in the same position after the
18 merger, except knowing we're facing a fierce
19 competitor, right? So, today a shipper comes to us
20 and says what's your rate for competing a move from
21 Laredo to Chicago and we tell them a thousand
22 dollars. That's what we're going to tell them before

1 the merger. They come to us after the merger, and
2 they say what's your rate to go between Mexico and
3 Chicago and we could say a thousand dollars.

4 It hasn't changed, in which the shipper
5 is equally well off from UP perspective or we can
6 say, wow, I think CP/KC is probably going to be
7 really competitive. I don't think we can keep doing
8 what we were always doing. Now it's \$900. But
9 whatever happens south of Laredo UP doesn't see and
10 UP doesn't get that money.

11 BOARD MEMBER FUCHS: Well, it sees it in
12 the sense that if UP's revenue division doesn't
13 change and CP/KC gets less, then the shipper might
14 because they get an artificially lowered price from
15 what the market would provide, they would buy more.
16 They would buy more. UP gets more -- their overall
17 revenue division because the shipper's increasing
18 their demand at a less subsidized price. In other
19 words, if the market rate was a thousand and because
20 of this mechanism it went down to 950, but UP always
21 got 500, the shipper is going to buy more
22 transportation at 950. So, that means if UP still

1 gets 500 and there's more transportation, UP gets
2 more profit and CP gets less profit than they would
3 otherwise in a competitive marketplace. It's not
4 that CP/KC is writing UP a check. It's that the
5 overall economic division is such that UP gets more
6 profit than they would in a competitive marketplace
7 and CP/KC gets less.

8 MR. ROSENTHAL: Maybe I'm not just
9 following because I'm not sitting here trying to do
10 the math, but if what's happening is, UP is charging
11 the same rate and the shipper is shipping more
12 that's good. And in fact, even if KCSM is charging a
13 slightly lower rate and volumes are increasing it may
14 be doing better too. It may be a pro-volume -- but
15 the thing is it's really hard to know what the actual
16 answer is going to be unless you see the real
17 numbers. And so, what we have is a gateway
18 protection offer, right? If somebody realizes there
19 has to be something done. The question is are you
20 going to go for a promise that's essential an empty
21 promise? That's what they told us. They told us.
22 They said you can't tell, right?

1 And so, the question is, yes, it's hard
2 to do. It's hard to be perfect. You can't be
3 perfect, but this is something that's done in the
4 marketplace, it's something that's fair, and it's
5 something that the shippers are actually asking for
6 and I don't think they're going to be asking for
7 something that hurts them and we know that they're
8 not asking for something because they think it's
9 going to put money in the pockets of UP, right? I
10 mean they're doing it because they think it's going
11 to help them. They're not trying to help us.

12 CHAIRMAN OBERMAN: Let me ask you a
13 couple, few questions. Since the Tex-Mex acquisition
14 of '03, whenever it was, '04, what has been UP's
15 experience at Laredo? We heard about BN's. What's
16 been UP's?

17 MR. ROSENTHAL: In what respect, sir?

18 CHAIRMAN OBERMAN: Well, BN showed us a
19 bar graph that their traffic completely went into the
20 tank, toilet, whatever you want to call it after that
21 merger because of the rates. They said that their
22 rate to Laredo doubled. What's happened to yours?

1 MR. ROSENTHAL: So, there's a couple
2 things. One, I don't think we know -- I didn't quite
3 understand the nature of the BNSF relationship.
4 Generally, we don't have --

5 CHAIRMAN OBERMAN: Well, they have to pay
6 -- there's a leg to get to Laredo that they have to
7 pay KCS for and that's what rate doubled, but they
8 are contending that it was because really of the
9 control over Laredo that allowed them to do that.
10 So, what's been your experience?

11 MR. ROSENTHAL: So, we generally don't
12 see, again, what the KCSM rates are because they're
13 usually these confidential Rule 11 rates that only
14 shippers see. I don't know how BNSF knew that their
15 doubled. There's no UP rate. It's a rate that KCSM
16 quotes to the shipper, and we generally don't know
17 what it is.

18 CHAIRMAN OBERMAN: No, no, they were
19 talking about the rates in the United States between
20 Robstown and Laredo. They weren't talking about the
21 Mexican rates.

22 MR. ROSENTHAL: I understand. We just

1 don't have a similar experience because we don't have
2 a similar relationship. We don't see the rates, so I
3 can't say what happened to KCSM rates. I mean I can
4 -- there are a couple of data points, right, Dr.
5 Salup has in his paper.

6 Before the transaction, UP's market share
7 was somewhere in the nineties for northbound traffic,
8 I think, now down to the sixties, so it's gone down.
9 I don't think Union Pacific is claiming -- I don't
10 think we have the type of evidence that BNSF had that
11 our traffic has dried up. That's not our claim here.
12 It's hard to know what's responsible for going from
13 90 to 68 or whatever it is over a course of 20 years,
14 and I don't think we're actually alleging anything
15 happened.

16 If you look back at the KCS/Tex-Mex
17 merger application, when they were predicting traffic
18 diversions, they predicted something tiny, like 1
19 percent or less than 1 percent of the diversion from
20 UP. So, they actually didn't think that there was
21 all that much competition, all that much opportunity
22 to take traffic. It's very different from the

1 application we see here where you've got CP/KCS
2 saying they're going to take large chunks of
3 intermodal of autos, of auto parts.

4 So, I'm not sure we've seen any evidence
5 of that. I think we were very concerned at the time,
6 but I don't know whether we've seen it. And again,
7 even if it's happened, it's commercial one-offs of
8 many situations and we tried to go back and look. As
9 I said, in discovery we asked them questions. We
10 wanted to get data and they say we don't want to give
11 you data. It's a lot of data and it's not going to
12 do any good anyway because you can never prove that
13 we charged a commercially unreasonable rate because
14 there's no standard to define it, so go away.

15 CHAIRMAN OBERMAN: Well, it seems to have
16 worked without foreclosing you at Laredo. Why
17 wouldn't that same condition phrased the same way
18 work in this transaction?

19 MR. ROSENTHAL: Well, again,
20 respectfully, one, we don't know whether it worked or
21 not because we can't prove anything about what
22 happened, so we're not going to come in here and make

1 accusations about foreclosure.

2 Two, as Dr. Salup said, this is a
3 different transaction. Again, KCS/Tex-Mex said we're
4 going to divert 1 percent of UP traffic. There's not
5 much of an incentive to do anything if you think
6 there's very little traffic you could capture.

7 CHAIRMAN OBERMAN: I don't mean at the
8 time. I'm talking about your experience since the
9 transaction doesn't seem to have foreclosed you?

10 MR. ROSENTHAL: Well, I mean because KCS,
11 physically, has the same route network then as they
12 have now. They're not getting up to Chicago.
13 They're not in places like that where there's now an
14 opportunity to take traffic.

15 Again, what the economist said is you
16 need to talk about means and a motive, right? They
17 had the means. They really didn't have the motive.
18 Now, they've got the motive and that's what concerns
19 us about this transaction. There's a lot more
20 traffic that CP can go after that makes it worthwhile
21 for them to engage in this behavior. Previously,
22 there wasn't much KCS could do. As they said, they

1 were dependent on UP to help bring them revenue.

2 CHAIRMAN OBERMAN: Well, aren't there
3 many places in the country where the limitation is
4 commercially reasonable rates, other than Laredo?

5 MR. ROSENTHAL: No.

6 CHAIRMAN OBERMAN: I thought that
7 condition had been imposed by the Board.

8 MR. ROSENTHAL: I think the condition has
9 been imposed.

10 CHAIRMAN OBERMAN: Yes.

11 MR. ROSENTHAL: I thought you were asking
12 a different question.

13 CHAIRMAN OBERMAN: I'm wondering why that
14 condition isn't working, won't work here, it's worked
15 in other places.

16 MR. ROSENTHAL: We don't know. I mean I
17 have no idea whether it's worked in other places.
18 It's not a term that really has any meaning and
19 that's the problem, so we don't know whether it's
20 worked or not.

