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Procter & Gamble

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Surface Transportation Board
Office of the Secretary
1925 K Street, NW
Washington, DC 20423-0001

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Dear Secretary Williams,

Reference STB Ex Parte No. 582 (Sub-No. 1).

The purpose of this letter is for The Procter & Gamble Company (P&G) to provide comments, perspective, and proposals to the STB relative to the above referenced proposed rulemaking procedure. P&G is a major manufacturer of consumer products that are distributed worldwide with sales exceeding \$38 Billion annually. Rail is a key mode of transportation for our inbound and interplant bulk materials, as well as outbound chemicals. Our annual rail shipment volume is over 27,000 carloads, and we use all of the major Class I railroads along with several regional railroads for these rail shipments. P&G supports the STB's decision to revisit its approach to competitive issues, service performance issues, and other general issues related to the current rail merger policy. P&G appreciates being given the opportunity to make comments on these important rule changes.

The comments outlined below address five of the nine issues that were suggested in the STB decision document (STB served March 31, 2000). The issues below are listed in order of priority relative to the various rule changes that P&G would like to see implemented.

Promoting and Enhancing Competition

P&G is supportive of a change in rail merger policy that would lead to the enhancement, rather than just the preservation, of rail competition. The collective impact of mergers over the past 10 years has lead to an overall reduction of rail competition for most shippers, and a greater emphasis on enhancing competition would help offset this loss. P&G believes that competition benefits both shippers and railroads, and ultimately the consumers who purchase our products. Competition not only leads to rate benefits for shippers, but it also helps to produce improved and more reliable rail service. Over the past several years, P&G has accumulated numerous data points that demonstrate how rail pricing fluctuates directly with the level of competition, and how rail service issues get resolved faster when competition is available.

However, before looking at enhancing competition, existing rail competition must be preserved through any future rail mergers. The factors contributing to the erosion of competition in future mergers will expand from the common forms such as closed gateways, the reduction in the number of railroads available to a shipper's facility, and terminal area competition to more subtle forms such as discriminatory rates that are designed to divert traffic from competing railroads and rate increases on less-desirable/inefficient routings to discourage the use of these routings by shippers. Approval of the proposed BNSF/CN/IC combination would be a case in point. For example in this case, shippers that are captive on the BNSF in Texas that move materials to Canada to locations that are open to both the CN and the CP are at a high risk of being subjected to discriminatory rates designed to keep the freight on the combined BNSF/CN/IC versus allowing it to go to the CP. This type of pricing would eliminate the CP as a competitor for these shippers by virtue of higher rates with the BNSF-CP routing. This type of situation will in essence include all shippers in North America that are captive on the BNSF, CN or IC shipping to locations that are currently open to either the CP/CN, the UP/BNSF or the KCS/BNSF as examples. The

current rail merger policy will need to be modified to account for these new ways of eliminating competition in order to just preserve the current level of competition in today's rail system.

Relative to enhancing competition, P&G is supportive of any changes that will accomplish this goal either in specific areas or across a broad portion of the rail system. However, P&G believes that the probability of enhancing competition, as part of a process that allows additional mergers of Class I railroads, will be very low. Significant changes in merger rules will be required just to hold competition at its current level if the number of Class I railroads is allowed to decrease.

At a minimum, P&G would like to see the following additions to the current rail merger policy.

- Merger applicants should be required to maintain open gateways for all major routings at reasonable rates. Permanent rate protection will be necessary to ensure that merger applicants do not make targeted gateways cost prohibitive for shippers to use, thereby forcing shippers to other gateways that are more efficient for the merger applicants.

- Merger applicants should be required to provide switching, at an agreed-upon fee, to all exclusively served shippers located within or adjacent to terminal areas.

- "Inter-switching" provisions similar to those used in Canada (published in Sections 127 and 128 of the Canada Transportation Act) should be adopted gradually over time across the board as opposed to just merging carriers. These provisions would provide for the right of a shipper located on one railroad to obtain competitive switching to another railroad for pre-established fees based on the distance of the move. These provisions should enhance competition without causing capacity or physical access issues for the switching carrier.

