STB FD-32760(SUB30) 7-8-98 A ID-189672 9 OF 13

(BN/Santa Fe's full Operating Plan and Progress Report are attached hereto as Exhibit A.)

For ease of presentation, this summary is organized into the following subject areas: line purchases, dispatching, preparation for direct BN/Santa train service, start-up interim haulage, and start-up of direct BN/Santa Fe service.

1. Line Purchases. BN/Santa Fe's purchases of the three UP/SP line segments set forth in the BN/Santa Fe Agreement are proceeding under the following schedule:

* Dallas to Waxahachie, TX: The closing took place September 20, 1996.

* Iowa Jct.to Avondale, LA: The closing is planned for no later than December 16, 1996.

* Bieber to Keddie, CA: The closing is planned for no later than December 16, 1996.

2. Dispatching. BN/Santa Fe plans to implement the dispatching protocol required under the CMA Agreement on or before December 16, 1996.

BN/Santa Fe will assume direct dispatching control on each of the three purchased segments. Necessary notices to affected employees were issued the week of September 16, 1996.

Closing and control dates are planned to coincide as closely as possible under the following schedule:

* Dallas to Waxahachie: Dispatching control from BN/Santa Fe's Fort Worth, TX Network Operations Center was assumed on September 21, 1996.

* Iowa Jct. to Avondale: Dispatching control from Fort Worth is planned to immediately follow the closing, which is to occur no later than December 16, 1996.

# Competition Policy In Communications Industries: New Antitrust Approaches

Prepared Remarks of Robert Pitofsky
Chairman, Federal Trade Commission

Glasser LegalWorks Seminar on Competitive Policy in Communications Industries: New Antitrust Approaches

March 10, 1997
Washington, D.C.

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Recent developments in the communications industries show a steady movement from direct regulation to increased reliance on free market incentives. As a believer in the efficiency of market incentives, I regard elimination or substantial reduction of regulation, assuming competition is a feasible alternative, as a good result. Of course, deregulation should be accompanied by a greater role for fundamental antitrust analysis and enforcement, lest the old shackles be replaced by new ones of private manufacture.

One theme of my remarks today is that antitrust, if it is to be effective in these newly deregulated areas, must take into account the special circumstances of each industry. Different sectors of the communications industry were regulated for different reasons, and the transition of various sectors to a free market may be complete or incomplete. As long as antitrust adheres to its tradition of paying careful attention to the facts of each industry, it can play a useful role.

Today I would like to offer some general observations about the transition from regulation to free market incentives and then address more specifically what is "new" about antitrust approaches in the communications industries. In examining what is new, I will in several instances draw examples from the Federal Trade Commission's recent action in requiring restructuring of the proposed deal involving Time Warner-Turner-TCI and then its approval of the transaction as restructured. As always, let me remind you that the views I express today are my own and do not represent the views of the Commission or any other Commissioner.

## A. General Observations

Let me begin by outlining a few principles that apply across the board to newly deregulated industries.

*First*, participants in a deregulated industry, accustomed to coordinated action among themselves or the protection of regulators who guarantee a monopoly franchise, often seek to extend anticompetitive aspects to a newly deregulated regime. Cartel behavior in place of government price restrictions is a classic example. In my own limited experience, this has not been a problem with respect to networks, cable distribution and cable programming. But there can be strong incentives for incumbents to keep new entrants out of what used to be the incumbent's protected domain. Obviously, that can be a problem.

*Second*, transition out of regulation is almost never complete and immediate. Rather, a patchwork of state, federal and international rules on protection from competition continues to apply. Serious regulatory problems arise where some players in an industry are regulated and some are not, with the unregulated free to raise or cut prices in pursuit of various competitive strategies. It is difficult and often unfair to try to maintain a system for long where direct competitors are subject to radically different regulatory rules. For example, many believe that a principal reason truck transportation was regulated for a time in the United States is because railroads were regulated, trucks were not, and competition between the two was impossible to maintain on anything approaching a fair basis. In a deregulatory environment, we should always be looking for ways to equalize treatment by reducing regulatory burdens on incumbents rather than by increasing them on new entrants.

*Third*, some policy goals can be handled comfortably in a regulatory regime but are not congenial to antitrust enforcement. During a transition some continuing regulation may be necessary -- for example, caps on cable rates or mandated access to local markets -- to assist during the period before full competition emerges.

*Fourth*, as a result of the first three points, application of antitrust to newly deregulated industries often involves unconventional issues from the point of view of traditional antitrust. The very fact that an industrial sector was regulated suggests the possibility of some past market failure, or at least some competitive peculiarities (or perhaps what the legislature thought were peculiarities), and therefore calls for a special sensitivity in applying conventional antitrust rules.

**B. What is "new" about antitrust approaches in communications industries?**

While antitrust fundamentals can apply to the communications industries, those industries are not the same as steel mills and grocery stores and therefore call for adjusted approaches.

Let me list six points which if not entirely new are at least different.

*First*, the principal antitrust concerns in communications markets usually involve unilateral rather than coordinated effects.(1) In communications markets, products are highly differentiated, transactions between suppliers and distributors are often not observable, buyers are large and sophisticated -- all contributing to the fact that coordinated effects, *i.e.*, price fixing or conscious parallelism, are not likely. For example, in the Time Warner-Turner merger, both companies were exceptionally large producers of cable programming. But, cable programming is highly differentiated: There are news offerings such as CNN, movie channels such as HBO, sports channels, family channels, cartoon channels, etc. Even if the merger significantly increased concentration in cable programming, demonstrating coordinated effects in the pricing of such programming may have been possible but certainly would have been difficult.

*Second*, because of the dynamic nature of markets and the impact of new technologies, the primary concern in communications arrangements is often access. That is because the entry of new technologies, and firms, is likely to dissipate market power over time, and so markets will tend to be self-correcting unless entry is impeded in some way. That in turn implicates vertical relationships between players in the market, because one method of exclusion is to deny access to critical inputs. Thus, one central aim of antitrust should be to protect the ability of markets to eliminate private restraints and reinvent themselves by precluding private restrictions on access to inputs that are critical to competition. Much of the order in *Time Warner* was designed to prevent the company's large cable subsidiary from discriminating against new programmers (who might compete with company-owned CNN and HBO), and preventing Time Warner's large programming business from discriminating against new methods of distributing programming to households in competition with its downstream cable companies.

One of the most difficult problems in antitrust analysis arises where a firm, or a group of firms through joint venture, obtains a bottleneck position in a marketplace. In some situations, customers and suppliers cannot survive in the marketplace without access to the bottleneck product or service, and rivals cannot effectively compete.

Antitrust sometimes requires that a monopolist or joint venture with enormous market power make its product or service available to all on fair and nondiscriminatory terms. An example is the *Terminal Railroad* case.[(2)] There, a group of 14 railroads owned the Terminal Railroad Association of St. Louis. The association controlled, through acquisitions, the two bridges and one ferry service that could be used to transport railcars across the Mississippi River at St. Louis. The river ran between St. Louis and East St. Louis, so railroads had to use bridges or ferries to get across the river, and terminal facilities were needed to connect individual railroads to the bridges and ferry facilities. One peculiarity of the situation was that none of the 24 railroads that served St. Louis had a line that passed all the way through. All of them had a terminus on one side of the river or the other, so interconnection facilities were essential to serve both St. Louis and East St. Louis, and points beyond. Thus, none of the railroads could transport railcars across the river without using the association's facilities.[(3)]

Since there was no other economically feasible way to get railcars across the river at St. Louis, the joint venture had market power. One remedy option was to undo the acquisitions, so there would again be two or three independent companies operating the facilities. The Supreme Court did not select that option as its remedy of choice, because it found that consolidation of the facilities provided substantial efficiency benefits and that the unified terminal system was of "great public advantage."[(4)] Instead, the Court ordered that the joint venture membership be open to any present or future railroad on "just and reasonable terms" that would place all railroads on a level playing field. In addition, any railroad that did not elect to become a member was to be given access to the terminal facilities, again on "just and reasonable terms."[(5)] But the Court may have recognized the difficulty of reaching agreement on what constitutes "just and reasonable" terms, because its fall-back position was to order dissolution of the asset consolidation if the parties could not reach an agreement that was in substantial accord with the access order.[(6)]

A less intrusive form of antitrust solution would simply direct the monopolist not to exclude customers, suppliers and potential competitors for an anticompetitive reason. The *Associated Press* case provides an example of that.[(7)] There, approximately 65% of the newspapers in this country were members of AP, a joint venture news gathering association that prohibited its members from selling news to non-members. The Court found that newspapers that lacked access to AP news were competitively disadvantaged. Moreover, competitors of existing members had to go through special hoops to become members,[(8)] and the incumbents had effective veto power.[(9)] The case is often cited in support of an argument for mandated access to an "essential facility," but the remedial order in that case was actually quite limited. Basically, the Court held that membership may not be withheld through discrimination based on competitive status. Specifically, a member of the joint venture was not to be given the power to exclude a competitor, and the by-laws were to provide that an applicant's competitive status was not to be considered in passing upon the application.[(10)] The reason for that more restrained remedial approach (compared to the one in *Terminal Railroad*) was not made clear in the Court's opinion, but it may have had something to do with the degree of need for access. There were two other sizable news gathering organizations (United Press International and International Press Service), as well as many smaller ones. Newspapers without AP service were found to be at a competitive disadvantage, but the Court did not say that membership in AP was essential for competition to exist.

But there may have been a more fundamental reason for the restrained hand in *Associated Press*. The kind of approach used in *Terminal Railroad*, so like conventional "regulation," is usually a stretch for antitrust. Antitrust rarely mandates access for several reasons: (1) if access is too easy, companies will be inclined to lie back and take no risks on the assumption they can free ride on the earlier investment and energy of their competitors; (2) permitting easy access for competitors can dampen the incentives for firms to undertake risky and costly investments in the first place, unless there are countervailing first-mover advantages; and (3) it achieves little to mandate access unless there is also provision to insure that price and other terms and conditions of sale are "reasonable;" otherwise the monopolist can agree to grant access but introduce terms that are so onerous that as a practical matter access is unavailable. But regulating price and other terms of sale on a continuing basis is exactly the thing that antitrust (as compared to a regulatory agency with ongoing oversight of firms in the industry) is ill-equipped to manage.[11]

*Third*, conglomerate effects are relevant in newly deregulated industries, but the scope of the doctrine is likely to emphasize actual or perceived potential competition. Indeed, since many deregulated firms will have been monopolists, the most important challenges for a time often will be from firms that are not present rivals in the market.

The Federal Trade Commission demonstrated its willingness to challenge a merger for its anticompetitive conglomerate effects in the *Questar* case,[12] which involved a situation not unlike that occurring in communications. The case involved the natural gas market in Salt Lake City, Utah. Questar was an integrated energy company, from natural gas production, interstate pipeline transmission, and local gas distribution. Questar was the only pipeline serving large industrial customers in the Salt Lake City area, who generally bypassed the local utility and purchased gas directly from other sources. Those customers used Questar's pipeline services to transport the gas either directly to their facilities or to the local utility, from which they purchased local transportation service.

Questar sought to acquire from Tenneco a 50% stake in Kern River Gas Transmission Company, which operated another interstate pipeline running through the area and was planning, not coincidentally, to build a lateral pipeline to serve industrial customers in competition with Questar.[13] That was one of the benefits of recent steps to deregulate the natural gas industry. Large customers could select their own suppliers, and contract separately for transportation of the gas. The evidence showed that Kern River was already having an effect on the market, before any lateral hookups were even built. It was actively soliciting customers, and Questar, in response, reduced prices to certain customers. Thus, potential entry was having precisely the kind of effect we would expect, and Questar's monopoly position was clearly threatened, if not already eroded. Questar's response was not surprising -- buy a major piece of the prospective competitor.

The potential competition theory in *Questar* involved primarily the actual potential entry theory, but there was also an element of perceived potential entry.[14] Kern River was an actual potential entrant in that it was actually planning to enter, and entry would have had a significant procompetitive effect on the market. There was also evidence that Kern River was perceived as a potential entrant at an earlier stage. Theory predicts that a perceived likelihood of entry can induce an incumbent firm to engage in limit pricing -- *i.e.*, moderate prices -- to discourage entry. There was evidence of that here. Having strong evidence of both kinds of effects made this a particularly compelling case. Questar offered a settlement, but it would have been too regulatory and it did not address the adverse effect of the acquisition on Questar's incentives to compete aggressively against the new entrant. The Commission authorized its staff to file for a preliminary injunction, and the parties promptly abandoned the transaction. The 50% interest in Kern River that Questar tried to buy was later acquired by The Williams Companies, which already owned the other 50% and had wanted to maintain Kern River's competitive independence.

When the theory of anticompetitive effect turns on actual potential entry analysis -- *i.e.*, but for the merger, the acquiring party would have entered the market independently -- a question arises as to the level of proof required to demonstrate that potential entry down the road would have occurred. In the Federal Trade Commission's 1984 decision in *B.A.T. Industries, Ltd.*,[(15)] a majority of the Commission concluded that a reasonable probability of entry was not enough and that "clear proof" that entry would occur was required. In this case, clear proof meant "concrete plans" such as a capital acquisition plan or a budget drawn up with entry in mind.

I believe the "clear proof" standard is inappropriate and in fact essentially guts the actual potential competition doctrine. Section 7 only requires that the effect of the transaction "may be" to lessen competition, and that has been interpreted in the majority of litigated cases as requiring only a reasonable probability.[(16)] At a more practical level, it is precisely in the most anticompetitive of conglomerate acquisitions that it is least likely that the government or a private party would discover documents assessing the prospects for entry other than by merger.[(17)] I would not impose a "clear proof" standard if a conglomerate merger were to come up today.

*Fourth*, in the communications sector, markets tend to be dynamic and high-tech, and therefore rivalry frequently occurs primarily in the form of competitive innovation. That observation is consistent with the general conclusions of the Federal Trade Commission's staff report on competition policy in high-tech and global markets, that competition in particular market segments increasingly focuses on various dimensions of innovation.[(18)] Tele-communications is an example of that kind of industry.

The fact that a market is "dynamic," however, does not automatically lead to the conclusion that antitrust enforcement has no responsibilities. For example, let's assume it was certain that local cable companies, at present monopolists or near monopolists, would have their market position challenged effectively by direct broadcast satellite transmissions, phone companies moving into the cable market, and even computer screens becoming a medium to transmit the kind of news and entertainment presently on cable. In anticipation of that rivalry, the legislature may decide to eliminate prior regulatory restraints. But the question remains as to *when* this newly introduced rivalry will become effective. Otherwise anticompetitive mergers, long term contracts or distribution arrangements cannot be justified on grounds that eventually their anticompetitive effects will be dissipated by new entry. Even if "eventually" is only 2 or 3 years away, there remains the concern that consumers will be exploited while we wait for the future to arrive.

For example, in *Time Warner*, some believed that new distribution technologies, such as DBS and other digital delivery systems, would put competitive pressures on both cable distributors and programmers to offer quality programming at reasonable prices. But a majority of the Commission, myself included, did not see that in the evidence. Not yet. Alternative technologies such as DBS had only a small foothold in the market, with perhaps a 3% share of all subscribers. Moreover, DBS is more costly, including up-front equipment costs, and it lacks the carriage of local stations. We included DBS in the relevant market, but it did not appear likely that this emerging technology would be sufficient to prevent the competitive harm from the Time-Warner-Turner-TCI transaction. (19) More recently, an investigation of a proposed merger of two head-to-head competitors in cable distribution produced similar kinds of evidence. These two companies competed for the same group of customers in an "overbuild" situation, where more than one cable company is franchised by the local authority to serve the same geographic area. The evidence indicated that DBS may not have been in the relevant market, and was unlikely to constrain anticompetitive conduct in any event.

Another antitrust concern -- mentioned already but worth repeating -- is that it is precisely in a dynamic marketplace that it becomes particularly important to insure that private arrangements do not impede the ability of new technologies to enter the market. Indeed, that is one of the reasons the order in *Time Warner* prevents the company from disadvantaging competitors at the distribution level by discriminating in access to programming.

*Fifth*, antitrust enforcement efforts to preserve and protect access sometimes lead to rather regulatory decrees. Not always, of course. In my view, one of the most important aspects in requiring that the Time Warner-Turner-TCI deal be restructured was the requirement that TCI in effect give up its previous stock position in Turner and move to a stock position in which it had less influence on Time Warner. If TCI and Time Warner, two of the largest cable companies in the United States, had the incentive and ability through stock ownership to influence the behavior of the other or to moderate their own behavior to benefit the other, that could have had a serious effect on the incentive and ability of programming rivals of the two companies to innovate or achieve access to the market.

In other situations, decrees can minimize the degree of regulation and maximize the impact of market forces. The most widely noted aspect of the Time Warner decree was the requirement that Time Warner set aside at least one channel for a news service that would compete with Turner's CNN. Given CNN's dominant position as a 24-hour news service, and Time Warner's strong position as a cable outlet, the merger could have entrenched CNN against future competition. Because of the acquisition, Time Warner had an incentive not to carry a competing all-news service, and a news network seeking to enter the market would have had a difficult time reaching a sufficient number of subscribers to be viable without carriage on Time Warner cable. This was a situation we needed to address. But the remedy was designed to be as non-intrusive as possible -- specifically, making available at least one Time Warner cable channel for 3 or 5 years depending on how Time Warner chose to satisfy the requirement. The Commission recognized that this is an area with First Amendment overtones and therefore left Time Warner free to use its own judgment in choosing the acquirer of the assets and in negotiating the price that it would be paid. Some objective criteria were adopted to insure that the second news service would be a significant competitor to CNN, and for that we relied on CNN's own definition of itself in its contracts with cable companies. My own view is that if an applicant for the channel satisfied the essentials of serving as a rival to CNN -- for example, it was a 24-hour news service but happened not to carry sports -- the Commission should not object to Time Warner satisfying the decree by accepting that applicant.

By citing examples of modest "regulatory" decree provisions, I don't mean to slight the problem. If it is important to protect access, and surely that will be of paramount importance in many dynamic industries, fairly elaborate provisions that protect against barriers to access, by discrimination or otherwise, will often be necessary.

Sixth, because telecommunications markets are complex and dynamic, joint ventures and other strategic alliances will often be a preferred form of doing business. We recognize, partly because the witnesses in our global competition hearings told us so, that American antitrust law with respect to joint ventures and other forms of competitor collaboration is less than clear. It is for that reason that the Commission has authorized its Policy Planning Staff for its next project to develop proposed guidelines for joint ventures and other forms of competitor collaboration.

**C. Institutional Differences**

Perhaps the most important consequences of moving from regulation to antitrust result from institutional differences between the two regimes. Antitrust relies heavily on legal precedent based on a clearly-defined principle of protecting the competitive process and consumer welfare, and cases may be pursued in any of a large number of forums, in both private and federal agency actions. In a regulatory regime, decisions are made by a prescribed agency, and they often try to balance the interests of a wide range of considerations and constituencies.(20) Parenthetically, the Federal Trade Commission has perhaps the best of both worlds: a clear mission and a consistent forum that develops expertise in particular issues over time.

Another difference is that regulatory agencies (and here I am excluding the FTC) have an ongoing relationship with the industry they regulate. That can be good in the sense that they develop a fact base from which to operate and a sensitivity to particular types of problems; it may be bad in the sense that regulators sometimes adopt the viewpoint of the firms that they regulate. Antitrust reaches for rules of general applicability across all industries, although at its best it pays attention to the special facts of particular industries.

Perhaps the most troublesome difference is that if antitrust is to govern, competition policy can derive from decisions in scores of different courts, as federal and state agencies and private parties bring suits to advance their interests. Although the courts do rely on precedent, which should produce consistency in the result, it is not that easy. The facts and the laws are complex, the economics may be even more complex, and the interests of the litigants are diverse. And, frankly, some courts are better at the task than others. The resulting problem is that it may be difficult to discern a coherent, consistent policy. In fact, we have something approaching that situation in the many court cases dealing with long distance and local telephone service in the wake of deregulation. Some would say that is a temporary problem that will tend to disappear once the transition from regulation to competition is complete. But that transition can take a while and the disorder, inefficiency and general mess produced by scores of antitrust cases, often reaching inconsistent results, is not a good thing. Some creative thinking about how to handle those transitional problems in an orderly way would certainly help.

**D. Conclusion**

To sum up the answer to the central question -- what is new in antitrust approaches in communications industries -- the answer is not so much in the basic antitrust rules we apply -- they have been around for years -- but how we apply them. There is, I believe, an increased understanding and appreciation of the difficulty of making regulatory decisions in dynamic markets that will promote the competitive process and other statutory goals without having unintended adverse effects on incentives or the ability of firms to compete. That applies to both regulatory agency decisions and to antitrust. That does not mean that antitrust should be timid in dealing with such industries. On the contrary, antitrust has an important role to play in keeping markets open for competition. But antitrust rules and remedies must be applied with an understanding and consideration of the particular facts of each industry.

1. There may be exceptions, particularly in markets providing alternative conduits rather than content (such as cellular telephone services or two cable companies serving the same area), and especially where products or services are sold to small businesses or individuals and prices are public.

2. *United States v. Terminal Railroad Association*, 224 U.S. 383 (1912).

3. For a detailed presentation of the facts, see David Reiffen and Andrew N. Kleit, *Terminal Railroad Revisited: Foreclosure of an Essential Facility or Simple Horizontal Monopoly?*, 33 J. Law & Econ. 419 (1990).

4. 224 U.S. at 410-11.

5. *Id.* at 411. The analysis by Reiffen and Kleit, supra, questions whether the association actually foreclosed access by non-members. The government's principal theory of the case seems to have been monopolization resulting in high prices, lower service and entry deterrence. *See* Reiffen and Kleit at 432-36.

6. 224 U.S. at 412.

7. *Associated Press v. United States*, 326 U.S. 1 (1945).

8. In part, a new member, if it was fortunate enough to be admitted, was required to pay 10% of the total amount of the regular assessments paid to the association by the old members in the relevant market since October 1, 1900 -- approximately a 40-year period. *Id.* at 10-11. That requirement did not apply to applicants that would not compete with an existing member.

9. What made the situation worse was that in many cities AP members also had contracts with UP and International News Service that required new newspapers to pay a large sum to enter the market. *Id.* at 13.

10. *Id.* at 21.

11. It should be noted that in *Terminal Railroad* and *Otter Tail Power Co. v. United States*, 410 U.S. 366 (1973), another case involving mandated access, the courts could defer to regulatory bodies to determine the proper terms of access.