21 CHAIRMAN OBERMAN: Well, it seems to have
22 been accepted by a lot of railroads over time. Let

1 me ask this question. Do you agree with BN's
2 response to my question that the one chart they put
3 there that showed what they feared and that was on a
4 thousand-dollar rate that had been 400 in Mexico and
5 then after the merger KCSM changed the Mexican
6 portion to 700, remember that chart? And they agreed
7 that those facts would not be commercially
8 reasonable if they were proven. Do you agree with
9 that?

10 MR. ROSENTHAL: So, if the question were
11 if we, the Board, instead of imposing your conditions
12 said we're going to freeze the pre-merger KCS end
13 division so that they can't raise it, if that's your
14 question, it would be commercially unreasonable to
15 raise the division, we'd take that deal.

16 CHAIRMAN OBERMAN: The question is --

17 MR. ROSENTHAL: But I don't know what
18 commercially reasonable means. Could somebody come
19 in and say, yes, it's reasonable for KCSM to raise
20 their division by a certain amount?

21 CHAIRMAN OBERMAN: The only question I
22 asked was the exact hypothetical they had up there.

1 That they had raised the Mexican rates from 400 to
2 700. And under those facts when I asked if those
3 facts were proven would they have established that
4 that was commercially unreasonable and BN said, yes.
5 They could prove it. They would win that case. Do
6 you agree?

7 MR. ROSENTHAL: No, I can't agree because
8 I really don't know what commercially unreasonable
9 means, so I can't agree with that.

10 CHAIRMAN OBERMAN: All right. Because
11 what I'm wondering is if there was some way if you
12 thought you were being foreclosed you would have
13 reason to think that and you brought a case and you
14 could get through discovery disclosure of what they
15 were doing with their Mexican rates, wouldn't that
16 enable you to prove a commercially unreasonable
17 situation?

18 MR. ROSENTHAL: I don't know. I mean I
19 could imagine -- you know, as a lawyer making
20 arguments about why it was commercially reasonable
21 for me to change a division, just because I think
22 commercially reasonable isn't a real term that has

1 any actual established meaning in the railroad
2 industry.

3 Again, if you wanted to define it to say
4 it means that you can't raise your division, okay,
5 that would be something, but it doesn't tell me -- it
6 also, as you said, you're asking me about that one
7 specific scenario, which is a pretty narrow scenario
8 of a change in a division where the whole total rate
9 remains the same.

10 Okay, well, what if the rate goes up five
11 dollars, what if the total rate goes down five
12 dollars? When is it adjusting rates and divisions
13 and when is it actually engaging in some sort of
14 manipulation and I think that's very hard to tell and
15 that's why I think it has to be defined in some more
16 objective, commercial, easily enforceable --
17 something that's not going to require the shippers to
18 come into the Board and ask for a lot of discovery,
19 something that they can actually implement
20 themselves, something that's not going to require
21 the railroads to come in and ask for discovery of our
22 competitors' rates and ratemaking practices. Make

1 is simple, put it in the hands of the shippers and
2 let it apply to the broad scope of cases that arise.

3 CHAIRMAN OBERMAN: Well, Michael, I have
4 to say I'm impressed with the irony of the railroads
5 coming in here one after another asking us to help
6 shippers to be able to get low rates without having
7 to go through a litigation process. I wonder if
8 we'll see that attitude at further proceedings. It
9 would be helpful.

10 MR. ROSENTHAL: I mean I appreciate that,
11 but just -- it can be ironic, it can be not, but I
12 think, at least according to their papers, right, NIT
13 League is going to come in and say the same thing and
14 ACC is going to come in and say the same thing, and
15 TFI is going to come in and say the same thing
16 because that seems to be the right thing to do on
17 this record.

18 CHAIRMAN OBERMAN: Well, it may be.

19 MR. ROSENTHAL: Every case is different.
20 Every record is different, but it's not just the
21 railroads who are asking for this.

22 CHAIRMAN OBERMAN: It may be that they're

1 asking for a simplistic result here because they know
2 how hard it is to bring rate cases under previous
3 procedures and how ineffective those earlier
4 procedures have been. We may be dealing with that in
5 the near future. It strikes me, from what I've
6 heard, that, partly because of what you say, it's
7 hard to know that there's going to be foreclosure
8 until it happens, and you'd know by experience
9 whether there was foreclosure because you see what
10 happens to your traffic; is that a fair way to think
11 about it?

12 MR. ROSENTHAL: Yes. I think it's very
13 difficult to detect even looking at your traffic
14 because when you're looking at these broad periods --
15 and I think you saw some of these issues come up with
16 BNSF, right? I mean traffic comes and goes, it moves
17 gateway to gateway, economic conditions changes,
18 that's all part of what makes this very hard to prove
19 and that's why we're trying to come up with a simple,
20 easily enforceable, concrete solution that doesn't
21 require Board intervention because it really is hard
22 to prove why something is happening and it's hard to

1 see a change in the marketplaces versus a change in
2 behavior

3 And you point out, these proceedings if
4 you have to come to the Board one at a time, a
5 shipper at a time it can be costly and somebody's got
6 to weigh those consequences and the costs and that's
7 why I think -- again, I think that's why ACC is
8 proposing this, but I think in this situation when
9 you're talking about a merger that's going to have a
10 major impact on gateways and particularly the Laredo
11 Gateway, which is so important, this is the right way
12 to address the problem that you've been wrestling
13 with. I mean you asked in PanAm -- I was listening
14 to the hearing -- I'm saying we want a standard. We
15 want something that we can enforce, and we were
16 listening and that's what we tried to do.

17 CHAIRMAN OBERMAN: One answer we got in
18 PanAm from Mr. Foote was that he would close no
19 gateways neither physically nor financially. And so,
20 that seems to me that's consistent with the concept
21 that we were talking about with BN this morning, that
22 if in a case you could get visibility into what

1 happened with the Mexican rates that would help you
2 prove that they had closed it financially.

3 It sounds to me, Michael, if I asked you
4 in your closing brief to provide us with a way to
5 measure commercially reasonableness you would punt;
6 is that a fair statement?

7 MR. ROSENTHAL: (Off mike)

8 CHAIRMAN OBERMAN: In other words, you
9 said can't be defined.

10 MR. ROSENTHAL: I mean I don't think that
11 it's a term that has a meaning. I think what you
12 could say -- just to be clear, I think you could say
13 -- I'm sorry.

14 CHAIRMAN OBERMAN: Well, the reason I
15 asked is that I don't disagree with you. Right now,
16 it's not clear what the meaning is, but that's why
17 members of the Bar exist to help us figure it out.

18 MR. ROSENTHAL: Absolutely. And so, what
19 I'm saying here is that you should be defining
20 commercially reasonable by imposing what we're saying
21 is that you'll charge the mileage pro rate. And
22 BNSF, I think their answer is sort of the same, it's

1 the mechanism is a little bit different.

2 You could define commercially reasonable,
3 as you suggest in your hypothetical, by saying you
4 can't increase the division, but you need a
5 definition.

6 CHAIRMAN OBERMAN: Are you willing to
7 take the challenge of coming up with other
8 definitions, other than the prorated one?

9 MR. ROSENTHAL: Honestly, that was our
10 best shot at coming up with something that was easily
11 enforceable were you could put the control in the
12 hands of the shipper, and we thought that was very
13 important to a solution because the Applicants kind
14 of try to merge BNSF and UP's proposals together, but
15 we don't have a matrix, right? We're not going to
16 see the rates south of the border. That's all
17 shippers. And we're not going to be able to go out
18 and tell shippers we're going to sell you this
19 service and get a rate. A shipper has to go to them
20 and say we want your single-line rate.

21 CHAIRMAN OBERMAN: I understand.

22 MR. ROSENTHAL: So, we've tried to

1 structure this in a way that we thought was the most
2 procompetitive, shipper controlled, defined a way
3 that people are not going to be coming back to the
4 Board to resolve disputes.

5 CHAIRMAN OBERMAN: All I'm suggesting is
6 that if you have one that wasn't your first choice,
7 if you have other alternatives, we'd like to be
8 educated because we have to decide something about
9 what we're going to do in this area.

10 MR. ROSENTHAL: I understand.

11 CHAIRMAN OBERMAN: And I don't want you
12 to use that slide we saw earlier of all those broken
13 eggs in one basket, so I'm not sure how we're going
14 to resolve this. Patrick?