- Carriers should be required to offer contracts for the competitive portion of joint-line routes when the joint-line partner has a bottleneck segment.

- Carriers offering origin to destination service should be required to quote rates over bottlenecks at operating interchanges with other carriers. This should be required without the need for a competitive access case.

"Three-To-Two" Issues

As the number of Class I railroads decreases, "three-to-two" issues can quickly turn into "two-to-one" issues. Consequently, both of these types of issues should receive more attention in merger proceedings, and greater weight should be given to arguments of competitive harm in those situations where the number of rail carrier alternatives within a corridor would be reduced by a merger from three to two, or worse yet, from two to one.

This issue should no longer be left to a case-by-case examination based on the individual circumstances of each case. The reduction of Class I railroads has created the need to look broadly at the new rail system that will result from any future merger, and to scrutinize major gateways, touch points of the merging railroads, and areas of heavy rail traffic for potential creative solutions that will address large areas as opposed to individual circumstances. An excellent example of this approach is the Shared Assets Area concept in the CSXT/NS/Conrail transaction. Rather than examine issues on a case-by-case basis, the CSXT and the NS developed a solution that actually gave greater flexibility to several shippers in these operating areas. Reapplication of this type of solution will need to be more of the norm with the potential of a reduced number of Class I railroads operating in North America.

"Three-to-two" issues, however, will quickly be replaced by numerous "two-to-one" issues if the number of Class I railroads continues to decrease. This will further increase the importance of examining these types of issues on a broader versus individual basis. Approval of the proposed BNSF/CN/IC combination would be a case in point. For example in this case, shippers in Memphis that are currently served by the BNSF and the IC will find that this proposed combination will suddenly leave them with one railroad versus two. Working on this issue on a case-by-case basis would not be efficient, especially when there are

several other cities/shippers that will have similar problems from the proposed combination used in this example.

"Downstream" Effects

Given that there are only six major Class I railroads remaining in North America, P&G believes that the elimination of the "one case at a time" rule at 49 CFR 1180.1(g) would be an appropriate step to take at this time. The last round of mergers has demonstrated that most of the Class I railroads are willing to merge to address the concerns they have relative to their ability to build market share. Upon the announcement by the BNSF and the CN of their intent to form North American Railways, clear written statements were made by other Class I railroads that they would be "forced to develop strategic responses" to this proposed combination. Based on the last round of mergers, it is easy to assume that one of the "strategic responses" could be more mergers, and this cannot be ignored when there are so few Class I railroads remaining.

With the elimination of the "one case at a time" rule, merger proceedings would then include the examination of the likely "downstream" effects of a proposed transaction, including the likely strategic responses to that transaction by non-applicant railroads. The impact of these strategic responses would need to be considered against each of the other elements of the merger policy for the applicant railroads. In addition, if any of the strategic responses included more mergers, it should be a requirement to stop the merger proceedings until such time that all of the proposed mergers can be reviewed against the merger policy as a package.

Safeguarding Rail Service

Recent railroad mergers have caused significant financial harm to P&G's business, as well as the businesses of other shippers. As a result, there is a need for additional safeguards in the merger review process so that any future rail mergers would not cause such harm. It is not reasonable for merging railroads to view it as normal for such a transaction to cause service disruptions to the point of harming a shipper's business. Railroads need to be held accountable for their business decisions, and if they are not willing to accept financial accountability, the merger should not be approved. Specific conditions that should be included in the review of future mergers are as follows:

- Merging railroads should be required to pay 100% of all premium freight expenses (usually trucking) incurred by a shipper as a direct result of merger-caused service disruptions. A mandatory 3rd party arbitrator should be set up in advance of the merger to settle in an expedited manner any disputes that may occur relative to this requirement. In addition, this requirement should not be dependent on any contract/contract language between the shipper and the merging railroad.