12. *FTC v. Questar Corp.*, No. 2:95CV 1137S (D.Utah 1995) (transaction abandoned); FTC Press Release, *FTC to Challenge Questar Acquisition of Kern River, Alleging Monopoly Over Natural Gas Transmission into Salt Lake City Area*, Dec. 27, 1995.

13. Kern River was a partnership owned in equal shares by a subsidiary of Tenneco and The Williams Companies, Inc.

14. The district court complaint also pled the loss of actual competition.

15 104 F.T.C. 852, 916 (1984).

16. *See, e.g.*, Philip E. Areeda and Herbert Hovenkamp, Antitrust Law ¶1121'e (1996 Supp.) at 821.

17. To the extent a "clear proof" standard relies on subjective evidence, *see B.A.T.*, 104 F.T.C. at 927-28, agency or court decisions may be based on evidence that is unreliable, because company statements may be motivated by a desire to influence agency review or merger litigation. See V Philip E. Areeda and Donald F. Turner, Antitrust Law ¶1121b (1980) at 103; Philip E. Areeda and Herbert Hovenkamp, Antitrust Law ¶1121'b (1996 Supp.) at 819 ("Few potential entrants will be found under [the *B.A.T.*] test").

18. FTC Staff Report: Anticipating the 21st Century: Competition Policy in the New High-Tech Global Marketplace (May 1996) at 18-19.

19. *Time Warner, Inc.*, Dkt. No. C-3709, Separate Statement of Chairman Pitofsky, and Commissioners Steiger and Varney, Feb. 7, 1997.

20. It has been said that regulatory agencies are more flexible and less hesitant than courts in balancing competing factors in its analysis. See Stephen G. Breyer, *Antitrust, Deregulation and the Newly Liberated Marketplace*, 75 Calif. L. Rev. 1005, 1043 (1987).

BNSF-2

BEFORE THE
SURFACE TRANSPORTATION BOARD

Finance Docket No. 32760 (Sub-No. 21)

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

# REPLY OF THE BURLINGTON NORTHERN AND SANTA FE RAILWAY COMPANY TO AUGUST 1 COMMENTS


Jeffrey R. Moreland
Richard E. Weicher
Janice G. Barber
Michael E. Roper
Sidney L. Strickland, Jr.

The Burlington Northern
and Santa Fe Railway Company
3017 Lou Menk Drive
P.O. Box 961039
Ft. Worth, Texas 76161-0039
(817) 352-2353

and

1700 East Golf Road
Schaumburg, Illinois 60173
(847) 995-6887

Erika Z. Jones
Adrian L. Steel, Jr.
Roy T. Englert, Jr.
Kathryn A. Kusske

Mayer, Brown & Platt
2000 Pennsylvania Avenue, N.W.
Washington, D.C. 20006
(202) 463-2000

Attorneys for The Burlington Northern and Santa Fe Railway Company


August 20, 1997

carrier, UPSP, it appears that UPSP has effectively created a 2-to-1 situation. We urge the Board to inquire into this problem and to take remedial action as necessary." (DOT at 6). As BNSF described in its August 1 comments, BNSF plans to file a separate petition for relief, seeking an order to require UP to open these industries to reciprocal switching by BNSF.

### E. UP SERVICE IS ADVERSELY AFFECTING BNSF's COMPETITIVENESS

Various commenters share BNSF's concerns with the impact of UP service failures on BNSF's competitiveness. BNSF's July 1 Quarterly Progress Report and August 1 comments described the impact of service issues in several instances, including haulage failures between Houston and Brownsville, failure to provide trackage at Oroville, California, mishandling of cars at the Sjolander facility in Dayton, Texas, and general failures to properly and timely handle BNSF cars in reciprocal switching. UP service delays and failures involving BNSF traffic or dispatching of BNSF trains on trackage rights lines are increasing and are adversely affecting BNSF's competitiveness.

At Houston, and between Houston and Iowa Junction, extreme congestion continues to exist with many trains tied up in operating sidings causing unacceptable delays to BNSF trains. UP appears to be giving preference to its trains over BNSF trains contrary to the dispatching protocol. In any event, shippers reliant on BNSF overhead train operations should not bear the consequences of UP service problems. BNSF is working with UP on solutions to the Houston congestion problem, but neither BNSF nor UP has not yet identified a workable solution.

BNSF-PR-5

BEFORE THE
SURFACE TRANSPORTATION BOARD

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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

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# THE BURLINGTON NORTHERN AND SANTA FE RAILWAY COMPANY'S QUARTERLY PROGRESS REPORT

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Jeffrey R. Moreland
Richard E. Weicher
Michael E. Roper
Sidney L. Strickland, Jr.

The Burlington Northern
and Santa Fe Railway Company
3017 Lou Menk Drive
P.O. Box 961039
Ft. Worth, Texas 76161-0039
(817) 352-2353

and

1700 East Golf Road
Schaumburg, Illinois 60173
(847) 995-6887

Erika Z. Jones
Adrian L. Steel, Jr.
Roy T. Englert, Jr.
Kathryn A. Kusske

Mayer, Brown & Platt
2000 Pennsylvania Ave., NW
Washington, DC 20006
(202) 463-2000

Attorneys for The Burlington Northern and Santa Fe Railway Company


October 1, 1997

BNSF's proposals are dependent upon UP's concurrence or Board action, and include the following:

1) Allow BNSF to control one of two UP mainline tracks through the Houston complex between Tower 26 and Dawes to connect with BNSF's trackage rights over the former SP line to New Orleans, or otherwise provide a route for BNSF to control that enables it to bypass Englewood Yard;

2) Grant BNSF supervisory dispatching control of former SP routes between Houston and Memphis and Houston and Iowa Junction;

3) Place a neutral third-party (PTRA) in charge of switching operations on the Baytown Branch;

4) Install PTRA as a neutral dispatcher of the HBT, as well as the entire Strang/Bayport Loop area, including Pasadena and Sinco;

5) Institute directional train movements by BNSF or PTRA to and from the Strang area;

6) Open the former SP Bayport Loop to reciprocal switching under supervision of PTRA;

7) Grant BNSF trackage rights between Caldwell and Bloomington, Texas, for connection with Tex Mex at Robstown, for traffic originating or terminating in Mexico, and for traffic moving to or from Corpus Christi and Brownsville;

8) Provide direct access to BNSF for all shortlines on UP lines over which BNSF has trackage rights in the Houston/Gulf Coast area; and

9) Grant immediate access to BNSF for all customers with legitimate build-in opportunities in the Houston/Gulf Coast area.

<u>Identification of "2-to-1" Shippers.</u> As noted in the July 1, 1997 Quarterly Progress Report and the August 1, 1997 Comments filed in the Oversight Proceeding, BNSF has been hindered by UP's failure to agree with BNSF on the process to be used in identifying "2-to-1" industries eligible for two-carrier service. While this process should be relatively straightforward, as a practical matter, the "2-to-1" identification process continues to be

BNSF

Burlington Northern Santa Fe Railway

# Gulf Coast Service Initiative Proposal

**Presented to:**

**Texas Railroad Commission**

**Hearing on Houston Rail Traffic**

**October 3, 1997**

**Representing BNSF:**

E. L. (Buck) Hord, VP Operations, UPSP Lines, 817 352-6678
Dennis A. Kearns, Executive Director Govt Affairs, 512 473-2823
Peter J. Rickershauser, VP UPSP & Mexico Lines, 817 352-6686
Michael E. Roper, Senior Attorney General, 817 352-2353

# BNSF GULF COAST SERVICE INITIATIVE PROPOSAL

## Assumptions

There are a number of reasons why BNSF has put forward the following proposal. They include:

-- Rail operations on UP in Houston have been extremely congested for a couple of months. This congestion is producing a transportation emergency for many rail customers, causing them to lose business and, in some cases, curtail production. At the same time, BNSF is required to expend additional resources to move our customers' traffic without meeting our service requirements and commitments, due to circumstances beyond BNSF's immediate control.

-- UP is currently informing customers that their service levels in the Texas Gulf area may not improve significantly during the balance of 1997.

-- BNSF can help reduce Houston congestion and get rail customers' shipments moving immediately if our proposal can be implemented. Customers can benefit from ongoing improvements to rail transit time and shipment velocity, permitting business to be recaptured, production levels to be restored, and railcar fleets to be reduced. A reduction in congestion in the Houston area will also speed the recovery of UP service to acceptable levels.

-- Customers and associations must act in leadership roles with the Surface Transportation Board to support BNSF's proactive proposal in order to achieve near-term service improvements. If rail customers have suggestions that will improve on BNSF's proposal, we want to hear them.

## Overview and Goals Of BNSF's Proposal

If the Surface Transportation Board approves the emergency measures contained in BNSF's proposal, they will be implemented on a temporary basis. To improve Gulf Coast congestion and assist customers in restoring normal shipping patterns with more consistent transit times, and in compliance with conditions imposed on BNSF to provide effective post-merger competition to UP/SP, BNSF's proposal seeks to:

A. Create and maintain clear routes for BNSF and its customers into, through and out of the Houston Gulf area which can also benefit UP in reducing congestion and getting rail shipments moving.

B. Provide a viable service alternative for customers who want to ship on BNSF during this period of extreme UP congestion, for shipments originating or terminating in the Houston/Gulf Coast area, either through reciprocal switch, haulage or, in some cases, establishment of neutral switching.

C. Reroute around Houston customers' traffic which need not move through the terminal area, speeding velocity, improving consistency and reducing current congestion.

D. Create additional short term capacity for handling ongoing customer shipments and directing excess car inventory to intended destinations on a timely basis by combining the facilities of HB&T, PTRA, and portions of UP under one management and direction.

Each specific point in BNSF's proposal supports and drives toward one or more of our temporary goals outlined above.

## Specific Points

1. BNSF to control a route between HB&T connections at Tower 26 or Englewood East Yard Track East 6 and Dawes on one of two SP mainline tracks through the Houston complex, to reach its trackage rights over the former SP, enabling BNSF to bypass Englewood Yard (former SP yard in Houston) and to mitigate present delays. BNSF would work with UP to allow UP/SP to operate their train movements on this trackage, when necessary, but would ensure a track was clear for BNSF and Amtrak train movements.

### What is the problem?

HB&T Rail Traffic Control Center (RTC) and UP Tower 68 control the routes BNSF must use between the HBT South Yard and its trackage rights route to New Orleans. UP has a doubletrack, mainline route past the north side of Englewood Yard; however, this route is usually cleared only for the passage of Amtrak trains. BNSF trains are delayed as much as six-to-seven hours after departure from South Yard before they can move across this segment, due to UP's practice of storing trains on these tracks. Alternative routings between the HBT and BNSF trackage rights lines via connections east of Englewood Yard are also congested.

### How will this work?

BNSF would not dispatch this trackage, but would supervise its use to ensure this route is clear in advance of BNSF train movements, as well as UP train movements. UP and BNSF would not be permitted to store trains on this trackage. UP/SP could use trackage for through train movements, as long as delays would not occur to BNSF trains.

### Why will this help?

Securing control of one of these tracks appears to be the only way for this route to remain open for passage of BNSF trains, ensuring BNSF trains can get through this congested area and maintain our service over trackage rights lines on a consistent scheduled basis.

2. BNSF should take control of dispatching former SP routes between Houston and Memphis, and between Houston and Iowa Junction.

What are the problems?

On both routes, UP is staging trains "with nowhere to go," taking capacity out of the routes by parking trains with power on passing sidings when its Houston area yards such as Englewood are unable to take trains in for processing. When the first five or six (or more) passing sidings on these routes are filled with trains enroute to Houston, UP or BNSF trains can neither get into or out of the terminals. As a result, BNSF trains can not meet customers' schedules because they can either not get out, or can not meet and pass other trains. BNSF has had numerous instances when trains being recrewed along these routes never move with the fresh crews in place. This consumes BNSF power and crew capacity, as well as tying up customer shipments and equipment. BNSF has frequently had as many as three of its consecutive daily merchandise trains tied up on these routes, each of which is scheduled for less than a 24-hour run time over UP.

This also violates the dispatching protocol which was imposed as a merger condition -- for example, BNSF intermodal trains, which are higher priority, are delayed by UP manifest trains, which have a lower priority.

On the former SP through route between Houston and New Orleans, used by BNSF, UP and Amtrak, dispatch control of the route is divided, which results in significant problems in handing off trains between BNSF and UP. BNSF dispatches the Iowa Junction-Avondale section of the New Orleans route (which it purchased for $100 million as a merger condition), but the Houston-Iowa Junction segment is dispatched by UP. As a result, independent dispatch decisions made by either carrier east or west of Iowa Junction can and have severely impaired train capacity and through service across the entire route. UP also owns and controls the parallel UP route between Houston and the New Orleans gateway, controlling additional through capacity that BNSF cannot match.

How will this work?

BNSF would take over temporary supervision of existing UP dispatchers on these routes. BNSF recommends that a Houston-area dispatch "command center" be established on the PTRA where these dispatch functions would be relocated.

The Digicon technology used by UP on former SP routes is compatible with BNSF's Digicon technology, making supervision by BNSF feasible on short notice. After authority is received to proceed with this plan, it would take approximately seven days to put this operation in place. The technology employed makes it possible to place the dispatchers in other locations, as well.

Why will this help?

BNSF will ensure that the train movement capacities of these lines are not lost by staging trains on all available passing sidings. This will allow BNSF (and UP) to get trains across these routes, moving shipments into and out of the Houston area, and taking shipments out of the Houston area which now only add to the congestion problems. BNSF will ensure that the dispatching protocol is enforced, and that both BNSF and UP, as well as Amtrak, trains will move in accordance with its provisions, imposed as a merger condition from the CMA agreement. Rail customers with access to both UP and BNSF will have improved options to get shipments moving around UP as necessary, which should ease both shippers' and UP congestion problems.

3. BNSF views the area south of the Houston Ship Channel between Sinco, Strang and the Bayport Loop, with operations intertwined at many locations between the UP's former SP trackage and the PTRA, to be a source of major congestion. It is also an opportunity to effect steady reduction in standing car inventory throughout the Houston terminal by combining available resources now used independently to provide optimum efficiency under the neutral management of the PTRA.

<u>What are the problems?</u>

Currently, traffic accessible to BNSF in the Strang area moves by UP through the Englewood Yard, contributing to the congestion at that point and slowing customer shipments by five to six days, whether destined for BNSF or UP beyond. Dispatch of trains on the PTRA is controlled by the UP from Omaha. UP is now tying up trains on the HB&T, impacting operations on the PTRA and on the BNSF -- for example, on Thursday, September 18, UP had eight dead trains on the main lines around the Houston area, turning these common routes into storage tracks. Current operations in the Strang area protect UP's interests, not the interests of rail shippers impacted by UP congestion. Further, customers in the former SP Bayport Loop which are closed to reciprocal switch have no options to route around UP's congestion.

Presently, the HB&T is dispatched from Union Station, but soon this function will be relocated to the UP offices in Spring, TX, per prior agreement between UP and BNSF dividing the assets of the HB&T. Now, however, even before UP has control of HB&T in Spring, trains are being dumped on the HB&T, and the neutral HB&T dispatcher has very little to say about it, with the main lines of the HB&T being used for storage of UP trains.

<u>How will this work?</u>

The PTRA, managed locally and jointly accountable to BNSF and UP, has established processes and procedures to insure it does not accept cars from connections unless they have a destination. This "flow control" meters cars onto the railroad to ensure it does not get gridlocked. BNSF recommends, on a temporary basis, that this management team and process take over directing operations to coordinate use of available capacity on key UP as well as PTRA rail routes between downtown Houston and the Bayport Loop area.

BNSF and UP would have to accept PTRA "flow control" of inbound cars, staging cars on their railroads prior to reaching the Houston terminal, to insure switch operations remain fluid to and from customers .

Temporarily, the PTRA should control dispatching of the HB&T, by supervising a neutral HB&T dispatcher. Under normal circumstances and over the long term, BNSF does not have any problem with UP dispatching the HB&T; after all, most of the rail lines which connect with it are UP routes. Right now, however, no one is able to get through Houston at all because of the way the HB&T is being used.

BNSF proposes that:

a. PTRA take over, on a temporary basis, neutral dispatch of the HB&T, as well as the PTRA and the SP route between Bridge 5A and Manchester Junction; Sinco Junction and Deer Park Junction; and West Junction and Harrisburg Junction. RTC is located in HB&T's Houston Union Station; PTRA and SP dispatching use Digicon technology, which can easily be relocated to Union Station. This would place neutral management control and direction at one location.

b. A "directional flow" operation would be instituted. All inbound cars for this area would be brought to PTRA's Pasadena Yard, where they could be available to customers within 24 hours of arrival. Depending on volumes, BNSF could make up a direct PTRA Pasadena train outside the Houston area for movement past intermediate terminals. All outbound shipments, whether originating on PTRA or SP, would be directed to Strang Yard for humping and classification into outbound trains. This makes the best use of both facilities. PTRA would deliver cars for SP customers at Strang. The Strang facility would make a direct train for the BNSF, bypassing Englewood and other yards, for delivery to BNSF at HB&T's South Yard (if further processing was required) or for movement out of the Houston area entirely. Strang would continue to make up any UP over-the-road trains required by UP's operating plan.

c. Customers on the Bayport Loop and elsewhere in the Strang area, now locally served by UP, would be given temporary access to BNSF linehaul through a neutral reciprocal switch by UP, permitting them to select either carrier as a way of bypassing congestion and getting their products to customers.

Labor impact would be minimal. The RTC operator would remain at Union Station. The equivalent of one non-agreement position around-the-clock would move from UP to Union Station with the necessary Digicon technology. PTRA and UP agreement personnel would continue doing the work they do now, under PTRA direction. PTRA would have the option of calling on existing UP and BNSF management teams for further assistance. Existing UP resources in place would be used; PTRA's expenses are jointly borne by BNSF and UP, both of which could provide additional resources. PTRA's TIES computer operation system is compatible with UP's TCS and BNSF's TSS systems.

Why will this help?

By adopting the proposed directional operation, available resources' capacities will be optimized and congestion can be reduced for customers, BNSF and UP.

Shipments destined for BNSF roadhaul from Houston would move directly to HB&T South Yard, permitting dispatch from Houston on BNSF trains within 24 hours and the reduction of three-to-four days out of customer-release-to-departure-Houston time. This would speed up customer flows, and reduce Houston congestion by getting shipments, which currently consume available trackage, out of the area.

PTRA, a joint facility, has shown itself to be an effective neutral operator in the Gulf area. PTRA has institutional knowledge of the area, trackage, facilities, and customers, and is the best organization to direct emergency operations to relieve congestion through much of the Houston port area.

Customers on former SP in the Strang, Bayport Loop and Sinco areas which are closed to switching would now be open or have access to BNSF via reciprocal switch on a temporary basis, for interchange at Strang, under supervision of PTRA.

4. Neutral third-party switching operations should be established on the former SP's Baytown Branch under the direction of the PTRA to assure expeditious handling of traffic for interchange to both UP and BNSF destinations.

What is the problem?

Interface problems between BNSF and UP for shipments moving to or from Baytown Branch customers cause many shipments to move, in error, via UP into Englewood, instead of via BNSF from Dayton, despite customers' routing instructions. Shipments moving to Englewood are severely delayed, impacting customers, and adding to unnecessary congestion at Englewood.

Theoretically the merger conditions permit BNSF to switch Baytown Branch customers accessible to it directly, but this is not a practical solution. The Baytown Branch is already heavily congested with existing UP operations. Adding more trains on this line would further congest operations. In addition, customers would have to separate their shipments for handling by UP and BNSF, and generally customers do not have existing facilities or capabilities to do this at their plant sites.

There would be no impact on labor. Existing SP labor would be supervised and directed by a neutral party, such as PTRA.

How will this work?

PTRA, as outlined in Proposal #3 for the Strang area and using the same direction and processes, would supervise UP's switch operations for Baytown Branch customers to insure shipments intended for BNSF at Dayton are interchanged to BNSF there. PTRA would only supervise what trains are made up, what they handle and when they run.

BNSF cars would be interchanged at the new operating tracks, adjacent to the Sjolander SIT facility, to be completed about October 1. UP/SP cars would be interchanged at Dayton Yard.

Why will this help?

It will make BNSF service for customers on the Baytown Branch a viable alternative, permitting them to bypass UP's Houston congestion while keeping cars out of UP's Houston yards which need not go there. Transit time for customers would be improved; for example, cars delivered by BNSF at Dayton, TX on Day 1 would depart Houston on BNSF trains from South Yard by Day 2, instead of days later if they are processed through Englewood Yard.

5. Additional south Texas/Mexico trackage rights over UP/SP are required temporarily, for traffic originating or terminating in Mexico, to keep BNSF Laredo and Brownsville gateway traffic out of the Houston area. These trackage rights should be between Caldwell and Bloomington, TX for connection with Tex-Mex at Robstown, for traffic originating or terminating in Mexico.

What is the problem?

BNSF's present routing to the Laredo gateway is via BNSF at Algoa, TX., thence UP to Corpus Christi/Robstown in connection with TexMex. This moves shipments into the Houston/Galveston area which need not go there and adds to congestion.

Why will this help?

It will reroute traffic away from the Houston area which does not need to travel through there, speeding transit times and consistency for business not originating or terminating in the Houston area, and freeing capacity in the Houston area for local traffic.

How will this work?

BNSF will reroute its existing trackage rights trains, under compensation as outlined in the UP/SP merger conditions, from the existing route through Algoa to the route via Caldwell-Flatonia-Bloomington, TX, on a temporary basis. Union Pacific will retain dispatch control. TexMex, also using this route for its Beaumont-Houston-Robstown service, will not be negatively impacted. Union Pacific would be compensated with trackage rights fees as provided in the BNSF agreement and supplements.

6. All shortlines not previously granted direct access to BNSF on the UP/SP lines where the BNSF has trackage rights should be given such access to provide customers on those shortlines immediate flexibility and relief from congestion being experienced in the Gulf Coast area.

<u>What is the problem?</u>

Some shortlines along UP/SP trackage rights awarded BNSF in Texas and Arkansas, for example, the Fordyce & Princeton, are having problems maintaining sufficient flows of traffic for their customers due to infrequent UP switching of interchanges. BNSF trains pass these interchanges over trackage rights several times daily, but are unable to serve these customers because of existing UP/SP merger conditions - these carriers do not qualify as "2-to-1" shortlines accessible to BNSF.