15 BOARD MEMBER FUCHS: I think what you're
16 alluding to is that over and over again in our rate
17 review, rate reform proceedings the rail industry has
18 sort of admonished the Board or at least pleaded to
19 the Board there are so many costs differences on
20 different routes.

21 There's a lot of costs on this end for
22 some routes. There's a lot of costs on that end for

1 some routes and while some of that could be picked up
2 on the interline, not all of it is going to be picked
3 up on the overall interline rate when you're breaking
4 it down on a pro rata mileage. And so I think what
5 we're all struggling with is the type of
6 simplification you all are describing is completely
7 contrary to every simplification idea that has been
8 put forward and rebutted by the railroads over the
9 years.

10 And I don't think it's enough to say,
11 well, the shippers are -- because the shippers have
12 been fairly consistent in more simplification is
13 better. It's the railroad industry, I think, that's
14 particularly newly in this proceeding talking about
15 how this simplification -- and I understand the I-5
16 Agreement, but that this simplification and the
17 relevance of cost considerations, among others, is
18 okay.

19 MR. ROSENTHAL: So, two words of that.
20 So, one, take a win, right? But second --

21 BOARD MEMBER FUCHS: I think KCS would
22 not consider it or CP/KC might not consider it a win.

1 MR. ROSENTHAL: Second, on the --

2 CHAIRMAN OBERMAN: Michael, we always
3 win.

4 MR. ROSENTHAL: I did want to get back
5 just on the cost issue because you raised it
6 yesterday with BNSF and I don't know whether you were
7 interested. I think Applicants had said something
8 about the railroads had objected to mileage-based pro
9 rates in other cases. Just to be clear, two things,
10 those were rate cases where there was a question
11 about how to divide hypothetical revenues.

12 And if you go back and you look at the
13 Board's proceeding in ex parte 657, when they
14 switched from a mileage pro rate to the more
15 complicated ATC model, what the shippers said is we
16 don't like ATC because it's not market based and the Board
17 said, well, mileage pro rate came into the legal
18 literature in the Nevada Power case because it was market
19 based.

20 These other things, ATC and all that,
21 they were addressing a different issue. They're cost
22 based. But the market based, mileage based pro rate

1 is kind of why we came to this idea because it is
2 consistent with the Board's precedent with what the
3 Board has looked at as a market-based thing.

4 I think it's used in the Board's waybill
5 sample when they're figuring out how to divide
6 revenue among carriers, I know, but it's crude, but
7 it's what is actually used and that's why we came back to the
8 mileage based pro rate as a reasonable look at what
9 the marketplace does.

10 BOARD MEMBER FUCHS: I understand, and
11 we'll move on, but I will said I had occasion to look
12 at that 657 passage that you're referencing in a
13 couple of the filings and I just have to say the term
14 "market based" and what it's referring to, whether or
15 not it's purely mileage, which is what's yours, I
16 think is open to debate. But we can review that and
17 take a look at the transcript and make sense of it.

18 CHAIRMAN OBERMAN: One more question
19 before we get to the Houston capacity issues, which
20 is, I assume, what Mr. Turner is going to talk to us
21 about. I cannot let this presentation by UP, this
22 procompetitive presentation by UP go by without

1 asking if you, and maybe it's not something you're
2 not prepared on, but if you want to enlighten us on
3 the procompetitive nature of UP's decision to take CP
4 out of the EMP Program which was announced last week.
5 According to the Trains article, which is where all
6 the information I have, Norfolk Southern, CN, KCS,
7 Florida East Coast, and CP were all in the EMP
8 Program with UP. And last week as a fairly direct
9 reaction to the pending merger application, UP said
10 CP you're no longer in the program. How is that
11 procompetitive?

12 MR. ROSENTHAL: The only thing I would
13 say on that item, Mr. Chairman, is that obviously
14 with the specter of the -- let me back up. The
15 original intent of the Box Program, the MP Box
16 Program that's a joint program between the UP and the
17 NS was to drive business to the railroads and
18 interline business.

19 Obviously, with the specter of the merger
20 and things like that, the competitive nature of those
21 things have changed quite a bit and so there was a
22 decision made, commercially, to make a change to

1 that. If for some reason the application isn't
2 granted, then obviously we could go back and look at
3 that at a future time.

4 CHAIRMAN OBERMAN: Well, my reaction is,
5 is that it was punitive, retaliation for the merger.
6 I can't interpret it any other way. You could say it
7 was commercially determined, but I assume that was
8 the commercial determination. And all things
9 considered, quite frankly, it doesn't put UP in a
10 particularly good light when we're considering
11 protecting UP's competition. A word to the wise, for
12 what it's worth.

13 MR. ROSENTHAL: Appreciate the feedback.

14 CHAIRMAN OBERMAN: Any other questions.
15 Okay, let's hear about Houston.

16 MR. TURNER: Okay. Good afternoon. My
17 name is John Turner, as Mike mentioned earlier. I'm
18 the Senior Vice President of the Harriman Dispatch
19 Center and Network Planning. And in my role I'm
20 responsible for managing the execution and planning
21 of over five critical resources. That's locomotives,
22 crews, line of road capacity, terminal capacity, and

1 freight cars.

2 To give you guys some perspective, I'm
3 the proud son of a retired conductor. Ironically, my
4 father actually worked on a portion of the Canadian
5 Pacific Railway in southeastern Iowa. I have two
6 brothers who are locomotive engineers for the Union
7 Pacific and my son works in Marketing Sales for the
8 Union Pacific, so we're three generations of Turners
9 in the railroad. In fact, irony of all irony, I have
10 an uncle that's a retired signal maintainer for the
11 BNSF, so we kind of spread our wings wide in the
12 railroad industry.

13 In 1997, I began my railroad career on
14 the Iowa/Minnesota Railway, which was a short-line
15 railroad in southeast Iowa, now currently part of the
16 Canadian Pacific Rail franchise. In 1998, I came to
17 the Union Pacific, again, working as a conductor in
18 train service, working broadly across Iowa and
19 proud to say that when remote control switching
20 operations were implemented on the Union Pacific, I
21 was one of the very first employees to ever have a
22 signed remote control licensed to operate in a yard.

1 Since then, I've taken a litany of
2 different roles broadly across the Union Pacific
3 Railroad and that's what's given me a broad
4 perspective for my responsibilities here today. You
5 mentioned we're going to talk about Houston. The
6 Houston history is well known to this Board and it's
7 with this history and a healthy respect for the
8 historical operation implications that we should view
9 the step function change in merger-related volume.
10 Failing to adequately prepare and plan and
11 acknowledge these risks doom us to repeat history.

12 It is for these reasons that we think
13 about the impacts being wide ranging. It's not just
14 the Union Pacific and its customers, it's the BNSF
15 and its customers, it's the KCS and its customers,
16 it's the PTRR, the Port of Houston, and even Amtrak
17 could be impacted if we're not careful about how we
18 implement the impacts of this merger.

19 We provided a map. I'm going to spend a
20 minute and I'm going to try to orient the group. But
21 you can see by looking at the map that the Houston
22 Complex is a tightly packed spider web of lines and

1 yards. In fact, if you think about the lines on the
2 outside of the map heading towards the middle of the
3 Houston Complex, some refer to those as the
4 interstates and going to the city center where
5 there's a series of downtown stoplights.

6 Frankly, when we were putting together
7 the material, I was thinking about as we present it
8 to the Board to try to explain some of the
9 complexities of this and had a difficult time doing
10 that because there are hundreds of customers that are
11 served in and around the Houston Complex.

12 In fact, there are about 15 yards, if you
13 look at the grey boxes depicted on the map, in each
14 of the sections, starting with the top left, you see
15 a Eureka Yard, in the center you see the UP's
16 Englewood Yard, just north of that there's Settegast
17 Yard, then you see the Baytown Branch, and then you
18 move down to the bottom left and you see Congress
19 Yard, you see the BNSF's Old South Yard, you see the
20 new South Yard on the BNSF and on and on. To the
21 east, you see the Portland -- not Portland rather but
22 the Port Terminal PTRAs Yards on both the north and

1 south side of the channel close to the Port of
2 Houston.