- To minimize the financial harm done by merger-caused service disruptions, shippers should be automatically allowed to break any contracts with a merging railroad to switch to an alternate rail carrier. This action should be triggered by the shipper in response to any potential shutdown situations, as opposed to being a result of a specific period of poor service by the merging railroad. Again, this requirement should not be dependent on any contract/contract language between the shipper and the railroad.

- Merging railroads should be required to pay 100% of any additional rail car lease expenses incurred by a shipper as a direct result of merger-caused service disruptions. Again, a mandatory 3rd party arbitrator should be set up in advance of the merger to settle in an expedited manner any disputes that may occur relative to this requirement, and this requirement should not be dependent on any contract/contract language between the shipper and the merging railroad.

For future mergers, the measures used to determine the extent of any service disruptions should be changed as they apply to safeguarding rail service issues. The evaluation of service should be done on a lane-by-lane basis as opposed to using system-wide averages. Total transit times (including switching and interchanging) should be measured for affected origin-destination pairs, and an increase of over 10%

in transit times above pre-merger averages would be used as justification for shippers to use alternate modes of transportation to keep their businesses operational. A fleet assessment using this data should be the basis to justify the need for shippers to add rail cars to their fleets to compensate for poor service.

Merger-Related Public Interest Benefits

In past mergers, P&G has seen very few of the claims made by the merging railroads materialize relative to the benefits that would be produced by the merger. In most cases, the claims of benefits were relatively general, difficult or impossible to measure, not time-bounded, and they were typically business projections that looked mostly at the merging railroads' part of the new system as opposed to the overall system results including the impact to the shippers. Claims of benefits such as "economies of scale required to support e-business initiatives to increase efficiency and productivity of both customers and railroads", "faster transit times, more reliable service, and better information to customers", "access to new markets throughout North America" and "the combination will enhance U.S. efforts to be both price and product competitive in export markets by providing an efficient rail transportation system that encourages a more even balance of trade" are typical of the general statements made that are hard to translate into expected results that any given shipper will see within a reasonable time after the merger is completed.

P&G believes that claims of public interest benefits should be rejected by the STB unless these claims are supported by data. Merging railroads should be required to present an analysis of the current situation relative to the expected benefit, the plan to make the changes required to produce the benefit, how the benefit will be measured, and how these changes will contribute to closing the gap between the current situation and the expected future state. General statements about expected benefits that are not supported by a plan and data have no value to shippers and are merely projections of what may happen as a result of the merger as opposed to what will happen as a result of the merger. The plan, the data, the measures, and the gap analysis then become a tool for the STB to measure whether or not the benefits claimed have really materialized after the merger is completed.

In situations where merging railroads do present a plan with data for their claims of public interest benefits, the STB should require an analysis from the merging railroads on what prevents these benefits from being achieved without a merger. Concepts such as marketing alliances with other railroads, cooperative operating practices, and improved information systems should be addressed in this analysis. The discussion should lead to an explanation of why the proposed plan can only be accomplished by merging railroads versus independent railroads working together as a team.

Conclusion

In general, the analysis required to understand the impacts of any future Class I railroad mergers will be far more complex than in mergers of the past. The continued reduction of Class I railroads creates the need for a much more detailed examination of the subtle impacts to shippers that will occur across potentially all of North America as opposed to only a particular region of the United States.



Michael R. Benoit
North America Rail Process Manager
The Procter & Gamble Company

CERTIFICATE OF SERVICE

The undersigned hereby certifies that on the 10th day of May, 2000, he served a true and correct copy of the above and foregoing document on all parties of record on the Service List (Appendix A of the Notice To Parties in this proceeding served April 28,2000) in accordance with the Surface Transportation Board's Rules of Practice by:

☒ United States mail, first class postage prepaid

☐ Facsimile transmission

☐ Hand delivery



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