<u>How will this work?</u>

Existing BNSF trains or, if necessary, additional BNSF trains would have access to the following shortlines, and perhaps others, based on customers' needs, using existing interchanges now exclusively available to UP and the shortlines. All of these shortlines currently are without access to BNSF along UP/SP trackage rights BNSF is operating over in Texas and Arkansas:

| | |
|---|---|
| **Gulf South:** | Point Comfort & Northern at Lolita, TX |
| | Rio Valley Switching Company at Harlingen, TX |
| **Gulf North:** | Angelina & Neches River at Lufkin and/or Prosser, TX |
| | East Camden & Highland at Eagle Mills, TX |
| | Fordyce & Princeton at Fordyce, AR |
| | Moscow, Camden & St. Augustine at Moscow, TX |
| | Texas South-Eastern at Diboll, TX |

BNSF would set cars out and pick cars up at the existing interchanges. Shortlines would have to separate traffic intended for BNSF from that intended for UP.

<u>Why will this help?</u>

This will give customers on these shortlines access to BNSF on a temporary basis for both car supply and shipments, providing additional access and protecting rail transit.

7. Customers with legitimate build-in opportunities recognized by the STB should now be given temporary access to BNSF using existing tracks, yards, and interchanges in order to provide them immediate flexibility to use BNSF as well as UP to route around congestion being experienced in the Gulf Coast area and get their products delivered.

<u>What is the problem?</u>

Customers in specific areas have been identified as having build-in/build-out rights to access BNSF when they are locally served by UP or SP prior to the merger, as part of the merger conditions. Currently, these customers have no option except UP service to and through the Houston/Gulf Coast area. Their shipments are delayed in the same congestion as other customers' shipments.

How will this work?

BNSF would either set out/pick up cars at the customers' facilities or at the junction between the customer and the UP/SP trackage rights line over which BNSF now operates, and delivery will occur between the junction point and the customer facility by either BNSF, UP or the existing customer switch carrier.

Why will this help?

BNSF service through and around the Houston area, in conjunction with other temporary measures proposed, would give build-in/build-out customers an option around UP to get their products to market and remove traffic from UP/SP, easing existing congestion.

## Other Questions About BNSF's Proposals

What do we mean by "temporary" in terms of duration of these rights for BNSF?

BNSF's proposal for temporary relief is 180 days.

How would UP be compensated by BNSF for use of its facilities?

Trackage rights and other charges as established in the merger conditions.

Could customers, on a temporary basis, enter into pricing arrangements with BNSF and route BNSF linehaul to and from the new access points listed until these emergency conditions end?

Yes. The most logical business for temporary rerouting to BNSF would be business moving to or from BNSF local points not jointly accessed by UP, but customers should have routing choice on all their traffic during this temporary emergency situation. Customers should be given this option, allowing them the option of exercising it.

Are there other aspects of BNSF's proposal to consider?

BNSF would set up a Houston command center on the PTRA in Houston, where dispatchers, dispatch supervision and customer service would be located.

BNSF would publish performance statistics weekly, including, for specific areas, time between bill, release, and departure from Houston area on through trains.

Shippers need to be involved in the process on an ongoing basis, and provide feedback as to whether the measures imposed are producing the desired results. BNSF would be willing to work with and submit information to a shippers' oversight group to ensure customer transit, reliability, and consistency issues are addressed.

How would shippers be involved in seeking implementation of these proposals?

Shippers and shipper groups affected by the acute and ongoing service failures on the Gulf Coast need to take the lead in filings with the STB, and could participate with groups such as the Chemical Manufacturers Association (CMA), National Industrial Transportation League (NITL), the Society of the Plastics Industry (SPI) or others to seek relief from the STB. Such shippers could support CMA, NITL and SPI in seeking action by the STB, and describe the current situation in statements that would be provided to CMA, NITL or SPI, or used in conjunction with a petition for relief. Shippers should provide and confirm the following facts to support the need for immediate action, either in a joint petition or by filing separately to support such relief:

A. The precipitous decline in UP/SP service to their facility and the existence of a crisis situation leading to the need for emergency action.

B. The impact of the present situation on their operations, interference with production, threat of shutdown and lost production.

C. How current UP/SP service compares with and is much worse than prior SP or UP service.

D. Inability of BNSF to provide effective service on its trackage rights on UP lines due to UP/SP operational problems.

E. Desire for BNSF to provide service on emergency basis and address service and dispatching issues.

Parties seeking and supporting the emergency relief should include shippers to and from affected Gulf Coast facilities, shortlines and through shippers whose service is affected.

BNSF would plan to file its plans immediately and concurrently with significant shippers' filings, as soon as possible. The current service emergency in the Houston area requires immediate action and relief for shippers as well as BNSF.

Under what authority and process could the STB act in this emergency situation?

The STB has jurisdiction and the authority to issue orders to address the current situation of acute congestion and gridlock as part of (A), its oversight authority and (B), its power to issue emergency car service orders under 49 USC Sections 11121 -11123.

A. The STB retained extensive authority to remedy problems arising from the UP/SP merger as part of its approval of the transaction. In this case, there are severe failures in the UP operating plan and its implementation that are adversely effecting shippers and BNSF's ability to effectively utilize the rights granted as conditions to the UP/SP merger. This is having immediate detrimental effects on service as well as threatening the viability of competition by BNSF as the new entrant.

B. When the STB determines that "shortage of equipment, congestion of traffic," or "other failures of traffic movement" exist which "creates an emergency situation of such magnitude as to have substantial adverse effects on shippers, or on rail service in a region..., or that a rail carrier cannot transport traffic offered to it in a manner that serves the public," the STB can issue temporary service orders (30 day periods to a maximum of 270 days) providing for the joint or common use of railroad facilities and other temporary changes in traffic handling and routing.

A petition seeking action by the STB should be filed as soon as possible by affected shippers or shipper organizations requesting expedited action.

<u>How and what would BNSF have to file with the STB?</u>

BNSF must show its ability to provide the service, equipment and resources envisioned by the proposal and that such service is in the public interest because it would materially alleviate the current crisis situation. BNSF would plan to file concurrently with a major shippers' organization filing.

<u>What timeline might be expected for the STB to review and act on the suggested filings?</u>

A BNSF petition would be filed as soon as shipper organization(s) commit to proceed, join in preparation of the petition, and shipper statements are available. Replies by UP would be anticipated shortly after. Due to the emergency nature of the Gulf situation and its impact on shippers, we would anticipate expedited STB action shortly after UP's reply.

<u>In this emergency situation, how is labor protected if any or all of the BNSF proposal is implemented under the direction of the STB?</u>

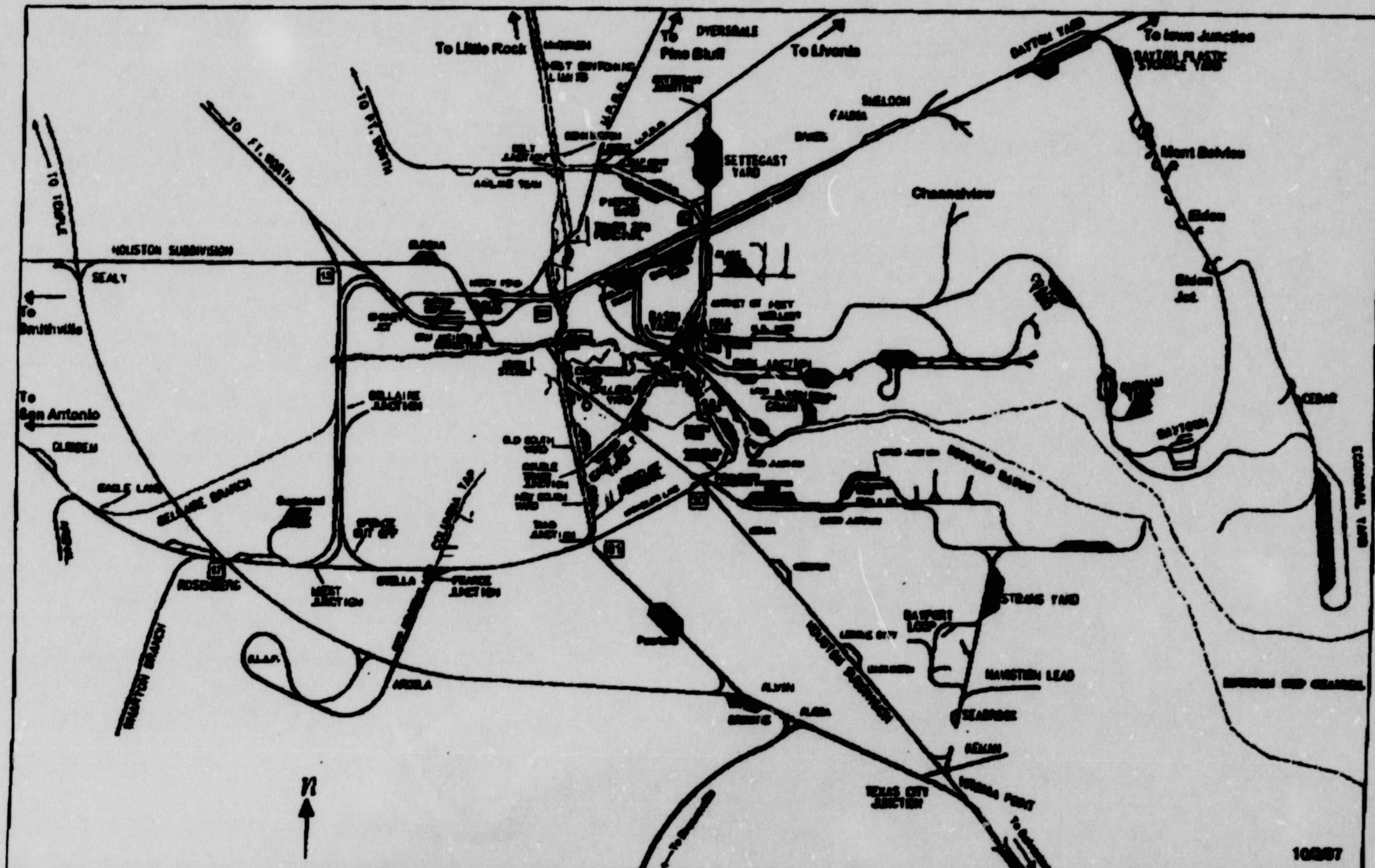
The STB has jurisdiction and the authority to issue orders to address the current situation of acute congestion and gridlock as part of its UP/SP merger oversight authority and its power to issue emergency car service orders under 49 U.S.C. Sections 11121-11123. In taking action in these circumstances, the STB also has the authority to address any labor concerns through attaching labor protective conditions as necessary.

Any orders addressing the trackage rights situation issued pursuant to the Board's oversight authority would most likely be subject to the <u>Norfolk & Western</u> conditions. These conditions allow implementation of a transaction upon twenty days notice to labor without implementing agreements. (Labor and management would remain obligated to subsequently reach such agreements through negotiation or arbitration.)

To the extent BNSF's proposal was implemented pursuant to the STB's emergency car service powers (49 U.S.C. §§ 11121 - 11123), the Board is required "to the maximum extent practicable" to use the UP/SP employees who would normally perform the work. To the extent it were necessary to use BNSF employees as a result of a car service order, it is likely that the STB would also impose the Norfolk & Western conditions on the transaction, since such orders would appear necessarily to flow from the overall grant of trackage rights to BNSF and the effects of the UP/SP transaction over which it would be exercising its continuing oversight jurisdiction.

September 24, 1997 (b)

# Houston Metro Area



SURFACE TRANSPORTATION BOARD

STB Ex Parte No. 573

RAIL SERVICE IN THE WESTERN UNITED STATES

# TESTIMONY OF

# MATTHEW K. ROSE

# DECEMBER 3, 1997

My name is Matthew K. Rose, and I would like to thank you for the opportunity to appear before you today. I am Senior Vice President and Chief Operations Officer of The Burlington Northern and Santa Fe Railway Company ("BNSF") with offices at 2650 Lou Menk Drive, Fort Worth, Texas 76131-2830. I joined BN in 1993, and served as Vice President of Vehicles & Machinery from June 1994 to January 1995. I was Vice President, South Region Field Marketing, from January to September 1995. I was Vice President, Chemicals from September 1995 to May 1996, and I was Senior Vice President, Merchandise from May 1996 until August 1997 when I was appointed to my present position.

Before joining BNSF, I was Vice President, Transportation for Triple Crown Services (a Norfolk Southern subsidiary) where I had functional responsibility for all facets of the truck/rail operation. Prior to that, I held various positions with Schneider National and International Utilities, a trucking conglomerate. I have a bachelor of exist on the lines and at the Houston Terminal. (A map of the Houston Terminal is attached hereto as Exhibit 5.) The conditions on these lines and at the Houston Terminal significantly limit our ability to successfully handle more traffic, because they consume resources (locomotives, crews and equipment) that would otherwise be available.

For the reasons stated above, we strongly believe the Board should impose the following additional remedies at this time.

1. In BNSF's October pleadings, we proposed that the STB allow BNSF to control a route through the Houston complex which would bypass Englewood Yard to connect with BNSF's trackage rights over the former SP line to New Orleans. BNSF now requests that the STB require that the HBT/PTRA/UP dispatching function at Spring, Texas, be jointly supervised by BNSF and UP, to ensure that lines in the Houston Terminal are not blocked and that operations are fluid for both UP and BNSF. Likewise, joint supervisory dispatching control would ensure that Tex Mex interests in the terminal are also protected and that Tex Mex's traffic does not add to Houston Terminal congestion.

2. We also request that the Board require joint BNSF/UP supervisory dispatching control of the former SP routes between Houston and Memphis and between Houston and Iowa Junction. Such dispatching control is still necessary in both of these corridors. The Houston-Memphis route had temporarily improved only to revert to severe congestion due to blocked sidings during the week of November 17. The Houston-Iowa

**BEFORE THE**
**SURFACE TRANSPORTATION BOARD**

| | |
|---|---|
| In the Matter of Union Pacific Corporation, ) <br> Union Pacific Railroad Company, Missouri ) <br> Pacific Railroad Company, Southern Pacific ) <br> Rail Corporation, Southern Pacific ) <br> Transportation Company and St. Louis ) <br> Southwestern Railway ) | Docket No. ____________ |

**JOINT PETITION FOR EMERGENCY SERVICE ORDER**


Martin W. Bercovici, Esquire
Arthur S. Garrett III, Esquire
KELLER & HECKMAN, LLP
1001 G Street, N.W., Suite 500 West
Washington, D.C. 20001
(202) 434-4100
Counsel for The Society of the Plastics Industry, Inc.

Nicholas J. DiMichael, Esquire
DONELAN, CLEARY, WOOD & MASER, PC
1100 New York Ave., N.W., Suite 750
Washington, D.C. 20005
(202) 371-9500
Counsel for The National Industrial Transportation League

Thomas E. Schick, Esquire
CHEMICAL MANUFACTURERS ASSOCIATION
1300 Wilson Boulevard
Arlington, Virginia 22209
(703) 741-5000
Counsel for Chemical Manufacturers Association


Dated: October 20, 1997

BEFORE THE
SURFACE TRANSPORTATION BOARD

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MERGER OVERSIGHT HEARING

---

UNION PACIFIC RAILROAD

--CONTROL AND MERGER AGREEMENT--

SOUTHERN PACIFIC RAILROAD

---

VERIFIED SUPPORT STATEMENT OF
INLAND PAPERBOARD AND PACKAGING, INC
INDIANAPOLIS, INDIANA

---

by: Donald A. Welch
Inland Paperboard and Packaging, Inc
4030 Vincennes Road
Indianapolis, IN 46268

September 29, 1997

# VERIFIED STATEMENT

My name is Donald A. Welch. I am General Manager-Logistics for Inland Paperboard and Packaging, Inc. I have been employed with Inland Paperboard and Packaging, Inc. for ten years. My transportation experience totals over twenty one years.

My business address is: Inland Paperboard and Packaging, Inc., 4030 Vincennes Road, Indianapolis, Indiana 46268.

Inland Paperboard and Packaging, Inc. is a vertically integrated paper products company with eight mills, forty corrugated container plants and twenty two warehouses throughout the United States. We produce kraft linerboard and medium at our mills, and various corrugated packaging containers and trays at our plants. Our net sales for 1996 exceeded 2.3 billion dollars and our total transportation costs were over 180 million dollars. Our products are marketed throughout the United States, Canada, Mexico, Europe and Asia, and rail shipments account for 35% of our total freight movements.

We have a paperboard mill based in Orange, Texas that relies heavily upon the Union Pacific Railroad for moving rollstock to our box plants. Due to the extreme congestion on the Union Pacific, and their inability to timely switch and move cars, we have suffered the loss of many thousands of dollars in unavailable inventory, and have shut down several key customers. The Union Pacific is unable to timely move cars anywhere in their new system, and primarily in the Texas/Arkansas venues.

We are seeing transit times measured in months, rather than days. For example, CSX car 507245 arrived in Pine bluff, Arkansas on August 24, 1997. The car was sent to River

Yard in error, then sent back to Pine Bluff September 4. Then the car was mishumped and sent to East St. Louis on September 5. The car remined there until September 12, when it was dispatched back to Pine Bluff. It finally was sent to its original desitnation, Carrollton, Texas, arriving one month and four days after initial shipment.

CSX car 137056 arrived Pine Bluff on August 21. It departed September 1 and arrived Hearne, Texas on September 10. It was finally delivered to El Centro, California on September 25, one month and ten days after shipment.

We still have four cars sitting in Hearne, which we have been unable to get the Union Pacific Railroad to move although the cars have been there about two weeks.

We have been experiencing many other problems at our Orange mill. Through trains are left sitting, blocking the siding that connects to the interchange. The Union Pacific has been unable to verify car records on offered lading. Cars are tendered to the Union Pacific at the interchange, then not moved to Beaumont. Average time from Orange to Beaumont has been one to two weeks.

We are also having difficulties from our Ontario, California mill, served by the Union Pacific Railroad. Cars arrive at North Platte, Nebraska and sit for a week before movement. Some of these cars were HOT and for our Tracy, California box plant.

We shipped a car of transferred rollstock from Mansfield, Louisiana on September 6. The car was delivered to the BNSF on September 26 in Kansas City. The Union Pacific was unable to move the car faster, despite our notification of it being HOT.

We have shifted as much business as possible from the Union Pacific to other railroads, but are unable to move all the lading elsewhere. We desparately need relief from the Union Pacific problems, brought about by its merger with the Southern Pacific, and we need it NOW!

Respectfully submitted,

Donald A Welch

Donald A. Welch
General Manager-Logistics
Inland Paperboard and Packaging, Inc.

<u>**VERIFICATION**</u>

County of Marion )
) ss
State of Indiana )

Donald A. Welch, being duly sworn, deposes and says he read the foregoing statement, knows the contents thereof, and that the same are true as stated.

Donald A. Welch

Donald A. Welch

Subscribed and sworn to before me this 30th day of September, 1997.

Elaine E. Gray

Notary Public

My Commission expires

ELAINE E GRAY
NOTARY PUBLIC STATE OF INDIANA
HENDRICKS COUNTY
MY COMMISSION EXP. AUG. 4,2001

CONDEA Vista Company
900 Threadneedle
Houston, Texas 77079-2990
(281) 588-3000

CONDEA VISTA

October 16, 1997

The Honorable Linda J. Morgan, Chairwoman
Surface Transportation Board
1925 K St. N.W., Suite 800
Washington, DC 20423

Dear Chairwoman:

CONDEA Vista Company is a petrochemical company which operates three production sites served by the Union Pacific Railroad in Lake Charles, Louisiana. Approximately 80% of our products (>2 billion pounds) are moved from our Lake Charles operation to our customers by rail. Critical feedstocks are also delivered to our operation by rail. In addition, Houston, Texas, serves as the primary focus of our export/import operations. In Houston, CONDEA Vista operates export facilities for plastic products produced at our Oklahoma and Mississippi plastic manufacturing plants.

Prior to the merger of the UP and SP railroads, rail service was considered poor, but tolerable, in comparison with other transportation modes. In the last few months rail service has deteriorated drastically. Railcar transit times west out of Lake Charles have increased in the range of 30% to 100%. Railcars of plastic shipped to Houston have been delayed for weeks. The result has been not only increased cost of exporting product, but, due to consequent delays in receiving empty railcars back at our producing plant, we have had to reduce operating rates to avoid running out of railcars. Delays in delivering product to customers has resulted in the necessity of delivering material by truck at higher cost. Because all Gulf Coast shippers are relying more heavily on trucks, a critical shortage of equipment and drivers has occurred in this mode of transportation also.

We have no viable alternative to move our products. For the majority of our business we are captive to rail. It is imperative that the Surface Transportation Board take effective, expeditious action to relieve the rail congestion in the Gulf Coast area.

I, James J. Hall, declare under penalty of perjury that the foregoing statement is true and correct. Further, I certify that I am qualified and authorized to file this verified statement. Executed the 16th day of October, 1997.

Sincerely,

JJHall

James J. Hall
Manager Distribution

P.O. Box 19029 • Houston, Texas 77224 0029

JONES-HAMILTON CO
5400 ENTERPRISE DRIVE
NEWARK, CALIFORNIA 94560-1310

TEL: (510) 797-2471
FAX: (510) 797-0162

October 7, 1997

Secretary
Surface Transportation Board
1925 K St. N.W.
Washington, D.C.

Dear Secretary:

I am submitting this letter through the Chemical Manufacturers Association (CMA) to request your assistance with the current congestion problems with the Union Pacific (UP) Railroad in the Gulf States.

My name is Bob Messemer and I manage the transportation and logisitics for Jones-Hamilton Co (JH-CO). We are a chemical manufacturer with operations in Newark, CA and Walbridge, OH and specialize in Sodium Bisulfate ($NaHSO_4$), Hydrochloric Acid (HCl), Sulfuric Acid ($H_2SO_4$), and Hydrogen Peroxide ($H_2O_2$).

Our primary concern is the impact the UP's situation is having on our supply chain from the Gulf States. Prior to the merger we experienced ten (10) to fourteen (14) day transit times, one way, between Texas and Southern California and Arizona. Since the merger these same transit times have increased to well above thirty (30) days. The "black holes" in Houston and San Antonio have had a trickle down effect on other interchanges such as West Colton, CA and Roseville, CA which have also impacted our transit times for intrastate shipments.