3 All of these yards are in a very heavy
4 industrial area. In fact, Houston is unique in the
5 Union Pacific franchise. A lot of the traffic
6 doesn't actually leave Houston. It moves from plant
7 to plant in very short moves. In fact, there is no
8 level of intensity that's rivaled on the Union
9 Pacific and likely anywhere in the United States. In
10 fact, every single day in Houston there are over 130
11 yard and local jobs that are responsible for serving
12 customers in and around the Houston Complex.

13 When you look at the intersecting lines,
14 each time one of those lines crisscrosses that's an
15 intersection just like in downtown. Each of those
16 when a train is traversing them blocks the route for
17 a train in the opposite direction. A train moving
18 east and west blocks trains north and south, so it's
19 very complex and it's a series of complex tradeoffs.

20 The Applicants failed to acknowledge the
21 risks in their applications. They cited, well, it's
22 just eight trains per day. That is not incremental

1 volume. It is a step change in volume. Going back
2 to 2009, we have never seen this large an increase
3 year over year or in any three-year period that we
4 can find.

5 In fact, a single train per day increase
6 on any of these line segments would be cause for an
7 enormous amount of analysis by my team bringing in
8 the BNSF and others to make sure that we had good
9 plans to be able to handle this business.

10 To give the Board some perspective, when
11 we talk about building capacity in a place like
12 Houston, there are enormous challenges. In fact, the
13 Applicants cite several examples of Houston-based
14 capacity. Many of those that they mentioned took
15 five to seven years to come to fruition, which is
16 outside of the envelope of the three-year plan that
17 the Applicants put in their application.

18 The challenges range from the acquisition
19 of real estate, many look around at property and
20 think, oh geez, look, you just have to move a few
21 things and it's easy. In Houston and in many cities
22 it's not that easy. There are utilities, gas lines,

1 water lines, implications related to communities and
2 others that have to be addressed as part of any kind
3 of capacity project, especially in Houston.

4 Next, I'll show you a map, the Board has
5 seen this. It's in the record in other proceedings
6 over the years, but the arrows are the KCS's current
7 main flows through the Houston Complex. I'm going to
8 start by working at the bottom left near where that
9 gold box is in a place called West Junction.

10 The dark blue arrows as they move north
11 through West Junction move up to another intersection
12 at Eureka Junction, taking a right before heading
13 north up towards Tower 76 before taking a right and
14 heading out towards Beaumont, Texas. Yes, sir?

15 BOARD MEMBER PRIMUS: So, is this, the
16 purple line, the main flow for where KCS is currently
17 moving through, and if so, who else moves along that
18 line and how many per day?

19 MR. TURNER: All the carriers move
20 through that line, so BNSF moves through there and
21 KCS moves through there currently, the Union Pacific
22 moves through there, as well as Amtrak. Currently,

1 there are 33 trains a day that traverse this West
2 Junction here at the bottom left.

3 BOARD MEMBER PRIMUS: And you may or may
4 not know -- thank you for that -- what's the general
5 timing -- again, you're going through a maze, so if I
6 were to start at that West Junction and come out, I
7 guess at -- is that Settegast Junction?

8 MR. TURNER: Yes.

9 BOARD MEMBER PRIMUS: Okay. What's the
10 timeline for that?

11 MR. TURNER: I don't have that one right
12 off the top of my head, but it's in hours. It's not
13 a few minutes run. It's in hours and it has to do a
14 lot with the complexities that I mentioned in the
15 opening.

16 You've got a lot of traffic, a lot of
17 yard and locals, and a lot of short moves, so it's a
18 very slow-moving terminal. It's not a high-speed
19 route. In fact, I'll take about that in some
20 upcoming slides about some of those complexities.

21 CHAIRMAN OBERMAN: How many of the 33 are KCS?

22 MR. TURNER: Between 10 and 11. It kind

1 of varies. I think the peak that I saw in the
2 analysis period it might have tipped up to 11 here
3 even recently, but generally speaking, it's around
4 the 10 to 11 range.

5 (Off the mike)

6 MR. TURNER: Yep. You bet. If you
7 started on the right-hand side, the light blue
8 arrows, starting from the east and moving west is the
9 primary flow, but the Applicant or the KCS
10 currently takes through the Complex, you can see as
11 they move from east to west through Tower 87, Tower
12 68, and Tower 26 ending up back at that same Eureka
13 Junction that I mentioned earlier.

14 Member Primus asked about this, but one
15 of the key areas when you think about the traffic
16 flows, if we go back to this year, the average trains
17 through this one section of track is 33 trains a day
18 today. At the highest peak in the analysis period
19 used by the Applicants they used 2015 to 2019, it was
20 34, so they're asking for seven more trains than what
21 was in the peak to go through this particular section
22 of the railroad.

1 CHAIRMAN OBERMAN: Are the 33 westbound?

2 MR. TURNER: It's in both directions.

3 It's east and west. They both have -- excuse me.

4 CHAIRMAN OBERMAN: There are 10 to 11
5 eastbound trains and 10 to 11 westbound trains?

6 MR. TURNER: Total. So, think five and
7 five. Generally, like day to day that might change
8 in one direction or the other.

9 (Off mike)

10 MR. TURNER: Between 8 to 10 based on
11 their app. We see eight in there most recent app
12 reply.

13 BOARD MEMBER HEDLUND: But is that four
14 and four?

15 MR. TURNER: Yes. Presumably, that's
16 based on what we can see in the operating plan, yes.

17 BOARD MEMBER HEDLUND: So, it's not eight
18 each way, it's four.

19 MR. TURNER: No, it's four in each
20 direction. It's this area that's the cause for
21 concern, specifically, and I'll talk about the
22 alternative routes which are the green arrows that we

1 used on there, but essentially, many of those
2 alternative routes are the equivalent of driving the
3 wrong way on a one-way street based on how the
4 terminal actually operates today.

5 But looking at West Junction, in
6 particular, because of how the KCS has to both enter
7 and exit the Houston Complex, even the alternative
8 route they still have to go through that particular
9 corridor, they still have to go through West
10 Junction. I'll talk a little bit more about what the
11 capacity looks like in some upcoming slides.

12 BOARD MEMBER HEDLUND: Could you tell us
13 where the Amtrak trains go?

14 MR. TURNER: The Amtrak passenger depot
15 is actually right here and then they have to take
16 that route.

17 BOARD MEMBER HEDLUND: And where do they
18 come from or go to?

19 MR. TURNER: They come from this part
20 here, the same route that the KCS takes, the most
21 efficient route through Houston, comes to this depot,
22 and then takes this same segment out onto the UP

1 Glidden Sub.

2 CHAIRMAN OBERMAN: So, the Amtrak trains
3 follow the blue and purple arrows. Correct?

4 MR. TURNER: Yes. Yes.

5 CHAIRMAN OBERMAN: Okay.

6 MR. TURNER: The Applicants original
7 submission largely ignores the setting of the
8 trackage rights lines, and the subsequent replies
9 have enormous flaws, which I'll point out. As the
10 Applicant has made mention, and others, the key to
11 unlocking the potential of this merger is the line
12 from Laredo going through Houston. To kind of walk
13 the group and orient everyone to where we're at, if
14 you start at the bottom left and you look at Laredo,
15 you can see the blue arrow and if you follow that up
16 to the north more towards Houston in the dark blue
17 those are KCS-owned tracks.

18 At Robstown, they get on UP-owned tracks
19 as part of their trackage rights and move north
20 towards the Bloomington area before taking a left at
21 a place called Victoria, Texas. It's at that point
22 that the Applicants get back onto what they call the

1 Rosenberg Line and then you see the intersections of
2 lines underneath the words "Rosenberg" that's where
3 all of the carriers come back together. So, that's
4 where the KCS is, that's where the UP is, it's where
5 the BNSF is, all heading into that section, that
6 yellow triangle that I showed you earlier before
7 traversing the Complex and heading east towards
8 Bloomington.

9 I find it a little ironic that the
10 detailed operating plan required all over the CP/KC
11 joint railroad that they needed to add capacity on
12 those lines, but yet, there's an assertion that
13 there would be no additional capacity required
14 anywhere on the trackage rights lines.

