

COVINGTON & BURLING LLP

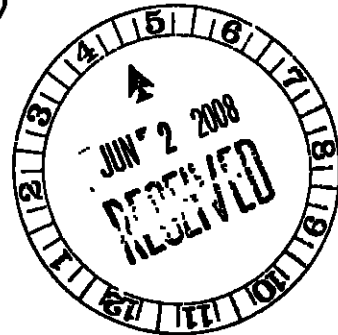
1201 PENNSYLVANIA AVENUE NW
WASHINGTON DC 20004-2401
TEL 202 662 6000
FAX 202 662 6291
WWW COV COM

WASHINGTON
NEW YORK
SAN FRANCISCO
LONDON
BRUSSELS

MICHAEL L. ROSENTHAL
TEL 202 662 5448
FAX 202 778 5448
MROSENTHAL@COV.COM

June 2, 2008

222503



BY HAND

Honorable Anne K. Quinlan
Acting Secretary
Surface Transportation Board
395 E Street, SW
Washington, DC 20423-00001

Re: Docket No. 32760, Union Pacific Corporation et al. – Control and
Merger – Southern Pacific Rail Corporation, et al.

Dear Secretary Quinlan:

Enclosed for filing in the above-captioned proceeding are the original and ten copies of Union Pacific Railroad Company's Reply to BNSF Railway Company's Petition for Clarification (UP/SP 408). Also enclosed is a disk containing the text of the filing in Word format

An additional paper copy of this reply is also enclosed. Please return a date-stamped copy to our messenger

Thank you for your attention to this matter.

Sincerely,

Michael L. Rosenthal

cc: All Parties of Record

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222503

UP/SP 408

BEFORE THE
SURFACE TRANSPORTATION BOARD

Finance Docket No. 32760

UNION PACIFIC CORPORATION, UNION PACIFIC RAILROAD COMPANY
AND MISSOURI PACIFIC RAILROAD COMPANY
– CONTROL AND MERGER –
SOUTHERN PACIFIC RAIL CORPORATION, SOUTHERN PACIFIC
TRANSPORTATION COMPANY, ST. LOUIS SOUTHWESTERN RAILWAY
COMPANY, SPCSL CORP. AND THE DENVER AND
RIO GRANDE WESTERN RAILROAD COMPANY



UNION PACIFIC RAILROAD COMPANY'S REPLY
TO BNSF RAILWAY COMPANY'S PETITION FOR CLARIFICATION

J. MICHAEL HEMMER
LAWRENCE E. WZOREK
WILLIAM G BARR
JEFFREY S. ASAY
Union Pacific Railroad Company
1400 Douglas Street
Omaha, Nebraska 68179
Telephone: (402) 544-5000
Facsimile (402) 501-3393

MICHAEL L. ROSENTHAL
Covington & Burling LLP
1201 Pennsylvania Avenue, N.W.
Washington, DC 20004
Telephone: (202) 662-6000
Facsimile: (202) 662-6291

Attorneys for Union Pacific Railroad Company

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BEFORE THE
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UNION PACIFIC RAILROAD COMPANY'S REPLY
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The Board should deny BNSF's Petition for Clarification of the Board's decision served May 1, 2008 (Decision No. 103). In Decision No. 103, the Board clearly and correctly held that BNSF could not have obtained broader trackage rights than those imposed as a condition in *UP/SP Merger* without Board authorization, and that BNSF could not obtain Board authorization unless "the parties mutually agree to broader trackage rights." Decision at 7.

In this Reply, we address three points raised by BNSF's Petition. *First*, we explain why Decision No. 103 correctly held that trackage rights must be based on a mutual, voluntary agreement, not the exploitation of a mistake. *Second*, we explain why, contrary to BNSF's claims, the Board's decision does not place a cloud on modifications to trackage rights in other merger-related settlement agreements. *Third*, we explain that BNSF could, through a voluntary agreement with UP, address the City of Richmond issues that led it to exploit UP's drafting mistake.