The financial impact of this situation has been overwelming, not only on JH-CO but our customers as well. The average cycle, the time it takes a railcar to reach destination and return to origin, was 25-30 days prior to the merger. We are now lucky if we see a car return to origin within sixty (60) days. Our fleet cost, based on the volume shipped, has now doubled. With the additional transit times we cannot maintain inventory at our terminals nor our railcar customers. Without product available via rail, we have had to ship via tank truck which has increased the cost of moving product as high as 100% above what we typically pay for rail service. We have had to incur these additional costs to keep our customers operating. We will have to pay penalties at terminals for not being able to meet the minimum throughput originally agreed upon. We have the product available, it just isn't getting from point "A" to point "B".

HCl is a necessity for a variety of processes including power plants, steel mills, water treatment plants, chemical manufacturing, and food processing to name a few. The inavailability of rail service has even impacted the raw materials for the HCl production point we sell from in Northern California. With less product available, from slower transit times and less production, we have lost significant amounts of business and growth opportunities.

We will appreciate your immediate and utmost attention to this matter.

Sincerely,

JONES-HAMILTON CO.

Bob Messemer/ja

Bob Messemer
General Transportation Manager

cc: Frank J. Principi CMA Arlington, VA

## VERIFIED STATEMENT OF: JOHN G. BRESLIN

## WITCO CORPORATION

My name is John G. Breslin, and I am Director of Logistics for Witco Corporation and have held this position for eight years. My duties include policy, procurement, and regulatory compliance in all transportation, warehousing and related activities in all geographies.

Witco Corporation is a specialty chemicals company with facilities located throughout the world. In the United States, Witco has 22 production facilities with eight facilities located in the Gulf/Southwest region. Six of the facilities as a result of the Union Pacific/Southern Pacific rail merger are exclusively served by the Union Pacific Railroad.

The purpose of my statement is to petition the Surface Transportation board to take immediate action to bring service levels back to pre-merger levels.

As a result of this merger, service is nonexistent in these regions. Transit times which were normally seven to ten days are now well beyond 30 days. These excessive delays coupled with lost and mis-routed cars are causing Witco to experience lost sales and production curtailments. Transportation costs have escalated for these facilities as Witco scrambles to find alternate means of transport to support business. Should this situation be allowed to continue without intervention, plant shutdowns and loss of business will cost Witco millions of dollars in lost revenue. It is imperative that action be taken immediately,

I, John G. Breslin, declare under penalty of perjury that the foregoing is true and correct. Further, I certify that I am qualified and authorized to file this verified statement. Executed on October 1, 1997.

Sincerely,

WITCO CORPORATION

John G. Breslin

By: John G. Breslin
Title: Director of Logistics

Subscribed and sworn to before me on this second day

of October, 1997.

J. Cookinham
JEAN C. COOKINHAM
NOTARY PUBLIC OF CONNECTICUT
MY COMMISSION EXPIRES MAY 31, 2000

FINA

## Verified Statement of Mike Spahis

## October 10, 1997

**Subject: Rail Service Issues**

My name is Mike Spahis, Manager of Logistics and Distribution for Fina Oil and Chemical Company, 8350 North Central Expressway, Dallas, Texas 75206. I am responsible for managing the distribution of Fina's chemical products from its various production facilities to multiple customer destinations. I am very familiar with the railroad operations as it pertains to Fina's shipments across North America. I am presenting these comments on Fina's behalf.

**Fina Oil and Chemical Company** engages in crude oil and natural gas exploration, production; petroleum products refining, supply and transportation, and marketing; and chemicals manufacturing and marketing. Fina relies heavily on the rail transportation industry to deliver several products to a variety of customers across the United States, Canada and Mexico. Fina has production facilities located along the Texas Gulf Coast, West Texas and Louisiana. Fina has a polypropylene facility located in La Porte, Texas that is served by the Port Terminal Railroad (PTRA) with an annual capacity of 1.5 Billion pounds. Fina also has a polyethylene facility located in Bayport, Texas that is served exclusively by the Union Pacific with a capacity of 420 Million pounds. Fina has a polystyrene facility located in Carville, Louisiana that is served exclusively by the Illinois Central with an annual capacity of 1.0 Billion pounds. Fina also has refineries located in Port Arthur, Texas and Big Spring, Texas. Approximately 90% of the polymer production volume

**Fina Oil and Chemical Company**
P.O. Box 2159 • Dallas, Texas 75221 • (214) 750-2400

is dependent on rail transportation. This equates to 2.6 Billion pounds or 13,500 rail shipments of Fina's 2.9 Billion polymer capacity. Distribution costs account for at least 20% of the cost of the product which is second to only raw materials. Rail transportation provides the only economic and service alternative for Fina's distribution network and the customer's inventory requirements.

Fina strives to meet the inventory requirements of its customers by providing consistent delivery of products in addition to providing high quality products and excellent customer service. Unfortunately, Fina has seen a rapid deterioration of rail service provided by the Gulf Coast based railroads. This decline in rail service began in late 1996 and has escalated to today's disturbing levels. There is no consistency or reliability in predicting rail performance today. This reduction of service has lead to increased costs of doing business, along with the increased dissatisfaction of Fina's customers.

The most pronounced problem is the physical movement of railcars from storage location to customer destination. Fina has experienced an abnormally high number of problems such as delays in transit times, mishandling of cars, and lost cars. These problems have increased significantly over the past two months. On average, for each railcar in transit, there is at least one identifiable problem with the railcar. When these problems occur, it is extremely difficult to resolve timely and efficiently, if at all. In the past, critical issues such as customer shutdown situations were resolved and addressed. Today, treatment for every problem is the same: *resolution by chance and luck.* This atmosphere has penetrated the entire organization. For example, polyethylene railcars historically have been stored in the plastics facility in Dayton, Texas. Today, there is no idea where the railcars will be stored and no input on the decision as to where to store these cars; Pine Bluff, Mount Belvieu, Tyler, Texarkana, East Baytown, San Antonio, East St. Louis, Hearne, etc. This causes departure delays, increased transit times due to out of route locations, inability to access these cars in emergency situations, and even problems in billing of these cars. Cars have been delayed from billing several days without movement or any expectation when the railcar will move. Cars have had to sit with no movement for up to twenty days, before departure after billing for no apparent reason. The transit times are very inconsistent and thus not predictable. In the past, within 15 days a car would reach destination anywhere in the country. Today, Fina has had transits up to 60 days with no consistency.

The problem is not just isolated to the Union Pacific Railroad. The congestion in Houston has lead to difficulties with the PTRA, HBT and BNSF railroads. This affects our polypropylene shipments leaving our La Porte facility along with our movements going to Houston or the West Coast from our Carville, Louisiana location. Problems have been identified on the Union Pacific Railroad, but those problems have spread throughout the North American railway system.

Fortunately, Fina has not had to shut down reactors, but did alter production rates, packaging patterns, and adjusted maintenance schedules due to inability of the railroad to deliver the required number of empty cars. These changes in production schedules have not been optimized and thus caused inefficiencies in the system and added incremental costs. As a precaution, Fina is storing excess empties in its plants to counteract the inconsistency and unpredictability of service.

The effects of these problems have lead to increased costs for both Fina and its customers. Due to the railroads' inability to deliver product to Fina's customers, Fina will deliver product from non-optimum locations or by alternative delivery means to keep the customers from shutting down its production. Fina is diverting cars from other customers, delivering via bulk truck or truck load at an increased cost over normal operations. Fina has had to bulk truck product to as far away as California on several occasions. Customers have canceled orders and thus Fina has lost unrecoverable sales because of the railroads' inability to deliver product. Fina has had to increase inventory levels to maintain safety stock for its customers. Fina has had to increase the number of private railcars to account for the increased transits and excess empty car requirements at an extremely high cost. Pertaining to inventory levels, Fina has (1) increased forward storage inventory levels, (2) added forward storage locations, and (3) increased safety stock held by customer relative to how Fina normally operates. Fina's customers are having difficulty forecasting their own inventory requirements due to the service problems. In isolated cases, Fina is having to extend credit terms for customers to account for the increased transit time. In a falling price market, Fina has had to issue credits for certain customers in extreme cases because there was a price decrease from when the customer ordered to when the car arrived. The increased costs will be reflected in the total cost of doing business and be felt by Fina, Fina's customers and the ultimate consumer of the products.

In conclusion, the focus of Fina's efforts has concentrated in dealing with delivery problems caused by railroad service deterioration as opposed to adding value for its customers. Fina is very concerned about the continued rail service degradation and the effect on Fina and it's customers.

I, Mike Spahis, declare under penalty of perjury that the foregoing statement is true and correct. Further, I certify that I am qualified and authorized to file this verified statement. Executed on Friday, October 10, 1997.

Mike Spahis

*Manager of Logistics and Distribution*

Fina Oil and Chemical Co., Inc.

**VERIFIED STATEMENT**
**OF**
**HARRY J. IGNATOWSKI**
**on behalf of**
**THE DOW CHEMICAL COMPANY**

My name is Harry J. Ignatowski and I am Manager, North American Rail Operations for The Dow Chemical Company. My business address is 2020 Dow Center, Midland, Michigan 48674. I have been employed by Dow in various capacities since 1967. I joined Dow with a marketing/logistics degree in 1967. From 1967 to the present I have held a series of logistics assignments within Dow that have included all modes of transportation. Since January of 1995, my primary focus has been Dow's rail operations in North America.

In my current position with Dow, I am generally responsible for Dow's rail car operations in North America. These operations include rail fleet management, rail fleet maintenance, rail service performance, and rail safety improvements. I have held this position since October 1994.

The Dow Chemical Company maintains headquarters in Midland, Michigan. Dow is engaged in the manufacture and sale of chemicals, plastic materials, hydrocarbons, and a variety of consumer specialties. Dow's wide range of products are used primarily as raw materials in the manufacture of customer products, or as aids or raw materials in the processing of customers' products and services. Dow ranks among the world leaders in the production of plastics, offering the broadest range of thermoplastic and thermoset plastic materials of any manufacturer. In addition, Dow is a world leader in the production of olefins, styrene, and aromatics. Finally, Dow's specialty segment is today comprised primarily of agricultural products and consumer products.

Dow operates five major production facilities in North America. By far, the two largest are located on the Gulf Coast near Freeport, Texas and Plaquemine, Louisiana. Dow operates smaller facilities at Midland, Michigan, Sarnia, Ontario, and Fort Saskatchewan, Alberta. Additionally, Dow operates a number of substantially smaller facilities located across North America. Dow's rail fleet consists of approximately 14,000 cars with annual rail shipments in excess of ninety thousand. Approximately one half of the Dow rail fleet (i.e., 7,000 cars) is utilized in shipping Dow products to and from the Gulf Coast.

Dow is very dependent upon efficient and timely rail service to and from its two Gulf Coast facilities. As a participant in the recent UP/SP merger proceeding (STB Finance Docket No. 32760), Dow voiced its concern about potential adverse impacts on these facilities which could result from the proposed merger. Because both of Dow's Gulf Coast facilities continue to be rail served <u>only</u> by the UP (i.e., the facilities are held "captive"), the impact of UP service failures are demonstrable and immediate on Dow's operations and therefore, also on our customer's expectations and needs.

As a participant in the on-going UP/SP oversight proceeding [STB Finance Docket No. 32760 (Sub-No. 21)], Dow had earlier commented favorably of the general progress of the merged UP. However, in his Verified Statement, Dow's William L. Gebo noted that a favorable comment on UP's performance was <u>only</u> as to that point in time and without the benefit (at that time) of seeing the effects of the merger on a broader basis. Soon after the submission of the Verified Statement of Mr. Gebo, Dow began to observe and experience an alarming deterioration in UP service and performance.

Dow has become extremely concerned with the rail service the Union Pacific railroad is providing to our manufacturing facilities, especially within the state of Texas and to Dow customers in general. A number of Dow plants have been shutdown or slowed because of lack of rail equipment caused by the Union Pacific service disruption. These Union Pacific service issues on Dow shipments began to escalate in August and September. Dow's rail service is continuing to deteriorate as we enter the month of October. Union Pacific service disruption on Dow shipments has appeared in three areas during the time frame of May, 1997 through September, 1997: (1) Union Pacific service failures on Dow shipments have more than doubled through September 1997 as compared to all of 1996; (2) Dow jeopardized cars on the UP/SP system that will not meet customer/Dow deliver schedules is at least 200% higher through the last week of September, 1997 versus the first quarter of 1997; and (3) Union Pacific performance target measuring % on time delivery against standards on key Dow strategic corridors is down from a goal for 1997 of 92.1% to a September actual of 53%. This is an all time low.

Various Dow plants in Freeport, Texas, Plaquemine, Louisiana, and Midland, Michigan have either slowed down or shutdown because of Union Pacific service disruption issues. In addition several Dow customers have been shutdown. In addition to the lost production or sales for Dow Chemical due to the UP/SP service disruption, Dow has had to switch numerous rail shipments to the truck mode thus incurring premium costs to move Dow products. Dow costs incurred through September, 1997 caused by the UP/SP service disruption totals at least $16 million this includes: (1) premium freight; (2) lost Dow production or customer sales; and (3) other costs such as fleet utilization decline and additional Dow resources to handle UP service disruption.

Of additional concern on Dow shipments is the issue of the impact of UP/SP service disruption and Union Pacific's ability to move time sensitive products in a timely manner. Dow has experienced emergency incidents that are related to poor Union Pacific service in moving time sensitive materials on a timely basis.

The UP/SP post-merger service which initially appeared to have little negative impact on Dow shipments and customers as early as May of 1997 has moved from a level of significant service disruption on Dow shipments in July 1997 to a major crisis for Dow's rail system in September. Dow logistical costs are rapidly escalating with each passing week and Dow's rail service with its customers is at an all time low. Dow needs service on Dow business on UP lines restored to at least the level of 1996 performance.

I, Harry J. Ignatowski, declare under penalty of perjury that the foregoing is true and correct. Further, I certify that I am qualified and authorized to file this Verified Statement. Executed this 10 day of October, 1997.

Harry J. Ignatowski

Harry J. Ignatowski

# VERIFIED STATEMENT OF CHARLES N. BEINKAMPEN

This statement is submitted by Charles N. Beinkampen, Director of Global Logistics, who has the authority to submit this statement on behalf of the E. I. du Pont de Nemours and Company.

DuPont is the largest chemical company in the world; a major producer of oil, natural gas and petroleum products and a leader in science and technology. The company operates 200 manufacturing and processing facilities in approximately 40 countries worldwide. DuPont is the second largest exporter in the United States. The company operates approximately 75 plants in North America and employs 65,000 in the United States. DuPont is the leading producer of Nylon intermediates which is the largest user of rail transportation.

DuPont is a significant user of rail service and a major customer of all the large railroads. The company operates a corporate fleet of 7000 rail cars with an estimated replacement value of $600 million. DuPont ships approximately 50,000 rail carloads annually for a cost of about $200 million which represents a significant percentage of the company's U.S. transportation cost. DuPont uses rail to transport raw materials to manufacturing facilities, transport semi-finished material from one DuPont plant to another DuPont plant and to ship finished products to DuPont's customers.

DuPont has several major plants on the Union Pacific Railroad which include Orange, TX; Victoria, TX; Corpus Christi, TX; LaPorte, TX; Texas City, TX; Denver, CO and Lake Charles, LA. These plants depend on rail transportation for inbound raw materials and outbound shipments of intermediates and finished product. These facilities ship approximately 23,000 carloads annually.

DuPont is a large shipper of hazardous materials and is very active in the Chemical Manufacturers Association's Responsible Care program. DuPont is concerned with the significant number of rail transportation incidents that have occurred in the industry. DuPont's record for the safe transport of hazardous materials historically has been a strong one. Even though DuPont has not experienced an incident with the Union Pacific, DuPont is concerned by the increased risk associated with Union Pacific's operating difficulties.

Since April of this year, DuPont has seen an erosion in Union Pacific's service. DuPont was experiencing transit delays on the majority of the shipments to plants or customers. Since July, Union Pacific's service has drastically deteriorated and transit time has increased by approximately 40%. DuPont's cars have been "lost" in UP's network, cars have been buried in an operating yard for 2 weeks and a total slowdown has occurred within Union Pacific's operating network. As an extreme example, Union Pacific mishandled a DuPont shipment which resulted in the car taking 78 days to reach destination. Normal transit time is 7 days.

These significant rail delays resulted in missed customer deliveries, plant curtailments, plant shutdowns and increased trucking and rail fleet costs. The financial impact is approximately $16 million year to date. Additionally, DuPont has experienced transit delays on intermodal shipments tendered for export business. These delays manifest in missed sailings to DuPont's overseas customers and creates a global disadvantage.

DuPont schedules processing operations based on the on-time delivery of necessary materials. By carefully managing the supply chain for just-in-time delivery of materials, DuPont operates facilities more efficiently and avoids additional inventory costs. When Union Pacific fails to provide reliable transportation, DuPont has to attempt to compensate by carrying more inventory and adding additional cars to the fleet. Union Pacific's deterioration in rail service has resulted in curtailed production, potential risk of jobs and missed customer shipments for DuPont and DuPont's customers.

I certify under penalty of perjury that the foregoing is true and correct.

C N Beinkamp

Charles N. Beinkampen
DuPont - Director of Global Logistics

October 6, 1997

# VERIFIED STATEMENT OF H. EDWARD PALMER

My name is H. Edward Palmer. I am Supervisor, Transportation Procurement for Eastman Chemical Company, a manufacturer and marketer of chemicals, fibers and plastics, based in Kingsport, TN. My address is 200 South Wilcox Drive, P.O. Box 431, Kingsport, TN 37662.

With 1996 sales of $4.782 Billion, Eastman Chemical Company is the 11th largest chemical producer in the United States. Eastman Chemical Company has major raw materials and product flows that are affected by the service problems currently affecting the Union Pacific Railroad Company system.

In my role as Supervisor, Transportation Procurement, I am responsible for the selection and procurement of transportation services for Eastman Chemical Company in all modes, including railroad freight services. I have been employed by Eastman Chemical Company for twenty (20) years in transportation, distribution and logistics functions, including rail equipment management, rail service management, and transportation procurement roles. I am authorized to file this statement on behalf of Eastman Chemical Company.

## DESCRIPTION OF EASTMAN CHEMICAL COMPANY, AND AFFECTED FACILITIES

Eastman Chemical Company manufactures and markets more than 400 chemicals, fibers and plastics. At present, 19 manufacturing sites are in operation or under construction in 11 countries. Eastman Chemical Company has its largest manufacturing locations in the United States, most of which are affected by the current service problems on the Union Pacific Railroad Company. The primary plants affected by these service disruptions, in order of magnitude of severity, are Texas Eastman Division, at Longview, TX; Tennessee Eastman Division, at Kingsport, TN; and Carolina Eastman Division, at Columbia, SC. Each of these three (3) plant sites are rail served, with Texas Eastman Division being directly served by the Union Pacific Railroad (as well as by Burlington Northern Santa Fe), and the other locations being served by rail carriers that interline with Union Pacific. The Texas Eastman Division plant ships and receives approximately 16,000 revenue carloads annually.

## DESCRIPTION OF DEGRADATION OF SERVICE, AND EFFECTS UPON EASTMAN CHEMICAL COMPANY

The Texas Eastman Division site, as well as the Tennessee Eastman Division site, has several major product flows into and out of the Houston area by rail, normally amounting to approximately 2,600 rail revenue carloads per year. In addition, the Texas Eastman Division site's rail service at Longview, TX is affected in other lanes by the deterioration in rail service extending outward from Houston. The loaded transit times for the rail movement from Longview, TX to Houston, TX have increased from three (3) or four (4) days prior to the UP/SP merger, to ten (10) to eleven (11) days transit at present. This has resulted in the need to ship much of this volume in tank trucks, at premium freight cost. The average monthly premium freight charges for these movements, as compared to normal rail movements, have been over $60,000. In addition, significant additional resources were required for extra expediting and special train premium charges to other destinations.

The Texas Eastman Division site also ships substantial numbers of cars to California. The loaded transit times have increased from thirteen (13) or fourteen (14) days on this movement, prior to the UP/SP merger, to widely varying transits ranging from fifteen (15) to thirty (30) days. Eastman has leased two hundred (200) additional hopper cars, at a cost of approximately $105,000 per month, to attempt to compensate for the additional transit times. However, this action has not been entirely successful, as sales have been lost.

During July, August and September of this year, plant downtime and lost production due to this rail service deterioration amounted to an average of over 6 million pounds in lost production volume per month.

In addition, there have been severe disruptions to the unit coal train operation by UP from the Powder River Basin of Wyoming to the Longview, TX plant site The normal seven (7) to eight (8) day orbits have deteriorated significantly; the most recent coal train had an eighteen (18) day orbit. Continued poor service of the coal train could easily cause a serious disruption to production capability.

Total premium costs for the last several months attributable to the UP/SP rail service disruptions have averaged $210,000 per month, in addition to the lost revenues and margins from the lost production volumes. For these reasons, Eastman Chemical Company supports the proposal of the Chemical Manufacturers Association for improving rail service over the Union Pacific Railroad system.

## VERIFICATION

I, H. Edward Palmer, declare under penalty of perjury that the foregoing is true and correct. Further, I certify that I am qualified and authorized to file this verified statement. Executed on the 8th day of October, 1997.

H. Edward Palmer
Supervisor, Transportation Procurement
Eastman Chemical Company
October 14, 1997

Ethyl

Ethyl Corporation
330 South Fourth Street
Richmond, Virginia 23219-4304
TEL: 804-788-5000

October 10, 1997

**Verified Statement of Russell L. Gottwald, Jr.**

My name is Russell L. Gottwald, Jr. and I am the Vice President - Product Supply for Ethyl Corporation headquartered in Richmond, Virginia. I am responsible for the worldwide purchasing, manufacturing, engineering and logistics at Ethyl. The intent of this letter is to inform the Surface Transportation Board of the deteriorating service on the Union Pacific Railroad and the costly results to our company.

Ethyl develops, manufactures and blends performance-enhancing and environmentally beneficial fuel and lubricant additives marketed worldwide to refiners and others who sell petroleum products for use in transportation and industrial equipment. Ethyl additives increase the value of gasoline, diesel and heating fuels as well as lubricating oils for engines, automatic transmissions, gears and hydraulic devices by improving combustion and fuel economy, lowering emissions, reducing metal wear and extended useful life of machinery.

Ethyl Corporation employees approximately 1500 people worldwide and has operations in Feluy, Belgium, Gent, Belgium, Houston, TX, Natchez, MS, Orangeburg, SC, Port Arthur, TX, Rio de Janeiro Brazil, Sarnia, Ontario, and Sauget, IL.