15 So, to highlight some of the interesting
16 things here today, it's not as simple --

17 CHAIRMAN OBERMAN: Mr. Turner, when you
18 talk about the trackage rights lines through the
19 Houston Terminal, are these all-trackage rights that
20 stem from the UPSP merger or do they come from some
21 other source?

22 MR. TURNER: I think they're all from the

1 UPSP merger, yep.

2 CHAIRMAN OBERMAN: Okay.

3 MR. TURNER: To highlight that it's not
4 just as simple as saying, oh well, it doesn't really
5 matter because the traffic is just going to change
6 from one carrier to the other. Today traffic that's
7 not destined for Houston or someplace east of Houston
8 doesn't go through Houston on the Union Pacific. So,
9 the eight trans that they're adding are going to be
10 new. These are additional trains that will be going
11 through the Complex. Today they bypass the Complex.

12 BOARD MEMBER PRIMUS: So, are you saying
13 all KCS trains bypass?

14 MR. TURNER: No, sir. I'm saying all of
15 KCS trains must go through downtown Houston. Today
16 traffic that the Applicants say that they're
17 targeting, finished vehicles, intermodal, things like
18 that, that they're going to try to drive to their new
19 joint franchise it'll all have to go through Houston.
20 Today those intermodals, the finished vehicles that
21 traverse on the Union Pacific is likely targeted by
22 the Applicants we bypass Houston, and we go to

1 gateways. We go to Chicago, we go to Memphis, we go
2 to St. Louis, those places.

3 BOARD MEMBER HEDLUND: So, you're saying
4 that the new traffic or eight additional trains are
5 really coming from Union Pacific.

6 MR. TURNER: I'm saying based on their
7 own application they're targeting business from both
8 the BN and the UP to drive towards Houston, yes.

9 BOARD MEMBER HEDLUND: So, this is
10 existing business, not additional business.

11 MR. TURNER: I think if you read their
12 application they'll say that there's some additional
13 business --

14 BOARD MEMBER HEDLUND: I'll let them
15 speak for themselves.

16 MR. TURNER: Okay. The Applicants in
17 their reply tried to correct the record by
18 essentially saying that don't worry. Houston has
19 handled this much traffic before. In fact, I think
20 on Wednesday, Mr. Orr showed the Board a graph that
21 showed the peak in 2016 and that we're well under
22 that when you layer on the KCS's proposed traffic

1 that it won't be a problem.

2 One of the critical flaws in that
3 analysis is that the data that they used encompassed
4 all of Houston. What I mean by that, and I said in
5 the opening, is a lot of the traffic in Houston
6 never actually leaves Houston. So, you have a lot of
7 point-to-point trains moving from plant to plant or
8 yard to yard inside of the Complex. So, just looking
9 at Houston in total and looking at the train count is
10 an enormous oversight because it ignores the actual
11 routes that the Applicants have to take through the
12 Complex.

13 Below is the Table and mine looks like
14 blue and blue, up there it should be purple and blue
15 and so on the eastbound flow we took and layered in
16 each of those segments that I walked you through on
17 the map with the arrows and then layered on the
18 business that would traverse those. So, you see some
19 directional routes where only four trains a day would
20 go through there. You see the eight trains a day
21 from West Junction to Rosenberg and from West
22 Junction to 26 that we talked about.

1 And if you take a look at the peak from
2 2015 to 2019, you see increases in traffic above the
3 peak that range from almost 6 percent, 5.7 percent to
4 over 31.5 percent over key routes inside of the
5 Houston Complex.

6 It's similar on the westbound move. We
7 layered on their westbound directional traffic,
8 layered on the segments where the eight trains will
9 be currently, and you see similar results.

10 The next slide shows what it actually
11 looks like on their route. This is the exact same
12 map that we started with only this time we layered on
13 the peak of 2015 to '19 and then layered on the eight
14 trains. We're setting new frontiers across this
15 particular segment of the route.

16 BOARD MEMBER PRIMUS: Hey, John, let me
17 ask a quick question. So, what's the total number of
18 trains that actually pass through the terminal, so
19 like a KCS would do? You're saying most of them will
20 come with destinations within the terminal and
21 around, so how many current trains actually act in
22 the same manner that KCS would in terms of coming

1 through the terminal?

2 MR. TURNER: That's frankly what's unique
3 about the KCS and the Houston Terminal. Almost all
4 the traffic that the UP and the BNSF runs in doesn't
5 run through in this similar fashion. It doesn't run
6 the entire length of the Complex. It literally only
7 runs portions of the Complex to get to the certain
8 yards because you're building trains from outside on
9 those interstates that I described earlier to come
10 into land into certain yards inside of the Houston
11 Complex versus KCS having to come from Laredo up
12 through Robstown and Victoria through Houston and
13 they've got to traverse the entirety of the Complex.

14 BOARD MEMBER PRIMUS: So, are they the
15 only freight carriers to do that because I know
16 Amtrak, of course, traverses through, but they'll
17 stop at a station, but are there other --

18 MR. TURNER: I would have to double check
19 that for you. I'm not sure if the BNSF has a train
20 or two. The Union Pacific does not.

21 The second flaw in the Applicants'
22 revision is they cite the clear route provision

1 saying don't worry about it. If it's a problem,
2 we'll just use one of the alternative routes. We
3 took the same analysis and did the same thing in this
4 matrix over the same period, and we get very similar
5 results.

6 If you go to the map, I think it's
7 important to note that the clear route condition is
8 for exceptions of extraordinary circumstances. It
9 isn't a license for everyday use. If you take a look
10 at the route, starting at the bottom left.

11 (Off mike)

12 MR. TURNER: There was a condition
13 imposed by the STB that said that if for some reason
14 the KCS or any carrier for that matter couldn't get
15 through on their primary routes that the dispatching
16 office had the clear authority under the joint
17 director to move those trains on a route that could
18 actually get them through the Complex.

19 So, you have your trackage rights, your
20 primary routes that you run the trains on today. And
21 if for some reason you couldn't get through there,
22 you could pick an alternative route to keep the

1 Complex moving.

2 CHAIRMAN OBERMAN: That's from the merger?

3 MR. TURNER: Yes. It's a condition from
4 the merger, yes. When you start at the bottom left
5 near Rosenberg at the 22.9 percent on the map and you
6 head through West Junction, moving kind of east or
7 from left to right, you see all the similar things.
8 There is one section that's 3.2 percent better where
9 the Applicants' traffic actually would fit. However,
10 you have to be able to get in there and out of there,
11 which they would not be able to do under the current
12 capacity constraints.

13 The other thing the Applicants ignore is
14 train length over time. Trains counts are important
15 in capacity planning, but so is train length,
16 especially in a place like Houston. I talked about
17 all the intersecting lines. We call those
18 interlocking in the rail business.

19 Each one of those, even though the map
20 looks like they might be a fair distance apart, some
21 of these junctions are literally 1,000 feet, 2,000
22 feet, 4,000 feet. They look like they may be a long

1 way away, but under current train sizes it's possible
2 that you could block multiple routes moving through
3 the Complex with a single train.

4 In fact, if you compare the KCS's peak
5 train counts and you layer on their average train
6 length, their average train length is actually 10
7 percent longer. This means that they're going to
8 actually consume more capacity than they have in the
9 past.

10 In fact, based on the Applicants' own
11 operating plan, they anticipate running trains up to
12 10,000 feet. This is several thousand feet longer
13 than they currently run, on average, through the
14 Complex. So, the notion that they're taking up less
15 capacity because they're just running directly
16 through the Complex is not entirely accurate.

17 The Applicants are not entitled to an
18 easy pass. There are not Houston express lanes
19 because doing so means in pairing, servicing hundreds
20 of customers throughout the Complex.

21 I mentioned before that the KCS trains
22 consume more capacity because they run the entirety

1 of the Complex and if you'll take a look at the map I
2 mentioned earlier with Member Primus's question, but
3 if you look at the map many of the trains that the
4 Union Pacific operates head towards Settegast Yard
5 and Englewood Yard, only traversing a small segment
6 of the Houston Complex, the same with many of the
7 BNSF trains where they might be running to the Old
8 Yard or their new South Yard on the west side of the
9 Houston Complex only traversing a small segment
10 versus traversing the entirety of the Complex, as KCS
11 does.