A. Trackage Rights Must Be Based On A Mutual, Voluntary Agreement.

BNSF's Petition questions the Board's statement that it will not authorize broader trackage rights unless the parties "mutually agree" to them. Decision at 7. BNSF asks the Board to "clarify" that it could obtain Board authorization if it receives an arbitral decision that the parties already have "*contractually agreed* to broader trackage rights," even if by mistake. Petition at 3 (emphasis added).¹

The Board's Decision No. 103 requires no clarification. The Board appropriately cut through the parties' technical arguments about contract law and based its ruling on the law governing trackage rights agreements. The Board correctly held that BNSF needed to obtain separate authorization for the broader trackage rights because they had not been imposed as a condition to address adverse effects of the UP/SP merger. It also correctly recognized that the parties had not reached a voluntary, mutual agreement for the broader rights, as would be required before they could be authorized by the Board.

The Board properly distinguished between (a) "[t]rackage rights imposed as a condition in favor of a named railroad[, which] do not ordinarily require any approval beyond the approval implicit in the imposition of the condition itself," and (b) additional rights, which require separate authorization, such as the rights in dispute here. *UP/SP Merger*, 1 S.T.B. 223, 443 (1996); accord *Burlington Northern/Santa Fe Pacific Merger*, 10 I.C.C.2d 661, 767 (1995). In this proceeding, the Board had directed the parties to modify their settlement agreement to reflect the conditions imposed by the Board, as clarified and supplemented by decisions issued

¹ BNSF has also launched a collateral attack on the Board's decision by filing an arbitration demand on May 29, 2008. As discussed below, UP believes the Board's decision requires no clarification and that BNSF cannot obtain trackage rights unless the parties mutually agree and the Board then acts. UP does not intend to endorse BNSF's collateral attack on the Board's decision by participating in that arbitration proceeding.

subsequent to *UP/SP Merger*. Decision at 4. The Board did not authorize any additional rights. If BNSF believed the Restated Agreement provided for broader trackage rights than those the Board had imposed as conditions to the merger, it should have sought separate authorization for those rights from the Board. Board precedent clearly establishes that a single settlement agreement may include certain trackage rights that are imposed as a merger condition and others that require separate authorization. See *Burlington Northern/Santa Fe Pacific Merger*, 10 I.C.C.2d at 766-67. BNSF certainly knew the rules, given its experience of following them in *Burlington Northern/Santa Fe Pacific Merger*. But it never sought authority to exercise the additional trackage rights in dispute here.

The Board also correctly applied the statutory principle most directly implicated by BNSF's request for clarification: except in specific circumstances defined by statute, the Board may not authorize trackage rights unless the line owner and the party seeking to become the trackage rights tenant have entered into a mutual, "voluntary agreement." *Boston & Maine Corp Trackage Rights Over Conrail*, 360 I.C.C. 239, 244 (1979); see also, e.g., *Arizona Elec Power Coop, Inc. v. Burlington Northern & Santa Fe Ry*, STB Docket No. 42058 (STB served Aug. 20, 2002), p. 7 (trackage rights exist "either as a result of mutually beneficial voluntary agreements or merger conditions imposed to preserve pre-merger competitive alternatives"); *Chicago & North Western Transp Co – Construction & Operation Exemption – City of Superior, Douglas County, WY*, STB Fin. Docket No. 32433 (STB served Jan 12, 1996), p. 2 ("Congress has left, except in certain specifically defined areas, the use of one carrier's tracks by another up to the voluntary agreement of the carriers subject to Commission approval.").

The parties' prior submissions establish that UP never "mutually agreed" or "voluntarily agreed" with BNSF to grant broad trackage rights to move intermodal traffic over its Cal-P Line

via Sacramento. All the evidence shows that UP made a mistake and BNSF exploited that mistake.

BNSF now wants to pursue its contract-law arguments in arbitration – that is, that UP and BNSF “contractually agreed” to broader trackage rights, without regard to whether the parties “mutually agreed” or “voluntarily agreed.” Petition at 3. However, Decision No. 103 correctly recognizes that Board-authorized trackage rights must be based on a mutuality that goes beyond the technical acts that might bind a party under contract-law principles. Accordingly, even if an arbitrator were to rule that UP’s mistake was not excused under contract law, BNSF would not be entitled to Board authority for broader trackage rights under 49 U.S.C. § 11323(a)(6).² The arbitration would be a futile action.