In the United States, Ethyl moves approximately 660,000,000 lbs. of product by rail annually. This represents approximately seventy percent (70%) of our total U.S. volume shipped on an annual basis. Approximately sixty five percent (65%) of this volume moves on the Union Pacific Rail System.

The deteriorating service has impacted nine Ethyl facilities including three Ethyl manufacturing sites located in Sauget, IL, Pasadena, TX, and Port Arthur, TX, three third party contract manufactures in Addis, LA, Crosby, TX and Gretna, LA, two contract drumming and warehouse facilities located in Port Arthur, TX and Houston, TX and one contract bulk export terminal in Deer Park, TX.

The following examples will clearly demonstrate the level of poor service we continue to receive from the Union Pacific. This is a small sample of the typical problems we experience daily.

**Example 1 -** Tank car ECDX 882011 shipped on August 29 from Sauget, IL to Houston, TX. The car arrived in Houston on September 9 but returned to Sauget on September 11 because incorrect billing was issued by the UP in error. The car departed again for Houston eight days later, September 19. The car arrived in Houston for the second time on September 23 but took seven additional days to interchange to the PTRA railroad for final delivery. The car finally arrived in Houston three (3) weeks late.

**Example 2 –** Tank car UTLX 74382 shipped on July 28 from Addis, LA to Lisbon, NY. Although the car was somewhere between the plant gate and the Livonia yard the entire time, the UP was unable to locate it. The car was reported lost on August 15 after repeated empty promises of departure. On August 20, the customer cancelled the order due to the delivery delay. The UP later notified Ethyl that locomotives had been diverted from the area to aid in alleviating congestion in Houston.

**Example 3** – Tank car ECDX 882328 shipped on September 18 from Sauget, IL to Roxana, IL routed GWWR–WOODRIVER-NS delivery. The normal transit for this move is 4 days. The GWWR delivered the car to an exclusive GWWR/NS interchange track on September 20. On the same day, the UP pulled the car from the interchange track in error. As of October 8, the UP has yet to return the car to the interchange track to enable the NS to complete delivery. The UP advised that the former SP yard staff was pulled and not replaced and the problem was a result of the inexperienced UP crew currently switching the yard.

Ethyl Corporation has incurred, as a direct result of the UP service problems, additional expenses of approximately $ 250,000.00, for the period of August 1, 1997 through September 30, 1997. The additional costs include but are not limited to additional administrative and operating costs, leasing of additional rail equipment and increased freight cost. This cost figure does not include lost business.

We respectfully request the Surface Transportation Board, to support the CMA/SPI petition and issue an order providing for the joint or common use of UP's facilities by other carriers, or issue other temporary changes in traffic handling and routing to resolve this problem in the most expedient way possible.

I, Russell L. Gottwald, Jr., declare under penalty of perjury that the foregoing statement is true and correct. Further, I certify that I am qualified and authorized to file this statement. Executed this 10th day of October 1997.

Sincerely,

Russell L. Gottwald, Jr.

Russell L. Gottwald, Jr.
Vice President – Product Supply
Ethyl Corporation

# VERIFIED STATEMENT

# OF

# MICHAEL E. PETRUCCELLI

My name is Michael E. Petruccelli. I am the Director of Distribution and Transportation, Chemicals for PPG Industries, Inc., One PPG Place, Pittsburgh, PA 15272 (PPG). I have been employed by PPG for 33 years in various capacities, including 24 years in rail distribution of its products. My duties include responsibility for the rail, highway and water needs of PPG Chemicals throughout North America. I am authorized to make this statement of behaif of PPG.

PPG is a multi-business, multi-plant corporation with manufacturing plants and other interests throughout much of the free world. In 1996, worldwide sales were in excess of $7 billion, of which approximately $4.7 billion was generated in the United States. In 1996, PPG had approximately 31,000 employees worldwide and approximately 20,000 in the United States. PPG owns and leases approximately 2,500 rail cars to transport various commodities including rail dependent commodities such as chlorine, vinyl chloride and 73% caustic soda.

PPG moves approximately 2.2 million tons of industrial and specialty chemicals each year to its North American customers utilizing its rail fleet of 2,500 leased and owned cars. Approximately 35% of this tonnage originates on the UP/SP system and additional tonnage moves over this system enroute from other ship points. In addition, our glass plants receive and consume over 320,000 tons of soda ash each year (nearly all of this originates on the UP/SP railroad).

PPG actively participated in the UP/SP merger proceeding before the STB in 1996. At that time, we were very concerned about the potential adverse impact that this merger would have on competitive service in and out of the Gulf Coast. We therefore opposed the merger unless very specific conditions were imposed by the STB. Unfortunately, most of those requested conditions were denied. Our biggest disappointment was that those specific requested actions, which would have provided real rail-to-rail competition, were not included in the final STB decisions. We are paying the price in the marketplace now by not having competitive rail service.

In October 1996, we started to experience various types of rail service delays on the combined UP/SP system in the Gulf Coast. This was about the time that the UP started the process of combining their operations with the SP as a result of the merger. A combination of other factors including derailments, a major ice storm and a number of railroad bridge and holiday shutdowns further compounded the problem during most of the winter months. At that time, we were experiencing delays of two to ten days. We increased our efforts to work with the UP operations people and, for the next several months, the UP/SP service in the Gulf Coast improved somewhat and, in some cases, got nearly back to normal.

Recently our worst nightmares have come true. Suddenly, in June 1997, the bottom fell out of the entire UP/SP rail system. We quickly went from serious service problems to a crisis situation. Today we are faced with a full disaster situation. Service on the UP/SP is worse than it has ever been.

Several of our customers have been forced to shut down. Others have come dangerously close to shutting down. We have been on the brink of shutting down our own plants because we are now running out of empty cars and critical raw materials. Initially, these disruptions were more or less limited to shipments originating from our large chemical plant at Lake Charles, LA. Recently, the problem has expanded to include inbound shipments of soda ash to Lake Charles and our glass plants at Wichita Falls, TX and Mt. Zion, IL. It has only been by substituting truck shipments, hiring special trains and around the clock expediting that we have not shut down more facilities. It has now reached the point that there are not enough trucks to continue to maintain the needed flow of products to our customers and materials to our plants.

In addition, it is important to note that the high volume industrial chemicals (chlorine, 73% caustic soda and vinyl chloride monomer) produced at our Lake Charles, LA plant can only be safely transported by rail and not by truck. Accordingly, the unreliable availability and routing of the special rail cars used for shipment of these products continues to threaten the continuity of production of many of our major customers who use these key intermediate materials for the manufacturing of end products. The emphasis on "just in time deliveries" in today's business climate further compounds the impact of the poor rail service on the UP/SP.

We estimate that PPG's direct out-of-pocket costs, caused by the serious deterioration of rail service on the UP/SP service for the past three months, exceed $1,000,000.

If this situation is not corrected immediately, the economic impact to PPG and its customers could skyrocket very quickly. For instance, if we have to shut down our Lake Charles chlor-alkali operations due to lack of empty chlorine cars, or either or both of our Wichita Falls, TX or Mt. Zion, IL flat glass plants due to the inability of the UP to deliver bulk raw materials (i.e. soda ash and caustic soda), our costs would quickly add up to many millions of dollars in a short time. In addition, we would face the possibility of major layoffs of employees at those locations. All three of the above plants are large volume continuous operations and the result of shutting any of them down would be an economic disaster.

The following facts for just two of our major products show the serious deterioration of UP/SP service during the third quarter 1997 on shipments out of our Lake Charles, LA plant.

| | Average Days 1996 | 1997 3Q | Δ Days | Δ % |
|---|---|---|---|---|
| **Caustic Soda** | | | | |
| Loaded Transit Time | 6.18 | 7.61 | +1.43 | +23.0% |
| Empty Transit Time | 5.76 | 7.72 | +1.96 | +34.0% |
| Total Transit Time | 11.94 | 15.33 | 3.39 | +28.0% |
| **Chlorine** | | | | |
| Loaded Transit Time | 4.57 | 6.68 | +2.11 | +46.0% |
| Empty Transit Time | 4.76 | 7.03 | +2.27 | +48.0% |
| Total Transit Time | 9.33 | 13.71 | +4.38 | +47.0% |

Although the above weighted averages are disturbing in themselves, we also have many specific point-to-point movements, not segregated in the chart, where the actual loaded and/or empty transit times have increased 50-100%.

Needless to say, the impact on service to our customers and utilization of our rail car fleet has been a total disaster the past three months. We have documented hundreds of examples of poor service on the UP/SP since June 1997, too numerous to include in this document. Since February 1997, we have met with and kept top UP/SP officials up to date on PPG's service problems on the UP/SP. We have continued to communicate and work with them to try and improve rail service to our customers and our plants. In mid-August we visited the UP/SP headquarters in Omaha to try and resolve these service problems. We had a good open discussion and left the meeting with an action plan we hoped would start to correct the service problems we had. Unfortunately, in spite of the efforts of the UP/SP's customer service and logistics people, the operating performance in the field has not gotten any better in most cases.

In our view, the Union Pacific's primary focus on cost reduction immediately following the merger has resulted in safety problems, labor disputes and very poor scheduling and dispatching that has resulted in completely unsatisfactory rail service performance. The Surface Transportation Board needs to consider all alternative actions that can be taken to expedite much more efficient movement of rail rolling stock and goods in the region served by Union Pacific. This may include directing the use of Union Pacific track by other capable railroad companies as long as such use will positively assist in the improvement of service in the affected regions.

Over the past several weeks, PPG has written letters to 48 key congressional members representing PPG's plants and our customer's plants who have been seriously impacted by poor UP/SP service. We have urged them to encourage the STB to exercise their oversight responsibility and authority over the UP/SP merger to help resolve what has become a transportation nightmare in this country.

Immediate and focused actions are required by the STB and the UP/SP to resolve serious and continuing adverse impacts on key manufacturing plants of both PPG and other major companies operating in the southern and central parts of the nation as well as the large number of customers served by these plants.

I, Michael E. Petruccelli, declare under penalty of perjury that the foregoing statement is true and correct. Further, I certify that I am qualified and authorized to file this verified statement. Executed this 6th day of September 1997.

Sincerely,

Michael E. Petruccelli

Michael E. Petruccelli
Director, Distribution & Transportation
PPG Industries, Inc.

SOLVAY

SOLVAY POLYMERS

*Quality Polymers Through Technology and People*

**Verified Statement of Michael Scherm**

My name is Michael Scherm. I am the Director of Logistics and Customer Service for Solvay Polymers, Inc.. I have been authorized to submit this statement on behalf of the company.

Solvay Polymers is a wholly-owned subsidiary of Solvay America, Inc. and a member of the worldwide Solvay group of companies. Our company manufactures 2.4 billion pounds of high density polyethylene and polypropylene plastic resin annually at our Deer Park, TX manufacturing facility.

Our principal means of product distribution is by railcar. We operate a fleet of more than 2700 privately-owned covered hopper railcars. Because 100% of our plant's production is loaded into railcars, the company is wholly dependent upon rail service to sustain our manufacturing operations and meet our customer's supply needs. We make more than 13,000 rail shipments annually.

We serve a customer base of more than 900 plastics processors located nationwide, Canada and Mexico. Our success, and our customers' continued operation, depends upon reliable rail service. The deterioration in the UP Railroad's service and its carryover effect on the BNSF has resulted in production shutdowns for us and our customers. In our efforts to meet our commitments to our customers, we have been and continue to be forced to make emergency shipments via bulk truck and even occasionally air freight. In addition, our railcar supply is no longer reliable. As a result, we have had to curtail production and source additional railcars. As a result of the current rail service problems, Solvay Polymers has been losing more than $235,000 a month. The problems have also adversely affected those who depend upon our production facilities for their business health - our customers, our suppliers and our service providers.

Every shipment from our manufacturing plant in Deer Park, TX must move through Houston on both the loaded outbound and empty inbound move. Since the first of the year alone, the average transit time for outbound shipments has increased by 15%. Average inbound empty railcar transit times have increased by nearly 20% in this same period. Once released, the amount of time a railcar takes to get out of Houston has increased from 1 to 2 days before January, 1997 to an average of 4 to 7 days today. Indeed, many times railcars have been lost for weeks and then re-discovered still in Houston.

Among the more notable areas affected by UP's service are UP destinations in northeast Texas, customers whose routing is BNSF over UP trackage rights and destinations in the Fort Worth area. For example, we recently had three railcars which were in transit for 49 days, 51 days, and 34 days to a Ft. Worth customer located only 300 miles from our Deer park plant. Our repeated efforts to work with the UP to move these cars more expeditiously were fruitless.

The UP's problems with mishandled shipments, lost railcars and railcars stranded on sidings has spread to other railroads interchanging with the UP. In short, the reliability of the entire rail

Solvay Polymers, Inc.
3333 Richmond Avenue, Houston, Texas 77098-3099 Mailing Address: P.O. Box 27328, Houston, Texas 77227-7328
713/525-4000 Fax: 713/522-2435 Customer Services: 1-800-527-5419

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system is in a crisis. We are to the point of being unable to predict when our shipments will be delivered, and we have even less confidence of getting our empty hopper cars back in a timely manner.

Although just this week the UP has announced plans to correct these problems, we have no reason to believe that they can do so without full cooperation and coordination with other railroads and direct oversight from some higher authority to provide needed accountability.

We urge the Surface Transportation Board to take immediate action under its current UP/SP oversight authority, or emergency service order provisions of the ICC Termination Act Sec. 11123. An immediate review of this situation is needed. We suggest that the UP should be required to submit a remedial action plan involving, and having the commitment of, all the railroads operating in the Gulf coast.

We are aware that the BNSF and the KCS railroads have made proposals which could, separately or in combination, provide immediate relief to the current rail congestion. These options must be given full consideration and ordered, if necessary, by the STB. As long as each of the railroads remain focused on its own interests, we fear the rail problems emanating from the Gulf Coast will remain unresolved well into 1998, costing American business millions of dollars more. An expedient solution requires the participation, cooperation and commitment to implementation by the UP, BNSF and KCS. The railroads will also have to be held accountable under specific measures to ensure that action is taken.

Left unchecked, we believe the situation will remain unresolved or get worse than it is today. This will be catastrophic for many Gulf Coast shippers and their customers throughout the nation, Canada and Mexico.

I, Michael Scherm, declare under penalty of perjury that the foregoing statement is true and correct. Further, I certify that I am qualified and authorized to file this verified statement. Executed this 10th day of October, 1997.

Sincerely,

M. Scherm

Michael Scherm
Director of Logistics and Customer Service
Solvay Polymers, Inc.

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**HUNTSMAN**

October 10, 1997

Mr. Vernon A. Williams
Secretary
Surface Transportation Board
1925 K Street, NW
Washington, DC 20423

**RE: UP-SP RAIL SERVICE PROBLEMS**

Dear Secretary Williams:

As Director of Transportation & Logistics for Huntsman Corporation, I would like to share with you my company's concerns over deteriorating service since the merger of the Union Pacific and Southern Pacific Railroads.

Huntsman Corporation is the United States' largest privately-held chemical company. Its operating companies manufacture basic products for the chemical, plastics, detergent, personal care, rubber and packaging industries. Huntsman-held companies have revenues in excess of $5 billion from multiple locations worldwide. Of the approximate 3 billion pounds of product shipped by rail per year, more than half originates in the southern gulf coast region.

Four of our facilities in Texas are captive on the UP: Chocolate Bayou, Bayport, Dayton, and Odessa. These locations make up about 20% of our total production shipped via rail. Although we are not captive at other locations, the combined UP-SP participates in many of our routes in the Midwest and West.

Moving our product has been particularly problematic in Fort Worth, where almost all traffic in and out of our Odessa facility is routed. Our business has been severely impacted at this facility because rail cars have been unable to get through the Fort Worth choke point. This has resulted in production cutbacks and increased truck shipments. We have had to lease 110 additional rail cars at a cost of approximately $63,000 per month. Adding cars to our fleet is a long term commitment because only new cars are available and suppliers will not lease new cars for less than five years.

The domino effect of the UP-SP problems has increased transit times for all rail shipments, which has affected every one of our facilities. We estimate that our additional trucking expenses exceed $200,000 per month for facilities in Chesapeake, VA, Port Neches, TX and Odessa, TX, combined. Shipments to customers which, prior to the merger, normally took five days now are taking 10-14 days, with sporadic situations of lost cars, misrouted cars and no bill cars which result in much longer transit times.

Delayed shipments of ethylene oxide from our facility in Port Neches, TX, to our Austin, TX, facility forced us to shut down operations for two weeks. As a result, we anticipate a claim from our customer of approximately $100,000 per day for our failure to meet contractual obligations. This delay by the UP was the result of congestion caused by a derailment which held up hundreds of cars between Valley Junction and Hearne, TX. Ethylene oxide is a hazardous material which should not be held up for extended periods of time. Just prior to the delivery of this rail car, we were making arrangements for emergency responders to inspect the status of the car.

We have a heightened concern for public safety based on these delays. Our emergency response teams recently responded when styrene in a rail car began to polymerize because its delivery was severely delayed. The product in the car solidified and generated tremendous heat and venting in the process. The press reported that the incident negatively impacted some 4,000 people living in the area. In addition, on September 18, 1997, fourteen rail cars derailed near Roscoe, TX, which blocked the main line and disrupted shipments and receipts into our Odessa, TX, facility. There were four Huntsman cars involved in this derailment. As a result, about $100,000 worth of plastic pellets were lost from one of our covered hopper cars. As such, we are growing increasingly concerned over the safety of our fleet.

We have made the UP-SP aware of these situations. Initially, as this congestion problem developed, UP-SP customer service tried to assist with normal response procedures. As congestion escalated to the present point, information, if you can get it, is not factual. Trip plans outlined in the UP-SP computer system develop into a wait-and-see approach.

We attempted on two occasions to help the UP-SP alleviate congestion on their lines by temporarily shipping product via the Burlington Northern Santa Fe. However, these requests were rejected. UP-SP eventually approved one shipment, but only after our plant had shutdown and they had a derailment on their line.

I am confident the UP-SP can pull out of this. However, we cannot afford to wait. We requests immediate action by the STB to issue an order providing for the joint or common use of UP-SP's facilities by other carriers, or other appropriate, temporary changes in traffic handling and routing.

I, David Parkin, declare under penalty of perjury that the foregoing statement is true and correct. Further, I certify that I am qualified and authorized to file this verified statement. Executed this 8th day of October, 1997.

Sincerely,

David Parkin

David Parkin
Director-Transportation & Logistics
Huntsman Corporation

Amoco Chemicals
Chemical Feedstocks Business Group
Transportation and Distribution
Mail Code 7043A
801 Warrenville Road
Lisle Illinois 60532
630-434-6297
Facsimile: 630-434-6380

Robert J. Theurer
Director

October 14, 1997

Secretary,
Surface Transportation Board
1925 K Street N.W.
Washington D.C.

## Verified Statement of Robert J. Theurer

My name is Robert J. Theurer. I am the Director of Transportation for **Amoco Chemical Company**, located at 801 Warrenville Road, Lisle, IL 60532.

I submit the following testimony in support of the Chemical Manufacturers Association ("CMA") and Society of the Plastics Industry ("SPI") petition for relief from the congestion in rail service currently being experienced in the Texas/Louisiana/Arkansas area.

Amoco Chemical, a Delaware corporation, is a wholly-owned subsidiary of Amoco Corporation. Amoco Chemical is engaged in the manufacturing, distribution, and marketing of chemicals, plastic resins, finished products, and fabrics. In North America, Amoco Chemical operates 20 plants. Amoco Chemical ranks among the top ten chemical companies in the United States in terms of chemical revenues.

Amoco Chemical is primarily a shipper of bulk chemicals and plastic resins and, as such, relies heavily on rail transportation, particularly for its outbound products . In 1996, Amoco Chemical shipped, in its owned or leased railcars, over 37,200 carloads, forty-four percent (44%) of which, approximately 16,400 carloads, originated in the greater Houston, Texas area ("Houston"). In 1996, Union Pacific ("UPRR") and the former Southern Pacific ("SP") originated over 13,400 carloads of Amoco Chemical's traffic across the UPRR rail system.

Amoco Chemical has five of its major plants located in the greater Houston area. Salient products, in decreasing volume sequence (excluding those that move <u>totally</u> by pipeline or marine), from these plants are: polypropylene plastic resin, linear alpha-olefins, styrene, polybutenes, alcohols, solvents, polyalpha-olefins and metaxylene. In this area, the Amoco Chemical transportation network is critically dependent on rail service and that from the UPRR in particular. This is supported by the following profile. Sixty-one percent of the nominal output from the Amoco Chemical plants in the greater Houston area (excluding those products that move totally by pipeline or marine), moves by rail mode. Of the rail volume, 86% originates on the UPRR. Two of those plants - the polypropylene plastic resin facilities at Chocolate Bayou and at Cedar Bayou - that account for 61% of Amoco Chemical's rail volume in the greater Houston area, are currently almost solely served by UPRR. The Chocolate Bayou plant is captive on UPRR. The Cedar Bayou plant was captive on Southern Pacific, and the location is still almost totally served by UPRR due to contractual considerations.

Because polypropylene plastic resin is the dominant commodity Amoco Chemical moved by rail in the Houston area, we focus our observations, though not exclusively, on the impact that recent UPRR congestion has had on operations at the Chocolate Bayou and the Cedar Bayou plants. Amoco Chemical is the second largest producer of polypropylene in North America, with installed capacity of 1.8 billion pounds per year, two-thirds of which is produced at Chocolate Bayou. Over 90 percent of the production from these plants is moved to customer destinations by bulk rail. About 13 percent of this traffic is moved UPRR direct. Most of the remainder is moved by the UPRR to the New Orleans, East St. Louis and Chicago gateways, in that order, and then interlined with other railroads.

The preceding profile illustrates how critical consistent UPRR rail service is to the Amoco Chemical transportation network. The size of our 1997 rail fleet was based on 1996 transit history. Amoco Chemical's ability to economically supply its chemicals and plastic resin to a worldwide customer base depends upon consistent, high quality rail service. Unfortunately, recent railroad congestion on UPRR in the Houston area has impacted the normal flow of railcars and has forced Amoco to cut back on production because UPRR has been unable to return railcars to our plants to consistently meet production schedules.