12 CHAIRMAN OBERMAN: Is there a short line
13 or a belt line in the Houston area?

14 MR. TURNER: There is the PTR. I
15 mentioned them before. On the map in purple, they
16 have lines where they service customers on both sides
17 of what we would call the ship channel at the Port of
18 Houston.

19 (Off mike)

20 MR. TURNER: Yes, sir.

21 CHAIRMAN OBERMAN: They don't go through
22 the whole terminal?

1 MR. TURNER: No. They're a switching
2 operation that just serves local customers.

3 CHAIRMAN OBERMAN: All the rest of the
4 spaghetti bowl is BN, UP, and KCS?

5 MR. TURNER: Correct -- and Amtrak. I
6 showed you a portion of this route earlier, but this
7 is another area where the Applicants failed to
8 analyze the route, and this isn't the only area of
9 concern. Houston isn't the only area of concern. We
10 have concerns on other locations which I'll highlight
11 in upcoming slides.

12 This is the route that I highlighted
13 earlier where they start at Laredo, and they come up
14 to Robstown across the trackage rights lines.
15 There's a bracket towards the middle of the slide
16 that says, "Inari to Bloomington." I'll use this
17 to illustrate some of our concerns.

18 The Applicants indicate that, look,
19 there's all these segments that come from Laredo all
20 the way up that have an enormous amount of capacity,
21 but when you layer on the step function change in
22 merger related growth, it's just not going to fit.

1 UP does similar calculations that the
2 Applicants did, and we refer to them often as
3 bottleneck analysis. Generally, these are very
4 straightforward calculations, but based on what we
5 were able to see from their application and we
6 haven't seen all of them, and I'm sure that they have
7 reasons that they consider to be proprietary, as we
8 do, in terms of how we calculate capacity. But
9 based on what we were able to see, we were able to
10 put together enough of those and reverse calculate
11 and get similar results to what we see on the
12 left-hand side.

13 The key to these calculations is in the
14 assumptions. When you're doing these types of
15 analyses, you usually have some actual data, usually
16 some train speeds, track availability in terms of how
17 much time is available during the day and how much
18 you take out for maintenance, those sorts of things.

19 But many of these assumptions, including
20 trains spacing, how much surge capability, how much
21 variability to factor into your capacity analysis,
22 these things are often rules of thumb. On the Union

1 Pacific we do studies to make sure we understand what
2 those look like. Specifically, if we're getting ready to
3 make an investment, we would do a study on a specific
4 line segment to make sure that we've got the
5 calculations right and that we're making good, solid
6 business decisions.

7 Based on what I can see in the
8 application and in the responses, their assumptions
9 are extremely aggressive, sometimes twice as
10 aggressive as what we would use on the Union Pacific.
11 What do I mean by that? In the matrix you can see on
12 the left-hand side they calculated what we would
13 consider to be a theoretical capacity. In other
14 words, this is how many trains you could fit through
15 there if everything were perfect, the spacing were
16 exactly like the assumptions, and you would say I
17 could get 41.1 trains through this particular
18 segment, Inari to Bloomington.

19 Based on their application, they
20 calculate what they consider to be a sustainable
21 capacity of 65 percent. Again, an extremely
22 aggressive assumption based on Union Pacific

1 calculations and how we plan for capacity. This
2 yields them a 26.7 trains per day through this
3 particular segment.

4 When you look at the sustainable capacity
5 and you match that up to the 2022 data, that leaves
6 them 1.7 trains per day worth of additional capacity
7 above what they put in their model. I can tell you
8 from experience that even that little bit of headroom
9 would be cause for additional analysis inside of
10 Union Pacific. What their analysis doesn't include
11 is any growth for the BNSF, who uses this exact same
12 line. It doesn't include any growth for the UP, who
13 owns the line and operates the line.

14 I mentioned that these assumptions are an
15 important part of the calculation and even a small
16 change in one of the assumptions can change the
17 outcome on how you may feel about capacity planning.
18 In this case, we simply just change the train
19 spacing from five minutes on the left-hand side to
20 just ten minutes on the right-hand side.

21 It changes the theoretical capacity by a
22 little over five trains, changes their sustainable

1 capacity at 65 percent to 23.4 trains and we match
2 that up against 2022 volume it goes red, just like
3 the routes I showed you on the Houston map.

4 Another area of concern what the
5 Applicants did do some analysis is the Neches River
6 Bridge, which they own, and is a trackage rights --
7 (Off mike)

8 MR. TURNER: It's east of Houston. I'm
9 going to show you a map here, right there. For some
10 reason, the Applicants --

11 (Off mike)

12 MR. TURNER: Yes, east of the Spaghetti
13 Bowl out near a place near Beaumont, Texas.

14 CHAIRMAN OBERMAN: So, it's on the line
15 towards Beaumont?

16 MR. TURNER: Yes, sir.

17 CHAIRMAN OBERMAN: Okay.

18 MR. TURNER: Very near Beaumont. For
19 some reason, the Applicants chose a different
20 calculation in their methodology, but we took the
21 Brownsville methodology, the Inari to Bloomington and
22 applied those same assumptions. What you get is 34.4

1 trains of sustainable capacity. The problem is, is
2 that based on the Applicants own projections they're
3 expecting to have 42 trains today.

4 I can tell you that it seems odd to me
5 that prior to the specter of a potential merger this
6 was a known area of concern for all the carriers
7 involved. To highlight some of this and to show the
8 Board the complexities around this, you can see that
9 this is a very busy area with a lot of different
10 interfaces, including, yes, the KCS, the BN, and the
11 UP. Amtrak has a depot right in the center of what we
12 would consider to be a bottleneck between the
13 confluence of all of the flows, but it's important to
14 note that their analysis didn't assume any growth for
15 barge traffic that travels underneath the Neches River
16 Bridge and the bridge has to be lifted to take its
17 rail capacity out throughout the day.

18 There is no growth for the UP, no growth
19 for the BN, and no changes in what Amtrak's doing.
20 In fact, as far as we can tell, based on the
21 application, there's no assumption made for
22 increased maintenance on this bridge with the

1 increased tonnage and volume going over it, which
2 seems unlikely.

3 We have deep concerns with the
4 operational impacts of the step change and growth,
5 merger-related growth. And the Applicants next claim
6 that if there is a capacity concern don't worry about
7 it because the Tex-Mex Agreement handles all of this.

8 The Tex-Mex Agreement was not designed to
9 handle a step change in merger-related growth. In
10 fact, past practice with our partners on the KCS is
11 quite different. The KCS has always paid for
12 incremental capacity. If it's true that this merger
13 is in the public interest, then the Union Pacific,
14 the BNSF, and our customers should not be required to
15 subsidize the Applicants' desires.

16 The second concern in the Tex-Mex
17 Agreement is, is that the timing of the Applicants'
18 projects that need to be done puts the operation in
19 jeopardy without having the capacity in place to be
20 able to handle it in the timeframe that they've
21 asked. I mentioned they've got a three-year growth
22 plan. I mentioned that many of these projects inside

1 of these city centers can take years to come to
2 fruition.

3 The other concern that the Tex-Mex Agreement
4 doesn't handle is, is that the answers for the
5 capacity projects might not come on lines covered by
6 the Tex-Mex Agreement. They could require for
7 capacity projects to be constructed on another
8 portion of Houston or some other portion of the
9 railroad and it wouldn't be covered under the
10 existing trackage rights agreements.

11 So, what is the Union Pacific asking for?
12 You heard Mike talk about a direct, straightforward,
13 mileage based, prorated gateway rate. We would ask
14 for a condition that the Applicants, the CP/KC
15 cooperates with the UP and other stakeholders in
16 developing a plan that actually addresses the needed
17 capacity for the trackage rights accommodating the
18 merger-related growth.

19 We'd ask that any increase in train
20 traffic only be allowed after the capacity is added
21 and paid for by the CP/KC. And lastly, as Mike
22 mentioned, the new bridge that's being constructed

1 at the Laredo Gateway we would expect to be on the
2 same terms and conditions as the existing bridge.
3 And with that, I'll be quiet, let you guys ask
4 some questions.