A Board decision to authorize trackage rights is imbued with public interest considerations. See 49 U.S.C. §§ 11324(c), (d). A voluntary agreement to grant trackage rights almost always will be in the public interest. See *Railroad Consolidation Procedures – Trackage Rights Exemption*, 1 I.C.C.2d 270 (1985). As the Board has recognized, when one railroad grants trackage rights to another voluntarily, “(1) trackage rights proceedings generally involve only the applicants and raise no major regulatory issues; (2) managers negotiate trackage rights agreements to make operations more efficient; (3) trackage rights effectively pool costs, reduce operating expenses of the participating carriers and, in turn, promote intermodal and intramodal competition; and (4) participating carriers make agreements that present mutually satisfactory solutions to operational problems.” *Id.* at 272 In addition, a voluntary agreement ensures that

² The Board has frequently noted that the interpretation of contracts lies within the purview of the courts, but the Board still must ensure compliance with statutory standards before authorizing trackage rights. That is, BNSF, as the proponent of a trackage rights application or exemption, would have the burden of establishing that BNSF and UP had entered into a mutual, voluntary trackage rights agreement.

“the lessor receives fair rent for use of its facilities and the public interest is served through the benefits flowing from rationalized rail operations.” *Id*

The Board’s analysis of voluntary trackage rights agreements shows why authorizing trackage rights based on a line owner’s mistake would be contrary to the public interest. If the potential trackage rights tenant cannot persuade the line owner to enter into an agreement voluntarily, it must be because the tenant’s presence would impose substantial costs and inefficiencies on the line owner, skew the competitive balance unfairly, or leave the owner without fair compensation for use of the owner’s line. In any of these circumstances, the Board would be acting contrary to the public interest if it were to impose an uneconomical or anticompetitive arrangement because of the line owner’s mistake.

This case illustrates concretely why involuntary trackage rights are contrary to the public interest. As UP demonstrated in its submissions, BNSF’s exploitation of UP’s mistake is not making operations more efficient, reducing operating costs, resolving operational problems, or rationalizing rail operations. It does the opposite. It is causing congestion and delays to UP’s freight trains and to the passengers who ride on the Cal-P Line. UP faces severe capacity issues on the Cal-P Line and, as a result of the delays, has been required to divert its freight trains to other, much longer routes. These problems will only increase as traffic on the line continues to grow. Adding capacity to the Cal-P Line would be very difficult and expensive, and thus BNSF’s continued unauthorized use of the line would result in congestion that would undermine UP’s ability to compete for traffic moving to and from the San Francisco Bay Area.

Moreover, BNSF’s exploitation of UP’s mistake does not reduce even BNSF’s own operating expenses. BNSF trains must travel an extra 50 miles, consuming extra time, crews, locomotives, and fuel, to use the disputed route over UP. The only costs BNSF saves are the

political costs of operating additional trains through the City of Richmond, and it does so only by transferring costs to UP and the passengers who use the Cal-P Line.

The record in this proceeding clearly established that UP and BNSF had not mutually agreed to broaden BNSF's rights to use the Cal-P Line. As a matter of law and transportation policy, the Board correctly applied its precedent and held that it would not authorize additional BNSF trackage rights over UP's Cal-P Line "unless the parties mutually agree to broader trackage rights." Decision at 7.

B. The Board's Decision Does Not Place A Cloud On Modifications To Trackage Rights In Other Merger-Related Settlement Agreements.

BNSF's Petition incorrectly claims that Decision No. 103 places modifications to trackage rights in other merger-related settlement agreements under a "cloud." Petition at 4. As discussed above, the Board's decision was consistent with established precedent and thus would not undermine any valid expectations about other merger-related settlements on which the parties voluntarily agreed. Moreover, BNSF does not point to any other situation in which merger-related trackage rights have been broadened without a mutual, voluntary agreement or proper authorization.

BNSF specifically references one situation in its Petition – UP's establishing a connection a new intermodal facility from trackage rights obtained in *Burlington Northern/Santa Fe Pacific Merger*. However, the right to establish that connection resulted from a voluntary agreement, and the specific trackage rights agreement implementing that right was submitted to the Board and exempted in post-merger proceedings. See *Burlington Northern/Santa Fe Pacific Merger*, 10 I.C.C.2d at 767; *Rio Grand Indus., Inc , S. Pac Transp Co , The Denver & Rio Grand W R R , St Louis Sw Ry , & SPCSL Corp. – Trackage Rights Exemption – The Atchison, Topeka, & Santa Fe Ry Lines Between Hutchinson, KS, and Chicago, IL, and Between Topeka,*

KS, and Kansas City, KS, ICC Fin. Docket No. 32721 (ICC served Sept 6, 1995). Voluntary trackage rights are not at risk.