Figure 1 shows the ratio of monthly actual to planned production by month year-to-date for the combined Chocolate Bayou and Cedar Bayou polypropylene plants. The graph shows a definite increase in the production cutback level over the July-September period. **Production at Chocolate Bayou is being constrained to 13.4 percent below sales/ production demand, incurring marginal revenue loss at the rate of $1 million per month. This never occurred prior to the September 1996 UPRR/SP merger.**

**As of October 9th, 1997 rail problems directly associated with UPRR service to the five Amoco Chemical plants in the Houston area have resulted in lost production and increased transportation costs totaling over $7.4 million, and the monthly rate has been escalating.** These losses come from:

- marginal revenue on lost sales that resulted from throttling plant production
- premium transportation costs (freight and transfer handling), for use of truck transportation versus the more cost effective rail mode.
- raw and product material value downgrading e.g. having to fuel or flare (i.e. burn off) liquid material that cannot be transported or used as a result of throttled downstream operations.

The impact of the UPRR service on Amoco Chemical's plant operations has been mainly manifested in the polypropylene plant operations at Chocolate Bayou. Figure 2 shows the number of returning empty and shipped loaded hopper cars to and from this plant as a function of time since June 1996. The essence of this chart is found in the increasing frequency of zero empty rail cars being returned to the plant. Figure 2 shows:

- a steady decline in the average number of returning empty polypropylene hopper cars, and a lesser decline in the number of loaded polypropylene hopper cars. Note the crossover in early July 1997, when the trend line for the average number of empties begins falling below that for the loads.
- the high frequency of days in which (other than Sundays) no empty rail cars are returned to the plant - in April 1997 and late-August/September 1997.

Figure 3 shows the daily number of loaded and empty polypropylene hopper cars at the Chocolate Bayou plant from January 1997 to the present. The linear trend-line depicting the average number of empties on hand has been steadily declining. In May 1997, this average began to fall below 50 cars -- the "safety stock" level for empties given the planned production rate, the variability of the empty rail car supply, and the 99 percent service level -- needed to prevent throttling of plant production. **The combination of less than adequate empty railcars on hand and an increase in the frequency of days with zero empty railcars returned to the plant due to increased transit times, has led to increased throttling (refer again to Figure 1) and complete periodical shutdown of polypropylene production units at the Chocolate Bayou plant in the period July through September 1997. These units are large scale continuous processes which have limited turndown capability and cannot be brought up and taken down without incurring appreciable transition and off-specification product losses.**

The majority of the Amoco Chemical polypropylene resin rail traffic goes from the greater Houston area through the New Orleans and Salem/East St. Louis gateways. Transit time to the New Orleans gateway has increased by approximately 60% or two days. This increase ties up about 55 additional railcars in round trip rail service. Transit time to the Salem/East St. Louis gateways has doubled to eight days. This increase ties up about 55 additional railcars in round trip rail service. Just these increases cited represent a 6.6% increase in our polypropylene rail fleet requirement. This increased demand without adding cars to the fleet - a move that would only contribute to increasing system congestion - also exacerbates the supply flow of returning empties to our plants and threatens our ability to keep them running without interruption.

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Amoco Chemical wants a level of rail service from the post-merger (UPRR/SP) system, specifically with respect to outbound transit time, manageable return empty railcar flows without extreme variances, switching frequency to its plants served by UPRR, at least equal to those elements provided by UPRR, on its system prior to the referenced merger. I respectfully request that the Surface Transportation Board issue an order providing for the joint or common use of UPRR's facilities by other carriers, select dispatch control by those carriers and any other temporary traffic handling and routing measures that would restore pre-merger service levels in a specified time horizon not to exceed the end of 1997.

I, Robert J. Theurer, declare under penalty of perjury that upon information and belief the foregoing statement is true and correct. Further, I certify that I am qualified and authorized to file this verified statement. Executed this 14th day of October, 1997.

Sincerely,

R. J. Theurer
Director, Transportation and Distribution
Amoco Chemical Company

kvw/mk

**Mobil Oil Corporation**

3225 GALLOWS ROAD
FAIRFAX, VIRGINIA 22037-0001

October 14, 1997

Verified Statement of Garret G. Smith, Mobil Oil Corporation - Union Pacific Rail Service Problems

I am the Rail Transportation Manager for Mobil Oil Corporation, responsible for providing rail transportation services, including but not limited to freight rate negotiations, rail car procurement, maintenance, and fleet utilization for our petroleum and chemical manufacturing facilities throughout the United States, Canada, and Mexico. We handle approximately 30,000 rail car shipments annually.

A significant portion of this responsibility includes petroleum and chemical rail shipments originating and terminating at our refinery, lube blending plant, and chemical plants located in Beaumont, Texas. Additional refineries or plants are located in Hull, Texas; Chalmette, Louisiana; Paulsboro, New Jersey; Torrance, California; Joliet, Illinois; Edison, New Jersey; Vernon, California; Portland, Oregon; Cicero, Illinois; and Kansas City, Kansas. These facilities are responsible for manufacturing products such as gasoline and diesel fuels, liquefied petroleum gases (LPG) , petroleum wax, lubricating oils, additives, and various chemicals.

Mobil facilities located in Beaumont and Hull, Texas, generating approximately 9,000 total inbound and outbound rail shipments annually are served by the Union Pacific. Much of our rail traffic originating or terminating in this area is shipped to locations which are either "captive" to the Union Pacific, or served by the BNSF via trackage rights granted in the recent merger.

All Mobil rail transportation in and out of this area has been severely impacted by the service problems caused by the Union Pacific over the past several months. The following information documents many of the problems we are currently experiencing.

Prior to the merger, the SP served our Beaumont, Texas facilities. Service provided by the SP was poor by their own admission, however, it was exceptionally good in comparison to the current situation with the UP. Two of our key lanes which are served by the UP from origin to destination will illustrate the typical service we are receiving today.

- Beaumont TX to Laredo TX: This route is key for Mobil to move products into Mexico. Transit times early in 1997 averaged 10 days, grew to 13 days in July, jumped to 20 days in August, and remained at 20 days through September.

**Mobil**

- Beaumont TX to Vernon CA: Prior to the merger, transit times to this UP "captive" customer averaged 10 days, with a gradual increase to 14 days in May, 1997. In June and July, the average was 20 days. In August and September this number jumped to an average of 30 days transit time.

The initial source of the delays were reported as congestion in the Houston area. Cars would arrive in Houston and sit for days at a time. When we contacted UP Customer Service, we were told that shortages of manpower and locomotives were the primary cause of the problems. At one point, UP Customer Service advised us that they had as many as 600 complete trains in their system without locomotives or crews to run them.

As the congestion in Houston grew, additional bottlenecks were created at other key interchange points. Other railroads began suffering the same congestion problems because the UP was refusing to take cars destined for their railroad because there was nowhere for the cars to go. We are currently seeing this bottleneck problem very clearly in Beaumont, TX. Cars that were usually out of town within one or two days en route to their destination, are now taking a week or more. The UP readily admits that main hubs such as Houston and Fort Worth are too congested to receive additional traffic.

Unfortunately for Mobil, a high percentage of our rail traffic in the gulf coast area currently passes through Houston en route to our customers. Because of the congestion on the UP, all other railroads in the area have been impacted. One key customer in this area is located in Deer Park, TX., which is served by the Port Terminal Railroad Association (PTRA). Cars can be shipped out of Beaumont on either the UP to the PTRA or on the BNSF to the PTRA via trackage rights granted in the UP/SP merger. Prior to the merger, the SP/PTRA transit time was an average of 5 days. This traffic was awarded in March, 1997 to the BNSF via their trackage rights, and transit times increased to an average of 9 days through July. In August, cars have been as much as 30 days in transit.

Other significant delays have been seen on routes utilizing BNSF trackage rights due to the congestion created by the UP. A very large Mobil customer located in San Antonio, TX. has also experienced problems of inconsistent service and growing delays in transit times. Prior to the merger, SP served the customer direct from Beaumont in an average of 5 days. In July 1997, this traffic was awarded to the BNSF via their trackage rights. Service began at 11 days in July, and grew to 22.5 days in August and September.

Clearly we do not believe that trackage rights have allowed BNSF to effectively compete for traffic in this area. While they have managed to be price competitive, service as you can see in the above examples is another matter. We also do not believe that the BNSF is entirely to blame, however, we cannot continue to suffer with this kind of service and remain competitive for this business. A 600% increase in transit time to Deer Park, TX., and a 450% increase in transit time to San Antonio, TX. is not acceptable.

# Mobil

Service to our Hull, Texas facility has also been severely impacted by the congestion in the area. This location usually ships cars two to three times a week during our non-peak LPG season, which is approximately March through September. This plant recently went **one month** without receiving a "switch" to take cars out of the plant, which were destined to our customers. Repeated calls by plant personnel to the local railroad contacts resulted in no action by the UP. The only explanation provided by the UP was that the trains that normally pick up cars from this facility were full, and no more room was available.

What began as a UP problem in the gulf coast has now grown throughout the country on their system. Additional bottlenecks, such as Colton, CA. and North Platte, NE. have also severely slowed transit times. An example of the impact in other areas are shipments from our Paulsboro, NJ. lube plant to Los Angeles, CA., which are originated by Conrail and terminated by the UP. In March, 1997, the UP portion of this trip ranged between 9 and 10 days. In August and September, the UP transit time increased to 15-18 days. Delays to west coast destinations on the UP continue to grow.

Inconsistency of information from UP Customer Service is also a problem. We have had two or three different people call about the same car and received three different answers regarding location, status, and ETA. Congestion is the standard answer given to virtually all transit delays, followed closely by crew and locomotive shortages. We are relying on realistic ETA's and accurate information on car status to make business decisions that will help avoid plant shutdowns, production slowdowns, and lost customers. When faced with decisions on how to avoid plant shutdowns, we need realistic ETA's rather than giving us an answer we want to hear just to get us off the phone. In a large number of cases recently, the UP has been unable to give us any ETA, so we have no idea when the cars will arrive.

Cars are being "lost" and misrouted on the UP with increasing frequency. We believe that cars stay on trains in transit to another location because they have no room at the destination city or railroad interchange. We recently had a number of cars in transit to San Antonio, TX. from Beaumont, TX. that ended up in St. Louis, MO. before they were turned around and sent back to their original destination. Other cars shipped to the same customer continued on the BNSF to Eagle Pass, TX.(on the Mexico border) because the UP could not accept them due to lack of room in their San Antonio yard.

All of the problems described above have had a severe impact on our overall transportation costs. Prior to the recent service problems, the UP provided us with some service guidelines for all of our business. As a result, expectations were made by Mobil and our customers that we would receive a reasonable level of service based on those guidelines. Actual transit times experienced by Mobil, as shown in the above examples are beyond reasonable, and have caused extreme hardship on Mobil and our customers.

## Mobil

To date, we estimate that Mobil has incurred approximately $3 million in additional transportation expenses as a result of UP/SP merger related service problems during the past three months alone. This cost only includes expenses associated with emergency truck shipments and increased car fleets to continue to serve our plants and customers. These actions have been necessary to avoid plant shutdowns, slowdowns, last minute production changes, and customer out of product conditions. As we have a set of service expectations from the UP, our customers also expect that we will be able to deliver product to them in a consistent manner. In order to keep their business, we have had to absorb the expense to do whatever it has taken to supply them with product.

Not included in this cost are near plant shutdowns and the impact on plant operations and personnel. We have recently experienced two near shutdowns as a result of being unable to receive products at our refinery in Torrance, CA. and our chemical plant in Beaumont, TX. in a timely manner. In both cases, transit times on inbound shipments significantly exceeded already deteriorated service.

A car shipped on the Paulsboro, NJ. to Los Angeles, CA. route took 40 days total transit, 28 of which were on the UP. This car was to supply the Torrance, CA. refinery with product to keep a critical unit in operation. Emergency truck shipments were required to avoid a plant shutdown, which would have resulted in a multi-million dollar loss to Mobil.

A car shipped to our chemical plant in Beaumont, TX. originated on Conrail in Pennsylvania. This car took 34 days in transit, 26 of which were on the UP, and 23 of those days were spent on the UP just to get it through Arkansas. Extraordinary efforts were required on the part of plant personnel to avoid a plant shutdown by ordering an emergency truck shipment and manually emptying bags of the product versus receiving it in bulk via rail cars.

In addition to the costs associated with responding to situations such as this, we now have dozens of additional people at Mobil tracking the movement of rail cars and working on contingency plans in the event critical rail cars are not delivered in time. This has become necessary for specific customers, including distributors who rely on Mobil to provide products that keep them in business. We have a global marine customer that purchases lubricating oil, and because of UP transit delays, was recently in jeopardy because they did not have the product needed to operate their ships. Emergency truck shipments were required to keep their ships running, which depleted product supply from our alternate source and impacted more customers.

In an attempt to improve service over specific lanes, we have asked the UP to allow shipments over alternate routes and other railroads. Within the past couple weeks they have been more receptive to allowing this, however, they have not been willing to ship on alternate routes at our contracted rate. On top of expenses already incurred for emergency truck shipments and increased fleet expenses, we are now being asked to foot the bill by paying significantly more for using alternate routes to destinations "captive" on the UP to improve service to acceptable levels and to minimize our losses.

## Mobil

If the current level of service on the UP is allowed to continue, it is estimated that Mobil could incur $1 million to $2 million in extra expenses per month until it is resolved. This is not cost that can be passed on to our customers, and represents a direct loss to Mobil. By their own admission, the current plans in place by the UP would not resolve their service problems for several more months.

In order to minimize the loss and restore service at least to previous levels, we are asking the STB to intervene by issuing an emergency service order permitting other carriers to assist by whatever means necessary to resolve this problem as soon as possible.

We do not believe this assistance should be restricted specifically to the gulf coast area. As the UP continues to combine their operations with the SP on the west coast, it is anticipated that the same problems will cause an already bad situation to get worse. Service in the west on the UP has also steadily deteriorated, and they have yet to combine labor agreements and computer systems that are by their own admission key ingredients to a successful implementation. It is likely that if the problems are corrected in the gulf coast, they will migrate to the west unless the UP is forced to resolve them in advance.

We appreciate the time and consideration the STB is giving this matter, and look forward to a quick resolution.

I, Garret G. Smith, declare under penalty of perjury that the foregoing statement is true and correct. Further, I certify that I am qualified and authorized to file this verified statement. Executed this 14th day of October, 1997.

Doug [illegible]
for Garret G. Smith
Rail Transportation Manager
Mobil Oil Corporation

**AKZO NOBEL**

This verified statement is submitted on behalf of Akzo Nobel Chemicals Inc. by Mr. John Laciak. Mr. Laciak has been employed by Akzo Nobel Chemicals Inc. for twenty one years and is currently Distribution Manager. As Distribution Manager, he is authorized to submit this statement. Mr. Laciak is a registered practitioner and has over thirty years experience in distribution and transportation.

Akzo Nobel Chemicals Inc. is a Delaware corporation with headquarters at 300 south Riverside Plaza, Chicago, Illinois 60606. Akzo Nobel Chemicals Inc. is engaged in the production, sale and distribution of various chemicals and catalysts.

The catalyst business unit conducts manufacturing operations in Pasadena, Texas and Vernon California the Texas plant is served solely by the Union Pacific Railroad. The Vernon plant is within the switching district of Los Angeles.

Production levels are confidential.

The Pasadena plant ships and receives about one hundred and twenty (120) rail cars per month. The Vernon plant ships and receives about two hundred and fifty (250) rail cars per month. Akzo Nobel Chemicals' manufacturing operations are very dependent upon receiving raw materials by rail. Its customers, chemical manufacturers and refineries, are dependent upon receiving finished products by rail.

Akzo Nobel Chemicals' manufacturing operations at the Vernon plant are affected by transportation of a critical raw material by rail from its Pasadena plant. Akzo Nobel Chemicals Inc. Entered into a supplier customer relationship in 1995 with the Southern Pacific Railway. Both parties agreed to a transit time of five (5) days between Houston, Texas and Colton, California. Another six (6) days were allowed for terminal movements to and from the Akzo Nobel Chemicals Inc. plants.

The agreement began to pay dividends. In 1996 loaded movements, over two hundred and fifty (250) by the Southern Pacific, were delivered sixty-three percent (63%) on time within the eleven (11) day goal. This year due to Union Pacific problems, the average transit time is up forty (40%) percent through August; from ten (10) days to fourteen (14) days. Since may 1997 Akzo Nobel Chemicals Inc. has shipped eighty-nine (89) trucks to Vernon, CA to maintain production schedules and satisfy customers. Truck shipments have added $338,000 to freight expenditures.

Akzo Nobel Chemicals Inc.
300 South Riverside Plaza
Chicago, Illinois 60606-6697
Tel. (312) 906 7500
Fax (312) 906 7680

AKZO NOBEL

The average transit time on shipments from Vernon, CA to our customer in Corpus Christi, Texas has increased twelve (12%) percent with the Union Pacific; from seventeen (17) days in 1996 to nineteen (19) days. Since may 1997 Akzo Nobel Chemicals Inc. has shipped thirty-three (33) trucks to satisfy customer requirements. Truck shipments have added $67,000 to freight expenditures.

Akzo Nobel Chemicals' efforts to service this customer by a competing rail carrier were negated by the Union Pacific's refusal to provide that carrier with revenue requirements for delivery. To avoid delays due to congestion, Akzo Nobel Chemicals Inc. must now look for a distribution center in Texas to receive rail cars, transported by the competing rail carrier, and transfer material to trucks for deliveries to Corpus Christi, Texas.

I certify under penalty of perjury that the foregoing is true and correct.

John Laciak

John Laciak
Distribution Manager

Subscribed and sworn to before me this 30th day of Sep, 1997

Notary Public: [illegible signature]

My commission expires: 1-14-2001

Notary ... Illinois
My Commission Expires 01/14/01

Akzo Nobel Chemicals Inc.
300 South Riverside Plaza
Chicago, Illinois 60606-6697
Tel. (312) 906 7500
Fax (312) 906 7680

PHILLIPS PETROLEUM COMPANY
BARTLESVILLE, OKLAHOMA 74004 918 661-6600

TRANSPORTATION SERVICES

Secretary
Surface Transportation Board
1925 K St. N.W.
Washington, D.C. 20005

**Subject:** Rail Service Emergency

My name is Fred E. Watson, Transportation Supervisor---Commercial Transportation, for Phillips Petroleum Company (Phillips). My mailing address is 328 Adams Building, Bartlesville, Ok. 74004. My responsibilities include all rail contracting activities, rail service issues, and implementation of corporate rail and truck transportation strategies. I have been employed by Phillips for 22 years and have held various corporate logistics positions during that time.

Phillips is an integrated oil and petrochemical company engaged in the exploration, transporting, refining, manufacturing and marketing of certain oil and petrochemical products. We operate a fleet of over 4500 rail cars to effect the movement of our products from major facilities in Texas and Utah. In 1997, Phillips will generate revenues in excess of $50,000,000 to the nation's railroads. Phillips, therefore, has a substantial interest in the issue of reasonable and reliable rail service in general and in particular on the Gulf Coast.

In second quarter of this year, rail service began to deteriorate with each passing week. By the time August arrived, rail service west of the Mississippi River was poor, with the Gulf Coast area near "gridlock". Neither the Union Pacific Railroad (UP) or the Burlington Northern Santa Fe (BNSF) have been able to produce consistent, reliable results since their pre-merger days. Although the UP seems to be having the most problems, the extent that UP's problems are causing the BNSF's operating problems is known only by those two railroads.

In a effort to respond to rail cars not moving for weeks at a time, cars lost, many customer complaints, and lost plant production, Phillips switched certain routings to the Burlington Northern Santa Fe (BNSF), acquired additional rail cars, and increased our truck shipments. Phillips has not completed calculations on the increased costs attributable to poor rail service, but the figure will be significant and still, rail service improvements are not evident.

Exhibit (A) attached hereto illustrates how UP/SP rail service specifically has deteriorated on our plastic resins shipments from Houston over a recent three month period. From this data it is easy to see how customer relations, fleet costs, and manpower costs are being negatively impacted.

Shipper confidence in the rail service being offered by the UP is extremely low and this data is evidence why. In many cases, shippers like Phillips have given up on the rail option since the there is no assurance the rail car will arrive on time or even at all. Although Phillips has added some rail cars to its fleet to help address poor rail transit times, shippers adding cars to their fleets is not the answer.

Phillips is convinced that more excuses are not needed. What is needed is an effective operating plan for the Gulf Coast. Both the BNSF and the KCS/TexMex have offered new operating proposals for the Gulf Coast that seem to be a fair, no excuse attempt to address the need for additional rail infrastructure and improved rail service. The UP has offered their plan. Perhaps the best solution is some combination of all the plans and the best solution may require additional competition, not less, if the need for more rail infrastructure is properly addressed.

Phillips believes the Surface Transportation Board should review the railroad's proposals and quickly move to support a much needed revised operating plan for the Gulf Coast. Numerous industries and communities are depending on effective action by the STB.

I, Fred E. Watson, declare under penalty of perjury that the foregoing statement is true and correct. Further, I certify that I am qualified and authorized to file this verified statement. Executed this 7th day October, 1997.

Sincerely,

Fred E. Watson

Fred E. Watson
Transportation Supervisor, Commercial Transportation
Phillips Petroleum Company

# VERIFIED STATEMENT
# OF
# RICHARD C. WALTERS

My name is Richard C. Walters. I am Manager, North American Distribution for the Chemicals Group of Air Products and Chemicals, Inc. The Chemicals Group represents $1.5 billion of the $5.0 billion in annual revenues of Air Products and Chemicals, Inc. We produce and distribute intermediate and specialty chemicals worldwide, with 75% of our production and distribution in the United States. This represents approximately 2.7 billion pounds, of which 45% or 1.2 billion pounds, are transported by rail. In addition, 220,000 tons of inbound raw materials are transported by rail into our domestic plants. We utilize rail services at twelve of our plants, all of which have been affected by the current disruption in the Texas-Gulf area. Each of these plants ships or receives product from this region, and all have felt the effects of this situation. I appreciate the opportunity to provide this statement as to the effects that the current service failure of the Union Pacific Railroad has on our company.

It is not necessary to recite the history of the UP-SP merger, or to repeat the problems associated with the integration of the UP and the CNW. The issue at hand is the tremendous burden being placed upon the chemical industry by the Union Pacific through their ill-planned and poorly executed merger. This burden translates into severe economic hardship for our industry. One of our concerns during the merger evaluation period was whether shippers would bear the cost of this merger through higher rates. We were assured by UP management that competition would keep rates in check, and that we would benefit from the many service enhancements that would be made available by this merger. Obviously, they were incorrect on both points. We <u>are</u> bearing the cost of this merger, through higher cost truck service, through lost sales, through plant shutdowns, through higher equipment costs, and through higher administrative costs. And the promised service enhancements are only a memory, far from the nightmare that we live with today.