5 CHAIRMAN OBERMAN: I have a few
6 questions.

7 MR. TURNER: Yes, sir.

8 CHAIRMAN OBERMAN: Who's paying for that
9 Laredo Bridge?

10 MR. TURNER: Currently, it'll be the KCS.

11 CHAIRMAN OBERMAN: Are you volunteering
12 to pay for part of it if you want access to it?

13 MR. TURNER: We would love to have a
14 conversation about that.

15 CHAIRMAN OBERMAN: I'm not sure that was
16 a direct answer, but it wasn't a no.

17 MR. TURNER: Well, if you think about the
18 current agreement over the bridge, there's a lot of
19 puts and takes related to all the trackage rights
20 things related to that.

21 CHAIRMAN OBERMAN: I'm sure, but it just
22 struck me that if you're asking them to pay for

1 infrastructure that they're going to use it only
2 makes sense if you're paying for infrastructure
3 you're going to use.

4 MR. ROSENTHAL: I would say one of the
5 things we're talking about is getting access on the
6 same terms that apply to the current bridge and at
7 least our understanding of the way that rates were
8 set for the current bridge is that they're set to
9 provide compensation for the cost of renewing the
10 bridge. I mean we don't own the current bridge that
11 we're paying this particular rate for it.

12 CHAIRMAN OBERMAN: Let me ask this
13 question. Earlier the BN, and I think you're saying
14 the same thing, is that your through trains don't go
15 through Houston, they go around it. You have to
16 honor the trackage rights through Houston that KCS
17 were granted in the merger. I can't tell from these
18 maps whether there is a way for the new CP/KCS
19 through trains to go around Houston; is there an
20 opening here for a tradeoff for the trackage rights
21 they have through Houston to be exchanged for
22 trackage rights around Houston so they can do what

1 they need to do and not go through this crowded
2 terminal it's a win for everybody?

3 MR. TURNER: I think we'd start with
4 doing the study and seeing what those implications
5 are. At this point, there's not a list of projects.
6 The study needs to be done because of the volume
7 we're talking about, but if at the end of that, as we
8 were looking at all of the potential alternatives to
9 resolve that we can have a conversation about what
10 that might mean and what those implications are on
11 other lines.

12 CHAIRMAN OBERMAN: My question really is
13 there a physical way to do it to get the CP/KCS new
14 trains, all of their trains for that matter, out of
15 the Houston Terminal and to go around it? I don't
16 know what's physically down there.

17 MR. TURNER: Physically, today we
18 interchange on the Union Pacific and take traffic
19 right off the Laredo Bridge and bypass Houston today,
20 so it's not a physical limitation.

21 CHAIRMAN OBERMAN: Well, that's for UP
22 trains and that goes to your routes, but that's

1 different than where the CP/KCS trains are ultimately
2 going. Does it make sense to use some of that
3 trackage for them and get them back to their routes?
4 I don't know what's there.

5 MR. ROSENTHAL: I mean I think the
6 answer, physically, one depends on where they think
7 their trains need to end up and if they're dropping
8 some traffic off and whatever on their Rosenberg sub
9 or at Shreveport, then maybe going in different
10 directions. But I think what John said is some of it
11 may be possible, but it would be something to talk
12 about and it's hard to talk about it without the
13 background of knowing what the relative differences
14 are and the options.

15 CHAIRMAN OBERMAN: Right. But if it's
16 not physically possible there's nothing to talk
17 about. It strikes me, from what I'm hearing, that UP
18 and BN would be delighted to get all the KCS through
19 trains out of the Houston Terminal because all
20 they're doing is adding to the congestion there from
21 your description and they're not stopping there.
22 They're going through; is that a fair statement?

1 MR. TURNER: I'm not sure love would be
2 the term that I would use. I understand the point
3 that you're trying to make.

4 CHAIRMAN OBERMAN: I mean I'm just trying
5 to respond to what's here. I have no expertise in
6 operations, but I keep hearing they're only going
7 through, so they don't need to be in Houston if
8 there was a way for them to get from here to there as
9 to where they're going.

10 MR. TURNER: Without seeing all the
11 details of their traffic files and sitting down and
12 actually doing a study, it's hard for me to say
13 whether it makes sense for that traffic to bypass
14 Houston or not. What I am saying is that the traffic
15 that they're targeting for the Union Pacific, based
16 on what we can see in their application doesn't go
17 through Houston today, but those are planning
18 decisions that need to be made and are balanced off
19 against lots of tradeoffs, including capacity.

20 CHAIRMAN OBERMAN: And I take it that
21 your testimony is that you have no specific capital
22 projects to improve the flow of traffic that you're

1 proposing to be conditioned to the merger?

2 MR. TURNER: Not specific projects, no,
3 not for this level of business.

4 CHAIRMAN OBERMAN: Well, it strikes me
5 that it's difficult to ask us to condition that after
6 a study is done CP/KCS pays for whatever the study
7 comes out with. That's kind of a open-ended
8 commitment. That doesn't seem practical.

9 MR. ROSENTHAL: There are couple things
10 here, Chairman Oberman. One, we weren't the
11 Applicants, right? Applicants came in and said
12 nothing needs to be done. They had time to prepare
13 an application. They had as much time as they wanted
14 to put together their application and their
15 conclusion was, to the extent they even studied it,
16 and nothing needs to be done.

17 So, we came in and we said, wait, you
18 haven't studied this. Here are our concerns. They
19 came back with these kinds of quick little things
20 that don't really hold up. So, one, they had to come
21 forward with something and they haven't. In the time
22 we had to file a reply, right, we were able to go in

1 and look at what they had done and ask them about it
2 and try to show why that was wrong, but we don't have
3 time to build their solution and these things are
4 difficult, right? There are tradeoffs. It involves
5 planning. These are things that people sit down and
6 negotiate over time and it's not our fault that they
7 put together this transaction on their timeframe and
8 are trying to get it through. And it's not our fault
9 that they didn't put together an application that
10 recognized this is a problem.

11 They're still telling you today or
12 yesterday or whatever, two days ago, that there are
13 no issues in Houston, that there's plenty of capacity
14 that it's operating. And if you believe that, you
15 believe that. But if you don't, I mean their
16 position is that there's no problem. There's no
17 reason for a study and again, it takes time and
18 that's the way it is.

19 And I mean I think BNSF made the point
20 yesterday. As far as putting in the money, I mean,
21 one, they've put in the money. And Member Hedlund, you
22 raised the question about procedurally what do you

1 do? Do you approve or not approve? I'm not sure it
2 matters. You could have a condition on it, and they
3 can decide whether to accept the condition or not
4 accept the condition, whether the condition is a
5 study or they can decide not to. But if they have --

6 BOARD MEMBER HEDLUND: My concern was
7 they have no basis on whether to accept the condition
8 or not because they have no idea what it's going to
9 cost them.

10 MR. ROSENTHAL: Right. But what I'm
11 saying is there's very little -- I mean they don't,
12 and we don't know what it's going to cost them
13 because the study hasn't been done, but they've
14 bought the railroad, right? I mean they've spent the
15 money. I'm not sure what there is to accept.

16 Now, they could decide, I guess, that
17 before further scrambling the egg, before making
18 other changes, they want to do the study so they can
19 see what it will ultimately cost them and that's a
20 decision that they can make. That's fine. They
21 don't have to go forward with the transaction.

22 You can give them time, give them time to

1 do a study and then they can decide whether to accept
2 or reject the condition. I mean there's different
3 ways to handle it, but I mean you're right to be
4 concerned, but it's up to them to decide, do we want
5 to further scramble the egg if we decide at the end
6 that it's too expensive to do, but that's their
7 decision to make.

8 BOARD MEMBER HEDLUND: I'll tell you what
9 I'm really concerned about, and it comes from the
10 experience east of Houston where a passenger railroad
11 and two hosts have been negotiating with each other
12 for years and if the host railroads want to not
13 cooperate there are a million ways they can do that,
14 so that's what I'm concerned about. I assume that
15 you would negotiate in good faith, but we've seen
16 another example where questions about that have been
17 raised.