C. BNSF Has An Available, Voluntary Solution To Its Richmond Problem That Does Not Require Exploitation of UP's Mistake.

Beyond the BNSF Petition's flawed effort to supplant Board precedent with contract-law principles, the Board should understand that there is an available, voluntary solution to the issues that divide the two railroads – yet another reason BNSF should not be allowed to exploit a mistake.

UP recognizes that BNSF faces severe political resistance to expanding rail traffic on its own line through the City of Richmond. Neither railroad benefits from BNSF's creating more political opposition to its operations.

Conversely, BNSF's current solution to its Richmond problem – exploiting UP's mistake – imposes unacceptable operating burdens on UP and the many passenger trains that operate over the Cal-P Line. UP faces a combination of (a) severe criticism whenever passenger trains are delayed on the Martinez Subdivision and (b) potentially unsolvable capacity constraints on the Subdivision, especially on a segment of tracks nestled between steep hills and the Carquinez Straits well beyond Richmond. Neither railroad benefits from BNSF's trains causing congestion on this line, delaying passenger trains, or operating via a highly circuitous route over UP that consumes railroad resources and costs shippers many hours of delay.

The parties have an available solution. In their settlement in *UP/SP Merger*, the parties agreed that BNSF may build a connecting track from UP's Cal-P Line just north of Richmond to the nearby BNSF line, so that BNSF can enter and exit UP's mainline and access its own

mainline toward Stockton.³ This would allow BNSF to use UP's line for a short distance to avoid expanding traffic on its own line through Richmond, without delaying passenger trains and consuming valuable capacity on the Cal-P Line all the way north to Sacramento.

UP has been, and remains, willing to facilitate this solution. UP would be happy to grant the necessary, voluntary trackage rights to support this solution, which would require removing the restriction on BNSF's right to use the Cal-P Line for just the short distance required for BNSF to avoid moving trains through Richmond. It appears to us, however, that as long as BNSF hopes to take advantage of using UP's tracks via Sacramento, BNSF lacks sufficient incentive to pursue the rational, voluntary solution.

Respectfully submitted,



MICHAEL L. ROSENTHAL
Covington & Burling LLP
1201 Pennsylvania Avenue, N.W.
Washington, DC 20004
Telephone. (202) 662-6000
Facsimile. (202) 662-6291

J. MICHAEL HEMMER
LAWRENCE E. WZOREK
WILLIAM G. BARR
JEFFREY S. ASAY
Union Pacific Railroad Company
1400 Douglas Street
Omaha, Nebraska 68179
Telephone: (402) 544-5000
Facsimile: (402) 501-3393

Attorneys for Union Pacific Railroad Company

June 2, 2008

³ The trackage rights agreement implementing the BNSF's trackage rights from Denver, Colorado to Stockton and San Jose, California, expressly allows BNSF to construct a connection from the Cal-P Line to its own line. See *UP/SP Merger*, STB Fin. Docket No. 32760, Applicants' Submission of Final Settlement Agreement and Implementing Agreements With BN/Santa Fe (UP/SP-266), dated June 28, 1996, Ex. B, Denver-Stockton and San Jose Agreement § 6(d) ("[BNSF] shall, at a later date, have the right to have a connection constructed, at its sole cost and expense, at Richmond, in the vicinity of SP's Milepost 15.0.")

CERTIFICATE OF SERVICE

I, Michael L. Rosenthal, certify that on this 2nd day of June, 2008, I caused a copy of Union Pacific Railroad Company's Reply to BNSF Railway Company's Petition for Clarification to be served by email and by hand on the following.

Adrian L. Steel, Jr.
Evan P. Schultz
Mayer, Brown, Rowe & Maw LLP
1909 K Street, NW
Washington, DC 20006

and by first-class mail, postage prepaid, on the following:

William A. Mullins
Robert A. Wimbish
Baker and Miller PLLC
Suite 300
2401 Pennsylvania Avenue, NW
Washington, DC 20037

Christopher A. Mills
Slover & Loftus
1224 17th Street, NW
Washington, DC 20036-3003

Gordon P. MacDougall
1025 Connecticut Avenue, NW
Suite 919
Washington, DC 20036



Michael L. Rosenthal