To help place in perspective the consequences that our company has endured, I offer several examples:

- During a recent four week period, movements of full and empty cars for a major raw material that one of our Midwestern plants receives from west Texas were delayed forcing us to source from other suppliers and utilize trucks. We incurred $3,300 in higher product costs and $92,000 for higher cost truck service.

- Tank car shipments to the Houston area ports were delayed causing us to miss the sailing of a vessel that was to contain 315 tons of bulk product for a Latin American customer. Rather than cause a 30-day delay for our customer, we incurred a $45,000 cost to have the ship return to port. This was our share of the $100,000 cost, the balance of which was paid by other companies.

- One of our New Jersey plants is dependent upon the railroads for a key raw material source in Texas. Since July, it has been necessary to ship twenty tank trucks to assure on-going production. Premium costs associated with these truck shipments have been $12,400 for transportation and $45,000 in additional charges from our supplier.

- Getting product to our Houston area customers is difficult enough. In early September, we received from a customer a full car of product at our Florida production site that had been billed as an empty. Upon further investigation we found that the UP had initiated return movements on five cars that had never been delivered to our customer.

- For most of our customer base, we are responsible for delivery of our products. A major customer in Texas has submitted a claim in the amount of $51,000 for lost production due to non-delivery of product.

- Recently the failure of the UP to make delivery to a customer in Missouri caused a potential plant shutdown. To assure continued production we shipped nine tank trucks at an incremental cost of $11,300. In addition to higher costs, this additional truck requirement is increasingly more difficult for our truck carriers to support as demand for truck equipment is at record levels.

- We utilize intermodal services for certain of our packaged products. Due to congestion in Los Angeles and poor service in Houston, we have had to revert to truck. This will cost us in excess of $10,000 per month.

- A railcar of methylamines, a hazardous material, bound from our Pace, Florida plant to a customer in Channelview, Texas, was lost. The car was eventually found by a Federal Railway Administration inspector at a plant of a company in the Houston area that does not do business with Air Products.

- We had conversations with a major raw material supplier regarding difficulties in continuing to assure uninterrupted supply to our two Northeast plants from Texas. We are jointly developing a barge-rail alternative that will eliminate the UP from the rail route. If fully implemented, this will increase the cost of this supply line by $30 - 35,000 per month.

- The safety record of the UP has deteriorated at an alarming rate. Within the past two weeks, a car containing ethylene was de-railed. Ethylene is a highly flammable product and is shipped in a specially constructed tank car. Fortunately, no one was injured and no product was lost, even though the tank was dislodged from its trucks. Though the incident was not catastrophic, we will be faced with significant downtime while the car is inspected and repaired and will undoubtedly have to replace the lost volume at a higher cost by truck.

- Our City of Industry, California, plant has had to resource a raw material and thereby receive trucks instead of rail. Net cost increase to our company is $38,000.

- Just this past week, delays in returning empty tank cars caused our Pasadena, Texas plant to decrease production rates. Lost production will result in $80,000 in lost margin, since production from this plant is normally fully allocated to our customers.

These are but a few examples of how our company has been affected by the Union Pacific to date. Every day we receive more details of threatened shutdowns, additional costs, and lost sales. Not yet quantified is the impact upon our management and administrative staffs. At headquarters we have increased car tracing support by 75%, and have similar additions at several of our plants. Plans to phase out numerous excess tank cars have been placed on hold, and we are now considering adding cars to our fleets.

Contrary to promises that shippers would not bear the cost of this merger, we are in fact bearing it in ways never imagined. Setting aside costs, which are, as stated, staggering, we are experiencing a complete breakdown of our ability to safely and effectively ship product by rail. We are increasingly concerned over the UP's ability to safely handle our products, most of which are regulated hazardous materials. We implore the Surface Transportation Board to intervene and utilize its statutory powers to protect the interests of the shippers and communities affected by this unfortunate situation.

I, Richard C. Walters, declare under penalty of perjury that the foregoing statement is true and correct. Furthermore, I certify that I am qualified and authorized to file this verified statement executed this 10th day of October, 1997.

Sincerely,

Richard C. Walters

Richard C. Walters
Manager, North American Distribution
Air Products and Chemicals, Inc.

# *Verified Statement of Eric W. Tibbetts*

My name is Eric W. Tibbetts. I am the Manager of the Rail Center for Chevron Chemical Company. My responsibilities include managing all rail transportation activities for Chevron Chemical Company. Chevron Chemical Company is a manufacturer and seller of polymers, petrochemicals and other industrial chemicals and end-use products.

It's domestic manufacturing plants are located in Baytown, Texas; Orange, Texas; Waxahachie, Texas; Belle Chasse, Louisiana; St. James, Louisiana; Knoxville, Tennessee; Abbeville, South Carolina; Marietta, Ohio; Fairfield, Iowa; Bloomfield, Iowa; Sparks, Nevada; and Colton, California. In addition, Chevron Chemical Company has contracted with several, third-party custom manufacturing and blending facilities in the U.S. which manufacture and beneficiate raw and intermediate products, acting as satellite manufacturing facilities for Chevron. The commodities transported are liquid and dry products including polyethylene, polystyrene, paraxylene, styrene, and additives.

Chevron Chemical Company ships approximately 2,000 railcars each month. The majority of the shipments originate in Marietta, Ohio; Orange, Texas and Baytown, Texas and are shipped to rail destinations throughout North America. A significant percentage of the Chevron rail shipments are either transported by the SP/UP or are moved over rail facilities controlled by the SP/UP for at least a portion of the trip.

Chevron Chemical Company serves over 1,500 customers at more than 2,000 destinations.

Chevron has observed a decline in UP service to the subject facilities since the second quarter, but the decline has become significantly worse since June 1997.

Attached are two charts which reflect an eighteen month and a one month view of the service the UP/SP has provided to Chevron's customers. Each chart clearly shows a decline in the carrier's service.

Chart I depicts the actual transit time, in days, from origin to destination and back to the point of origin, expressed as an index (the average round trip for the first quarter of 1996 is expressed as "100" and we have measured the subsequent quarterly averages against the Q1-96 period). For example, the Q3-97 period is 128% of the base quarter. That translates to 28% more inventory in transit, a 28% increase in fleet size and innumerable episodes of expediting "shutdown" cars.

Chart II is a metric Chevron created just over one month ago. We believe it is a reasonable picture of the "health" of our railcars on the UP/SP and is especially helpful to identify a trend of improving or declining service across the entire franchise. We have elected to track the number of cars which should be moving (i.e. Not at an interchange or storage track, etc.) but are "stuck" on the UP system for a minimum of 48 hours. Many have been stationery for longer periods. We have chosen to focus on the 48 hour period because we believe that any car held for a period longer than 48 hours will not meet our customers' expected delivery windows, unless we exert direct and active intervention with the carrier.

These charts indicate that Chevron is "baby sitting" between 80-180 cars per day and that the trend is increasing over the last six weeks. Despite Chevron's efforts, some number of

these cars do not reach their destination on time. This results in significant time, effort and substantial money being spent on emergency truck shipments, not to mention the gross inconvenience to our customers who may have to slow down or shut down their operations.

Chevron Chemical Company strongly supports the CMA position. We encourage the STB to carefully select a few comprehensive metrics, monitor with UP/SP their performance against those targets; and finally, if targets are not achieved, to issue Emergency orders which alleviate the congestion, regain shipping reliability and restore the public's confidence.

I, Eric W. Tibbetts, declare under penalty of perjury that the foregoing statement is true and correct to the best of my recollection and understanding. Further, I certify that I am qualified and authorized to file this verified statement. Executed this 9th day of October 1997.

Sincerely,

Eric Tibbetts

Eric W. Tibbetts
Manager, Rail Center
Chevron Chemical Company

**VERIFIED STATEMENT**

**OF**

**JOHN A. NOLL**

**Witness Qualification:**

My name is John A. Noll. I am Manager of Bulk Transportation for BASF Corporation (North America) located at 3000 Continental Drive - North, Mount Olive, New Jersey 07828-1234. In my position as Manager of Bulk Transportation, I am responsible for the procurement of bulk transportation including tank truck, tank containers, rail transportation and direct transloading, either rail to truck or truck to rail. The procurement activities of my department support all of the business units within BASF North America. I routinely work with all modes of transportation to provide transportation services for the distribution of BASF products.

Prior to holding this position I have held related positions in the transportation function including Manager of Pricing, Manager of Operations and Manager of Planning and Development. I have 31 years of logistics experience and have worked in the chemical industry for the past 23 years. In those positions, as in this one, I have been acutely aware of the significance of safe, environmentally sound, competitively priced, reliable transportation service(s) to the viability of the chemical business. My years of experience in the transportation industry have demonstrated that distribution costs and reliable on-time delivery are critical elements leading to efficient manufacture, marketing and supply of chemical products in a highly competitive industry.

I hold a Bachelor of Science in Logistics from The Pennsylvania State University as well as other industry certifications. I am very familiar with and have first hand experience in the service provided by the Union Pacific and Southern Pacific Railroads prior to their merger, as well as the service of the newly formed Union Pacific System as a result of the merger. The purpose of my statement is to demonstrate BASF's support for the development of an order under Section 11123 of the Interstate Commerce Act that will provide restoration of rail service on the Union Pacific System as well a normalization of rail service with Union Pacific connections that are suffering the ripple effect of the congestion and service disruptions on Union Pacific System.

**Background Information:**

BASF Corporation is the North America representative of the BASF Group, one of the world's leading chemical manufacturers. The BASF Group is a global organization with approximately 103,000 employees, serving customers in more than 170 countries around the world.

Headquartered in Ludwigshafen, Germany, BASF has production facilities in 39 countries. From its beginning in 1865 as a manufacturer of dyestuffs from coal tar, BASF has become a producer of a full range of products available from modern chemistry--from crude oil and natural gas to sophisticated, value-added consumer products. BASF sales worldwide are approximately $32.5 billion distributed among six operations--oil and gas, chemicals, products for agriculture, dyestuffs and finishing agents, plastics and fibers, and consumer products. BASF strives to be a reliable, environmentally and safety conscious corporate citizen throughout the world.

BASF Corporation (North America) is one of the 10 largest chemical companies in North America. BASF Corporation has annual sales of approximately $6.5 billion and has approximately 16,000 employees in the United States, Canada and Mexico. BASF Corporation manufactures and markets a broad range of chemicals, fibers, polymers, coatings and colorants to virtually every key industry and consumer products such as pharmaceutical, vitamins and agricultural supplies. BASF's determination to be a strong competitor in North America has been strengthened recently by a strategic restructuring through which we are emphasizing and improving our core competencies.

BASF Corporation is in the vanguard in the chemical industry with our efforts to build confidence in our manufacturing activities, to become more competitive in the North American and global economies and to include reliable distribution of our products to our markets, as well as safety and environmental protection as part of our strategy in the decision making process.

BASF Corporation produces well above 6 billion pounds of production each year. The most economical and preferred method of shipping our products is via rail transportation. Over 50% of all of the pounds produced at our manufacturing locations is shipped via rail transportation. The range of rail pounds shipped varies from 0% to as high as 99% predicated on the size of the site and the product mix. Our larger sites, namely Freeport, TX; Geismar, LA; Wyandotte, MI; Joliet, IL; and Altamira, Mexico range from 60% to 99% dependence on rail transportation to distribute their production to markets. BASF Corporation ships or receives approximately 38,000-40,000 carloads of traffic on average annually. BASF relies very heavily on the railroad industry to distribute its production directly to customers as well as to replenish supply of material at our various bulk terminal and transloading sites including terminals located at key ports for the shipment and receipt of products in international or foreign commerce. These bulk terminal facilities are the key to the balance of product supply for BASF's global markets and facility exchange programs which will intensify with the recent signing of the NAFTA and GATT trade agreements.

**Description of Impact on BASF Corporation:**

BASF Corporation has been directly impacted by Union Pacific service at facilities that are both on-line to the Union Pacific as well as facilities that are off-line to the Union Pacific. The current service levels have a severe impact on our distribution network on all traffic including outbound loads, empty car supply, site switching and raw material supply that move into, out-of or through the Union Pacific System. The impact of the UP/SP service deterioration includes:

- Our car cycles are completely out of sync;
- Raw material supply is erratic and remains extremely tight among 18 of our most important manufacturing locations;
- Our terminals have little or no inventory and shipments to our markets must be made directly from production;
- Production schedules are constantly changed predicated on the supply of empty cars or raw materials needed to sustain them and several of our sites have taken outages in advance of their schedules due to the disruption of material and car flow;
- Alternative methods to receive inbound raw materials have been and continue to be developed that have and will substantially increase our cost of production;
- Distribution costs for some products have increased dramatically, such as acrylate where our cost has increased from 3.5 cents per pound to over 9.6 cents per pound shipped;
- Inventory carrying costs have increased due to excess inventory in the rail pipeline caused by extended transit times and congestion;

- On a weekly basis, one or more of our production facilities is at risk of a shut-down; and
- The mishandling of our cars, including sensitive products, raises safety concerns.

Currently , a BASF production facility in Santa Ana is shut down due to lack of styrene because of the near gridlock of the Union Pacific's Colton, California yard. This material originates in Odessa, TX and travels through congested areas in Texas and Arizona before reaching the Colton Yard. This material, styrene monomer, is classified as a Flammable Liquid and contains inhibitors that protect the product from reacting while in transit. Should the inhibitor breakdown due to the longer transit time through warm climates, the material will react causing rupture discs to burst releasing material and toxic fumes into the atmosphere. The railroad's mishandling of this product en route may create a safety risk.

The BASF Freeport, Texas site and raw material suppliers in the Houston District of the Union Pacific System should be a high priority for operational support or action by the Surface Transportation Board. Tank truck lift capacity at Freeport, TX and Geismar, LA have reached maximum levels. Shipment dates are being missed and orders are being delayed . Congestion levels and rail car delays are equally important to BASF locations shipping through the states of Arkansas, Louisiana, Arizona and California.

**Areas of Additional Cost and Other Impacts:**

BASF has essentially changed its distribution network to satisfy internal and external customer order fulfillment requirements. We have experienced increases in transit times of 40% to more than 100% variation in loaded and empty trip times on our rail shipments and empty car return movements.

For the purpose of this statement we are providing the following specific examples of the increases we are experiencing in key routes. The percent increase shown is the increase in transit days on this route from third quarter 1996 to third quarter 1997:

| ORIGIN | DESTINATION | PRODUCT | PERCENT INCREASE |
|---|---|---|---|
| Freeport, TX | Aberdeen, MS | Acrylic Acid | 62% |
| Freeport, TX | Garyville, LA | Acrylic Acid | 75% |
| Freeport, TX | Chicago, IL | Butyl Acrylate | 156% |
| Freeport, TX | Chicago IL | Neol | 46% |
| Freeport, TX | Texas City, TX | Butyl Acrylate | 96% |
| Freeport, TX | Monaca, PA | Ethyl Acrylate | 46% |

| | | | |
|---|---|---|---|
| Freeport, TX | Midland, MI | Butyl Acrylate | 86% |
| Freeport, TX | Anderson, SC | Caprolactam Chips | 31% |
| Freeport, TX | Houston, TX | Ammonium Sulfate | 100% |
| Freeport, TX | Littlefield, TX | Ammonium Sulfate | 84% |
| Texas City, TX | Brownsville, TX | Butyl Acrylate | 60% |
| Texas City, TX | Cincinnati, OH | Plasticizer | 51% |
| Geismar, LA | Compton, CA | Polyol | 67% |

In addition, we have had a number of shipments that have been lost in transit or have "entered a black hole" while in transit and have placed our customers in jeopardy of shutting down. For example, UTLX 646483 was shipped on June 28th from our Geismar, LA facility. The car was lost in San Antonio, TX; mishandled back to San Antonio, TX ; delayed through Colton, CA; and finally delivered to Long Beach, CA on July 29th. BASF's relationship with a key customer was put in jeopardy due to the poor level of rail service.

We are currently gathering the detailed cost of the UP operational problems to BASF. An estimate of these costs is provided below.

| | August 1997 | September 1997 |
|---|---|---|
| 1. Added/Premium Freight Cost | $450K | $600K |
| 2. Cost of Lost Sales or Production | $ 25K | $100K |
| 3. Other Monthly Costs: (mileage credits, inventory carrying cost, administrative) | $ 75K | $100K |
| **TOTAL ESTIMATED** | $550: | $800K |

Although we have been forced to move to more expensive forms of transportation such as tank trucks, to maintain shipping during the UP/SP crisis, we are at the point where even that alternative is only available on a limited basis. Our core truck carriers simply do not have sufficient equipment available to be a viable substitute for the railroad. Although we have worked with carriers to move additional trucks and personnel into the affected regions, we can not maintain the service expected by our customers with alternate modes.

Due to the nature and mix of our product lines, we cannot add more rail cars to our fleets due to order lead times; the cars would take almost a year to build and would not be needed when rail service eventually returns to normalized levels.

**SUMMARY**

Union Pacific System service and congestion issues resulting from the merging of the Union Pacific and Southern Pacific Railroad systems has seriously impaired BASF's ability to efficiently provide effective distribution of products through our supply chain directly or indirectly to our markets. The impact is having severe cost implications, creating significant operational and production disruptions, and eroding the confidence levels of our customers, threatening our own viability.

BASF Corporation strongly urges the Surface Transportation Board to provide initiatives under Section 11123 of the Interstate Commerce Act that will provide for immediate measures that will restore Union Pacific Railroad service to normalized levels and or levels of safety and service that were enjoyed by BASF and its customer base prior to approval of the merger of Union Pacific and Southern Pacific Railroad systems.

# VERIFICATION

STATE OF NEW JERSEY

COUNTY OF MORRIS

John A. Noll, being first duly sworn, deposes and says: that he has read the foregoing statement, knows the facts therein, and that the same are true as stated.

John A. Noll

John A. Noll

Subscribed and sworn to before me this 17th day of October, 1997.

Ellen V. Roberts

Notary Public

My Commission Expires:

May 31, 2002

Ashland Chemical

Purchasing/Logistics Department
Systems/Processes
Training & Quality Group

Ashland Chemical Company
Division of
Ashland Inc.

Address Reply:
P.O. Box 1063
Columbus, Ohio 43216
Fax: (614) 790-3179

Secretary
Surface Transportation Board
1925 K Street, N.W.
Washington, D.C.

My name is Carol Sitz, Logistics Planning Specialist, Ashland Chemical Company, 5200 Blazer Parkway, Dublin, Oh 43216. One of my job responsibilities is to lead the Ashland Chemical Co. rail modal team; the team consists of six associates and as a group we are responsible for the planning and implementation of rail programs and policies for the company. A primary goal of this team is to work with rail carriers to provide consistent rail transit and strive for continuous improvement of rail service.

Ashland Chemical has twelve divisions; Ashland Plastics, Composite Polymers, Drew Industrial, Drew Marine, Electronic Chemicals, Foundry Products, FRP Supply, General Polymers, Petrochemicals, Specialty Polymers & Adhesives, Industrial Chemicals & Solvents, and Fine Ingredients. Ashland Chemical supplies more than 70,000 customers by all modes of transportation; the largest North American distributor of chemicals, thermoplastics and fiber-reinforced plastics, Ashland's markets include industrial manufacturing, transportation and plastics processing. The company produces and markets hundreds of specialty chemicals-from water treatment systems to ultra-high purity electronic chemicals for the semiconductor industry. Petrochemical operations combine methanol and maleic anhydride production with the marketing of petrochemicals produced at Ashland Petroleum's Catlettsburg, KY refinery.

Ashland Chemical has twelve plants served by the Union Pacific Railroad (UPRR), Composite Polymers Division (CPD) plants in Hayward, CA and Jacksonville, AR; Electronic Chemicals Division (ECD), Newark, CA; General Polymers Division (GP), Chandler, AZ; Industrial Chemicals & Solvents Division (IC&S), Chandler, AZ; Clearfield, UT; Fairfield, CA; Houston, TX; Midland, TX; Minneapolis, MN; Shreveport, LA; St. Louis, MO, and Petrochemicals Division, Allemania, LA. Ashland Chemical pays approximately 20 million dollars annually directly to rail carriers and purchases inbound raw materials and products for distribution, such as plastics, chemicals, and petrochemicals on freight delivered basis. The UPRR participates in approximately 27 percent of Ashland's rail shipments.



Headquarters:
5200 Blazer Parkway
Dublin, Ohio 43017
(614) 790-3333

Cable Address: Aroplaz OH
Telex: 245385
Answerback: ASHCHEM
Fax: (614) 790-4119

In addition to our plant locations, Ashland has raw material suppliers located at Odessa, Deer Park, N. Seadrift, Channelview, Texas City and Chaison, TX from whom we buy on a regular basis shipping to various locations which are also served by the UPRR. As a result of unavailable cars and extended UPRR transit times we have doubled our lead times to suppliers and have missed requested customer delivery dates. We have received emergency truck shipments to keep Ashland plants and our customers' plants running.

The UPRR has provided Ashland Chemical with standard transit for their portion of rail movements. During calendar year 1997, 75 percent of shipments between Allemania, LA and Chicago exceed standards, 100 percent of shipments between Allemania and Council Bluff, IA, 88 percent between Allemania and Kansas City, 21 percent exceed standard between Allemania and Memphis, between Geneva, UT and Salem, IL 33 percent of shipments exceed standard, from Houston, TX to Midland, TX 63 percent exceed, from Los Angeles, CA to Kent, WA 28 percent exceed standard, from Ogden, UT to Fairfield, CA 85 percent of shipments, and between Viola and Sweetwater, TX 35 percent of shipments exceed standard.

Ashland's methanol plant located in Allemania, LA is served by the UP. On 9/2, 9/10, 9/11, 9/12, and 9/18 available cars were not pulled into plant for loading. If we do not have cars available for loading, we cannot make customer requested delivery dates. During September, twenty-six cars pulled from this plant were not weighed as requested which also delays delivery to customers. On 8/8 and 9/19, we requested cars be reweighed but this was not accomplished.

Ashland Chemical has a resin plant in Los Angeles, Ca served by the LAJ. Prior to the UP/SP merger the interchange between the LAJ and SP was done five days a week. Since the merger we see approximately one interchange a week. This seriously affects the Plant's operations; both inbound raw materials and outbound customer shipments have been converted from rail to tank trucks at an additional cost of $23,700 for the month of August.