18 And also, to the point of Amtrak, just a
19 minor point, Amtrak has two trains through there a day or
20 at least they did before COVID. I don't know what
21 the current schedule is, but I would note that that
22 route of the Sunset Limited has just about the lowest

1 on-time performance of any long-distance route in the
2 country, so they ought to be very concerned about
3 what's going on in Houston, but they have not
4 expressed any concern about that. And indeed, have
5 put a letter in the record that they support the
6 arrangement subject to some conditions, none of which
7 have anything to do with Houston, so that puzzles me
8 a little bit.

9 And then the third thing is also going to
10 the experience on this other question. You mentioned
11 that they haven't taken into account future growth by
12 BNSF or UP on this line. Are you saying that they
13 should pay not only for the additional capacity
14 required to carry their trains, but also the capacity
15 to accommodate future growth of your trains and BNSF?

16 MR. TURNER: No. What we're saying is --

17 BOARD MEMBER HEDLUND: Good.

18 MR. TURNER: If you're going to do an
19 analysis that says that you've got all this excess
20 capacity, which is what they actually put in their
21 reply, you have to consider all of the factors and
22 those factors are I assume the BNSF. There are some

1 larger customers, unit train facilities, in and
2 around this bridge that traverse this bridge to get
3 to the facilities to go to Port Arthur and Beaumont
4 and other facilities in and around there and we're
5 saying you have to account for that in your planning
6 and it's not. It's simply not in their analysis.

7 BOARD MEMBER HEDLUND: But the
8 implication of that, I think, is that you're saying
9 that if they have to account for it, then maybe they
10 have to pay for it. This is what I do not
11 understand.

12 MR. ROSENTHAL: No, I think what they're
13 saying -- you asked three questions.

14 BOARD MEMBER HEDLUND: Yes.

15 MR. ROSENTHAL: To deal with the first
16 one is how do you deal with the level of maybe
17 distrust about negotiation and I think one of the
18 possible solutions was brought up yesterday. Let's
19 bring in some expert, all these railroads have
20 companies they use to help analyze these --

21 BOARD MEMBER HEDLUND: I know there are
22 ways, but hopefully it would be shorter. Hopefully,

1 people would cooperate, but there is some experience
2 out there with host railroads who are opposed,
3 fundamentally, to a transaction, dragging their feet
4 and dragging things out literally for years

5 MR. ROSENTHAL: I understand the concern
6 and I think there has to be maybe some timeframe for
7 getting an expert together or getting the expert
8 started and running on their timeframes. I think
9 we're committed to working with that sort of process.

10 I think there's an easy solution, but I
11 don't think there's an easy solution to Houston where
12 they're talking about putting in eight trains. And
13 again, if you think the evidence is that there aren't
14 going to be any problems, okay.

15 BOARD MEMBER HEDLUND: Again, it's eight
16 trains, but it's four in one direction and four in
17 another direction.

18 MR. ROSENTHAL: It's four in one
19 direction --

20 BOARD MEMBER HEDLUND: It's not eight
21 trains on necessarily all on the same track.

22 MR. ROSENTHAL: Not all on the same

1 track, but you can look at the route and you can see
2 that from --

3 BOARD MEMBER HEDLUND: No, I understand.

4 MR. ROSENTHAL: There are portions where
5 there are eight and then there are portions where UP
6 -- but to the point about payment, what John was
7 saying is that a lot of their studies say, okay,
8 we're going to add eight trains and that's all we
9 have to worry about in three years. So, is Houston
10 going to have capacity in three years if we add these
11 eight trains?

12 What John was saying is if you really
13 want to worry about what Houston's going to look like
14 in three years, you have to look beyond the
15 Applicants eight trains and think is Amtrak going to
16 have another train going through, is UP going to add
17 more starts because Houston's a growing area, is BNSF
18 going to have to add. It doesn't mean they have to
19 pay, but it means that in planning something you
20 can't say, oh, there's room for eight trains,
21 therefore, we don't need to worry.

22 CHAIRMAN OBERMAN: Any other questions?

1 (No response)

2 CHAIRMAN OBERMAN: I think we're done for
3 the moment. Thank you. Thank you both for your
4 patience. I am making an executive decision and that
5 is that we were hoping we had a few short witnesses
6 who wanted to be heard this afternoon. I'm not even
7 sure that they want to be heard. It's very late.
8 Everybody, I believe, has had enough for today. So,
9 we're not going to hear any more witnesses today. A
10 few procedural announcements.

11 We are going to convene virtually Monday
12 at 1:30 Eastern and we will go for about four and a
13 half hours. We may get through all of
14 the witnesses, but if not, we'll convene again at
15 9:30 Eastern on Tuesday and go no later than 1:00 to
16 finish all of the other witnesses. And I'm confident
17 that within those timeframes we will finish.

18 There are no more railroads, which takes
19 a lot of time. I mean I suppose another railroad
20 could pop up over the weekend. And then we will
21 convene at 10:30 Eastern on Thursday for CP's
22 rebuttal. All of these will be virtual, and I think

1 we have nothing else on that day. Hopefully, it
2 won't take more than three, four, five, six hours --
3 whatever it takes, CP will have ample time for its
4 rebuttal.

5 A scheduling Order will come out. It is
6 obvious that the original plan to have final briefs
7 due on October 14, which was two weeks after this
8 hearing, will have to be extended. I would suggest
9 that we may tweak it a day or two. That will be
10 October 20th. We do not plan to change the final
11 comments on the EIS process. That will stay at
12 October 14th because these hearings are not about the
13 environment. So, people who are listening who want
14 to be heard on that, that deadline will stay the
15 same.

16 I anticipate, I don't want to prejudge it
17 because I really don't know what the Board is going
18 to do, but there were a number of issues raised about
19 representations made by CP. CN raised a number of
20 questions. There were questions raised here in this
21 proceeding that I anticipate that CP may want to deal with in
22 their briefs because there may not be time to answer

1 all of those by next Thursday. That's up to CP.

2 And I think we'll focus on that before we
3 close out next Thursday, but that may mean that if
4 there is stuff that CP wants to submit to us in
5 response to some of the things that have been raised,
6 there may be a need to give others an opportunity to
7 comment on anything new that CP has that responds to
8 these issues that have been raised. So, I'm not
9 prejudging it. Right now, I think you should assume
10 the final briefs will be roughly October 20th, but
11 there may be a little time. It'll be short, if there
12 is, a week, 10 days, something like that.

13 As I think most people know who follow
14 this process, under the NEPA law, the Board cannot
15 finally resolve this issue until the environmental
16 process is done. That is a time-consuming process,
17 and it is our intent that if we extend the briefing
18 that it will not extend the overall date by which we
19 are ready to rule on this because we still have to
20 wait for the environmental folks to finish and that's
21 going to take a little while.

22 I'm not at liberty to tell you what our

1 time estimates are, not on the record, so I hope
2 everybody understands that. And I'm handed a note
3 that my ambition that we might actually finish on
4 Monday is, as usual, overstated because there were
5 some people who cannot appear Monday, can only appear
6 Tuesday, so we will have to convene for some time on
7 Tuesday. And we are cognizant that Tuesday evening is Yom
8 Kippur, so we're going to end early afternoon to
9 accommodate everybody who needs to get out of here.

10 So, with that, I think I speak for all of
11 us by saying we are really appreciative of the
12 tremendous amount of effort that's gone into these
13 presentations. We cannot function without all
14 stakeholders' input. It's been enlightening.
15 There's a lot for us to chew on and we're not done
16 with the hearing, so we will see you all on Monday at
17 1:30 Eastern. So, thank you all. Those who are
18 leaving, including me, safe flights and we'll see you
19 and have a good weekend.

20 (Whereupon, the hearing was adjourned.)

21

22

CERTIFICATE OF COURT REPORTER

I, GAYNELL CATHERINE, Court Reporter, do hereby
certify that that the testimony contained herein is a
true record of the testimony given by said witness,
and I further certify that I am neither attorney nor
counsel for, related to, or employed by any of the
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taken; and, further, that I am not a relative or an
employee of any attorney or counsel employed by the
parties hereto, or financially interested in the
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GAYNELL CATHERINE

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