Another resin plant is located in Jacksonville, AR, also served by the UP. On 8/15 the UP pulled a full car of styrene as an empty in error; on 8/1 an empty car was pulled from the plant and inadvertently returned the following week. During August, raw materials originating in Louisiana were routed through Chicago due to congestion which caused transit delays; tankwagons had to be utilized to keep the plant operating resulting in $18,977 additional freight dollars. Jacksonville has had to make more than one call to get both loaded and empty cars spotted.

Ashland has an IC&S location in Fairfield, CA. During August two loaded cars were pulled from the plant as empties; the cars were returned after talking with the local yard. An empty car was released by Fairfield and pulled, two days later it was returned to the plant. Fairfield requested a car of acetone be pulled into the plant; it took three days for the car to be spotted. A meeting was held with local UP personnel to discuss missed switches.

Ashland also has a maleic plant at Neal, WV served by the NS. On April 4, 1997, we shipped a car (GATX 34444) to a customer on the UP in Lynwood, CA. We were able to get the car to the customer about May 9, there is conflicting information on actual placement. Due to the extended transit time, prolonged heating of the car's contents was required. The customer released the empty car to the UP on May 15. We were subsequently able to get the empty car interchanged to the NS at St. Louis on August 21. This is an approximate five month turn around time on a shipment which should take around four weeks.

We have also seen indications of morale problems with the UP operating and service center personnel. Our local plant people have been told to "write your Congressman" and to "get another railroad." Ashland's customer service people have experienced phone disconnects while seeking solutions to service problems.

Due to the vast number of occurrences and severity of Union Pacific's service failures, Ashland Chemical urges the STB to issue an order providing for the joint or common use of UP's facilities by other carriers, or any other temporary changes in traffic handling and routing that will provide relief from current UP service.

I, Carol R. Sitz, declare under penalty of perjury that the foregoing statement is true and correct. Further, I certify that I am qualified and authorized to file this verified statement. Executed this 26th day of September, 1997.

Sincerely

Carol R. Sitz

Carol R. Sitz
Logistics Planning Specialist
Ashland Chemical Company

**Allied Colloids**

Allied Colloids Inc
P.O. Box 820
Suffolk, Virginia 23439-0820

Tel 757 538 3700
Fax 757 538 3989

October 13, 1997

Mr. Vernon Williams
Secretary, Surface Transportation Board
Allied Colloids
1925 K St. N. W.,
Washington, D. C.

**Subject: Union Pacific Rail Service Problems in Texas/Louisiana/ Arkansas Area**

Dear Mr. Williams:

Allied Colloids Americas is an global manufacturer and marketer of speciality chemicals. Within the United States, we have manufacturing sites in Suffolk, VA; West Memphis, AR; Old Bridge, NJ; Batavia, IL; South Gate, CA, and Albemarle, NC. (Attached is a brochure that describes our business in more detail.)*

Raw materials are shipped from Texas via rail. Currently a total of 4-6 tank cars (186,000 lbs. ea.) of Acrylic Acid and 2 lubricating oil tank cars (180,000 lbs. ea.) are shipped per month. Since the merger of the Southern Pacific and Union Pacific, there have been significant delays in receiving material resulting in truck shipments which are more costly. Additional costs for tank truck shipments have averaged $9,000/mo.

Also there are two Allied Colloids suppliers located in Texas and Idaho that ship bentonite(clay) to customers located in Arkansas and Louisiana. Routings from Idaho are UP-Durant, OK-KRR and the standard transit time is 14 days. In the last two months, transit time has averaged 21 days. From Gonzalez, TX to our customer in Port Hudson, LA, the routing is UP-NEWOR-KCS and the standard transit time is 14 days. The past two months transit time has averaged 30 days. These delays have resulted in Allied leasing two additional railcars at a cost of $760 each per month. Additional freight costs for hopper trucks have totaled $8120 per month.

Anytime that we have had problems regarding these cars, we have called the UP Customer Service, only to be put on hold or not to reach anyone. When we have been able to talk to a person, the best they are able to do is register our issue as a problem log. It is rarely that we get any constructive response. We have been advised that the reason for the delayed deliveries is due to lack of power and employees to operate the trains.

An example of the problems that are occurring took place the week of 10/6/97. GPFX 10500 was due to deliver to Ashdown, AR on 10/10. The car was interchanged with the KRR on 10/8. On 10/9, the UP pulled the car and billed it out as an empty for Caldwell, ID, the origin. The car was still loaded and had never reached final destination. The car now has an ETA for delivery into Ashdown of 10/15 GPFX 10801 was due to deliver to the customer on 10/11.

* Descriptive brochure associated with original verified statement only.

It was necessary for the customer to receive one of these two cars by 8 AM, 10/13 in order to prevent shut-down.

Several phone calls were made between Allied Colloids' Traffic and Sales personnel, the UP and KRR on 10/10 to ensure that GPFX 10801 would delivery since GPFX10500 had gone astray. At 4:30 PM on 10/11, Allied received a phone call from the customer advising that the car had not arrived. Numerous phone calls then took place between Allied's Traffic, Sales, Customer Service, truckload carriers, UP and KRR on 10/11(Saturday) and 10/12(Sun) detailing the problem, trying to determine alternate solutions, trying to get the car moved to ultimately get product to the customer to prevent shut-down. The railcar had not moved on Friday or Saturday due to lack of power and crew. The end result was that we did manage to get the car delivered at ~9:00 Sunday evening through the combined effort of everyone involved. Allied Colloids does not have the resource to provide for each move like this one, nor should we have to provide such resource.

It is currently costing Allied ~ $18,640 per month in out-of-pocket costs due to the UP service problems. This does not include the additional employee resource that we have to use resolving these issues. To date, we have not lost any customers; however, we have come extremely close to shutting down our customers as well as our own plant.

Allied Colloids would like for the STB to issue an order for the joint or common use of UP's facilities by other carriers, or other temporary changes in traffic and routing to accommodate these service issues.

I, Ronda A. Bynum, declare under penalty of perjury that foregoing statement is true and correct. Further, I certify that I am qualified and authorized to file this verified statement. Executed this 13th day of October, 1997.

Sincerely,

Ronda A. By

Ronda A. Bynum
Transportation Manager
Allied Colloids

BEFORE THE
SURFACE TRANSPORTATION BOARD

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IN THE MATTER OF UNION PACIFIC CORPORATION, UNION PACIFIC RAILROAD COMPANY, MISSOURI PACIFIC RAILROAD COMPANY, SOUTHERN PACIFIC RAIL CORPORATION, SOUTHERN PACIFIC TRANSPORTATION COMPANY AND ST. LOUIS SOUTHWESTERN RAILWAY

SERVICE ORDER NO. 1518

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# PETITION OF THE BURLINGTON NORTHERN AND SANTA FE RAILWAY COMPANY TO INTERVENE IN SUPPORT OF THE JOINT PETITION FOR EMERGENCY SERVICE ORDER

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Jeffrey R. Moreland
Richard E. Weicher
Michael E. Roper
Sidney L. Strickland, Jr.

The Burlington Northern
and Santa Fe Railway Company
3017 Lou Menk Drive
P.O. Box 961039
Ft. Worth, Texas 76161-0039
(817) 352-2353

and

1700 East Golf Road
Schaumburg, Illinois 60173
(847) 995-6887

Erika Z. Jones
Janice G. Barber
Adrian L. Steel, Jr.
David I. Bloom

Mayer, Brown & Platt
2000 Pennsylvania Ave., NW
Washington, DC 20006
(202) 463-2000

Attorneys for The Burlington Northern and Santa Fe Railway Company


October 24, 1997

VERIFIED STATEMENT OF
ROLLIN D. BREDENBERG AND ERNEST L. HORD

This is the Verified Statement of Rollin D. Bredenberg and Ernest L. Hord. This statement will describe The Burlington Northern and Santa Fe Railway Company's ("BNSF") plan to address service problems described in the Joint Petition for Emergency Service Order filed by shippers on October 21, 1997. This statement also describes the resources BNSF would bring to bear to address the current service crisis in the Gulf Coast area if the Board grants the Joint Petition.

A.

BACKGROUND AND QUALIFICATIONS

Rollin D. Bredenberg. I am Vice President, Operations, South, of BNSF. My business address is 2600 Lou Menk Drive, Fort Worth, Texas 76131.

I began my career in the railroad industry at Southern Pacific Transportation Company ("SP") where I spent 29 years in various management positions. I was Superintendent from 1980 to 1981 and Assistant General Manager in 1981 at Houston. I was also General Manager at Houston from 1982 to 1983 and again from 1987 to 1991. I also was General Manager, Western Lines between 1983 and 1987. I joined The Atchison, Topeka and Santa Fe Railway Company in 1994 as Assistant Vice President, Intermodal Operations. From October 1995 to April 1997, I served as Vice President, Transportation. In April, 1997, I was appointed to my current position as Vice President, Operations, South, which encompasses BNSF operations throughout Texas, Louisiana, California, and the Southwest.

(i) PTRA should have temporary supervisory dispatching control of the HBT, as well as the entire Strang/Bayport Loop area, including Pasadena and Sinco, and the joint UP-PTRA line from PTRA North Yard to Deer Park Junction;

(ii) Directional train gathering and distribution flows should be instituted on a temporary basis to and from the Strang area; and

(iii) PTRA should be placed temporarily in charge of switching operations on the Baytown Branch.

Under these proposed steps, BNSF traffic originating at Strang would be moved directly to New South Yard and bypass Englewood Yard as reflected on Exhibit 2, saving an estimated three or more days in overall transit time. The implementation of each of these steps is described below.

**(i). PTRA as a neutral supervisor**

First, a neutral party with overall supervision of various terminal facilities in this area would provide even handed, impartial use of available resources geared toward overall efficiency rather than the interests of any single carrier. PTRA has proven itself to be an effective neutral operator in the Gulf Coast area. PTRA has institutional knowledge of the area, trackage, facilities and customers, and can be expected to fairly balance shippers' service needs with the needs of UP and BNSF.

**(ii). Temporary directional flow to and from Strang**

A key component of BNSF's plan is the temporary institution of a directional flow operation in the Strang area. As shown in Exhibit 2, Strang Yard is a relatively small hump yard located southeast of Houston. Presently, it is used to classify both inbound and outbound cars. However, Strang does not have the capacity to handle both inbound and outbound classification simultaneously. Currently, traffic originating in the Strang area,

UNITED STATES OF AMERICA

SURFACE TRANSPORTATION BOARD

+ + + + +

EX PARTE NO. 573

PUBLIC HEARING ON RAIL SERVICE

IN THE WESTERN UNITED STATES

+ + + + +

MONDAY

OCTOBER 27, 1997

+ + + + +

WASHINGTON, D.C.

The Public Hearing was held at the Surface Transportation Board, 1925 K Street, N.W., Suite 760, at 10:00 a.m.

BEFORE:

| | |
|---|---|
| LINDA J. MORGAN | CHAIRMAN |
| GUS A. OWEN | VICE CHAIRMAN |

we --

CHAIRMAN MORGAN: But then we still have Southern California, Sunset Route issues as well as continuing to clear up Houston, is that pretty well the summary of where we are?

MR. DAVIDSON: Well, that's it. But I would tell you, as far as the Sunset Route goes, there is very little blockage of any sidings on the Sunset corridor today except in connection with getting into Southern California. And Brad, how many trains did you say we had on the Sunset Route?

MR. KING: We had a total of 12. Some are Yuma to West Colton and then some are up towards Bakersfield, but a total of 12 that were staged.

MR. DAVIDSON: But on the Sunset Route you wouldn't -- the Bakersfield --

MR. KING: There's eight.

MR. DAVIDSON: There's eight.

CHAIRMAN MORGAN: But under your recovery plan you estimate that all of this will be resolved by January 1, is that --

MR. DAVIDSON: We do, and I would say to

you that I will be terribly disappointed if we're not substantially cleared up by very shortly after Thanksgiving. And I have confidence that we're making rapid enough progress that -- well, I'm just confident that we should not extend beyond Thanksgiving by any appreciable manner.

CHAIRMAN MORGAN: So your estimate of today is that within 30 days this will be resolved, in essence?

MR. DAVIDSON: Or very shortly thereafter, Chairman Morgan. We are making excellent progress. Now, my troops here may disagree me, but I do set goals in the company and that's my goal.

CHAIRMAN MORGAN: Now, given the difficulties of the past several months in trying to get to where we are today, if you were in our shoes here, would you be comfortable with concluding that this will be resolved in 30 days?

MR. DAVIDSON: If I were you, Chairman Morgan, I would continue to monitor us closely, call us to account. I don't know what your schedule looks like, but if you wanted to have us in shortly before

# TROUTMAN SANDERS LLP

ATTORNEYS AT LAW
A LIMITED LIABILITY PARTNERSHIP

1300 I STREET, N.W.
SUITE 500 EAST
WASHINGTON, D.C. 20005-3314
TELEPHONE: 202-274-2950
FACSIMILE: 202-274-2917

William A. Mullins

202-274-2953

October 30, 1997



HAND DELIVERY
The Honorable Vernon A. Williams
Secretary
Surface Transportation Board
1925 K Street, NW
Room 711
Washington, D.C. 20423

RE: Petition for Emergency Cease and Desist Order and Complaint

Dear Secretary Williams:

Enclosed for filing are the original and ten copies of the Petition for Emergency Cease and Desist Order and Complaint of The Texas Mexican Railway Company and The Kansas City Southern Railway Company. Also enclosed is a check in the amount of $2,300 for the filing fee as required by 49 C.F.R. § 1002.

The text of this pleading is contained on the enclosed 3.5-inch diskette. Please date stamp the enclosed extra copy of the pleading and return it to the messenger for our files.

Sincerely yours,

William A. Mullins
Attorney for The Kansas City Southern Railway Company

Enclosures
cc: Arvid E. Roach, II, Esquire
Erika Z. Jones, Esquire

**BEFORE THE**

**SURFACE TRANSPORTATION BOARD**

**The Texas Mexican Railway Company**
**1200 Washington Street**
**Post Office Box 419**
**Laredo, Texas 78042**

**and**

**Kansas City Southern Railway Company**
**114 West 11th Street**
**Kansas City, Missouri 64105**

**Complainants,**

**v.**

**Houston Belt & Terminal Railway Company**
**501 Crawford Street**
**Houston, Texas 77001**

**and**

**Union Pacific Railroad Company**
**1416 Dodge Street**
**Omaha, Nebraska 68179**

**and**

**Southern Pacific Transportation Company**
**1416 Dodge Street**
**Omaha, Nebraska 68179**

**and**

**The Burlington Northern and Santa Fe Railway Company**
**2600 Lou Menk Drive**
**P.O. Box 961034**
**Fort Worth, Texas 76161**

**Respondents.**

**Docket No.:__________________**

**PETITION FOR EMERGENCY CEASE AND DESIST ORDER AND COMPLAINT**

The Texas Mexican Railway Company ("TexMex") and Kansas City Southern Railway Company ("KCS") hereby submit the following Petition for Emergency Cease and Desist Order and Complaint alleging that Southern Pacific Transportation Company ("SP"), Union Pacific Railroad Company ("UP")(collectively, "UPSP"), and The Burlington Northern and Santa Fe Railway Company ("BNSF") have (1) unlawfully leased and/or acquired "joint use of" certain properties of The Houston Belt & Terminal Railway Company ("HBT") without seeking the required approval of the Surface Transportation Board ("Board") under 49 U.S.C. § 11323(a)(2) and § 11323(a)(6); and (2) the HBT is unlawfully abandoning or discontinuing its service without proper authority under § 10903.

Tex Mex and KCS seek an Emergency Cease and Desist Order from the Board ordering UP, SP, BNSF, and HBT to immediately stop their plan to divide the assets and operations of the HBT without the Board's prior approval under the Interstate Commerce Act. The Board must immediately stop the unlawful transactions and seek public comment on the proposal before allowing UP, SP, BNSF, and HBT to consummate the transaction, which is currently planned for midnight, October 31, 1997.

## JURISDICTION AND PARTIES

1. Tex Mex is a Class III rail carrier which owns and operates lines of railroad within Texas.
2. KCS is a Class I rail carrier which owns and operates lines of railroad throughout the MidWest and Southern United States. KCS owns a 49% interest in Mexrail, the parent company of Tex Mex.
3. HBT is a terminal rail carrier which leases and operates rail lines within Houston, Texas.
4. SP is a Class I rail carrier affiliated with UP which owns and operates rail lines throughout the Western United States.

5. UP is a Class I rail carrier affiliated with SP which owns and operates rail lines throughout the Western United States.

6. BNSF is a Class I rail carrier which owns and operates rail lines throughout the Western United States.

7. Additional complainants include various shippers on the HBT whose letters are attached to this Complaint and Petition for Emergency Cease and Desist Order.

8. The Board has jurisdiction of this Complaint pursuant to 49 U.S.C. § 11701.

**STATEMENT OF FACTS**

9. The HBT was incorporated in 1905 and was the subject of a large control transaction in 1950 by the Board in *Houston Belt & Term. Ry. Control*, 275 I.C.C. 289 (1950). Through a series of unapproved stock transactions since that time, UPSP and BNSF have each gained 50% of the stock of HBT.

10. On September 9, 1997, SP, UP and BNSF each filed a Notice of Exemption for overhead and/or local trackage rights over HBT's tracks. The Notices were published in the Federal Register on September 24, 1997. *See, Southern Pacific Transportation Co. -- Trackage Rights Exemption -- The Houston Belt & Terminal Railway Co.*, Finance Docket No. 33461, 62 FR 50049; *Union Pacific Railroad Co. –Trackage Rights Exemption -- The Houston Belt & Terminal Railway Co.*, Finance Docket No. 33462, 62 FR 50049; and *The Burlington Northern and Santa Fe Railway Co. -Trackage Rights Exemption – The Houston Belt & Terminal Railway Co.*, Finance Docket No. 33463, 62 FR 50049.

11. On October 20, 1997, UP sent a letter to the shippers on the HBT stating that the HBT will be dissolved effective November 1, 1997 and that UP will then be handling their business. *See*, Exhibit 1.

12. On October 25, 1997, the *Houston Chronicle* published an article in which UP and BNSF were both quoted as stating that the HBT will be dissolved as of November 1, 1997. *See*, Exhibit 2.

13. It appears that at midnight, Friday October 31, 1997, the Respondents plan to discontinue the operations of the HBT and dissolve the HBT. As evidenced by the shipper statements attached hereto as Exhibit 3[1] and the Verified Statement of Patrick L. Watts, Vice President - Transportation, The Texas Mexican Railway Company, Exhibit 4, these actions will cause serious harm to the shippers in the Houston area and cause harm to Tex Mex. The transaction will seriously alter the operations of, and the competitive balance of, the overall rail transportation system in the already devastated Houston area.

## ARGUMENT

### A. Emergency Cease and Desist Order

Complainants first petition the Board for an emergency cease and desist order preventing UPSP, HBT, and BNSF from ceasing HBT's operations and dissolving the HBT without prior approval of the Board and without notice to the public or the Board of their intention to undertake this momentous transaction. These actions are particularly disturbing because they occur in the midst of the largest crisis the railroad industry has ever seen and the dissolution is scheduled to occur merely four days after the Board held an emergency hearing on the rail problems in Houston, Texas and the rest of the UPSP service area and in the face of a soon to be

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[1] Given the fact that UP did not hold a meeting with HBT shippers until today, whereby UP explained its actions with respect to HBT, at the time of this filing, HBT shippers had little time to actually digest UP's explanations and to determine whether or not they will actually be harmed by the proposed transaction. However, based upon conversations between Complainants and the shippers who attended UP's meeting today, Complainants have indications that nearly a dozen shippers are concerned and will be filing statements with the Board. Given the fact that only three hours have passed since the end of that meeting and the filing of this petition,

issued order regarding those service problems. Now, without regulatory approval and little, if any, notice to shippers and the public, UPSP, BNSF, and HBT are planning on discontinuing the operations of a carrier and dissolving its operating functions right in the midst of this crisis and right in the area that is the heart of the rail service crisis.

The Board must immediately stop the illegal dissolution of HBT with a cease and desist order. The public has a vested interest in receiving proper notice of transactions and in having the Board review proposed transactions under the Board's proper statutory authority. The need for proper review of this transaction far outweighs any harm that UPSP, BNSF, or HBT would incur by delaying consummation of the transaction until such time as the Board and the public have had an opportunity to review the proposed transaction and discontinuance of HBT's operations. Therefore, the Board should immediately issue an Order for UP, SP and BNSF to cease and desist their dissolution of HBT and then begin an investigation of these unlawful acts.[2]

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Complainants were unable to gather any shipper statements. These statements will be supplemented as later appropriate.

[2] In ruling on cease and desist petitions, the Board has not always applied the same standards for issuance of stay petitions, which are found in *Washington Metropolitan Area Transit Commission v. Holiday Tours, Inc.*, 559 F.2d 841 (D.C. Cir. 1977) ("*WMATC*"). *See Fox Valley & Western Ltd.-Exemption, Acquisition and Operation-Certain Line of Green Bay and Western R.R. Co.*, 9 I.C.C.2d 272 (Jan. 22, 1993)("*Fox Valley & Western*"), *dismissed as moot*, 15 F.3d 641 (7th Cir. 1994), (cease and desist order issued without compliance with *WMATC*). Nonetheless, this petition meets the *WMATC* test. The four-criteria to be considered in determining whether emergency action is appropriate include: whether the petitioner has shown a substantial likelihood of success on the merits; whether the petitioner will suffer irreparable harm; whether other affected parties will suffer substantial harm; and where the public interest lies. *WMATC*, 591 F.2d at 843.

There is a strong likelihood that the Complainants will succeed on the merits of their complaint, *i.e.*, that UP, SP, BNSF, and HBT are unlawfully attempting to discontinue the operations of a rail carrier without Board approval and that UPSP and BNSF have, in the guise of trackage rights, really conducted a defacto lease of the properties of the HBT. *See*, additional argument in the Complaint for further support of merits of Complainants concerns. The Complainants and the shippers on the HBT will suffer substantial and irreparable harm if this transaction is allowed to proceed. *See* Verified Statement of Patrick Watts, Exhibit 4.

## B. **Complaint**

Under 49 U.S.C. § 11701, the Board has authority to begin an investigation of a rail carrier following the filing of a complaint. This authority includes investigating rail carriers who undertake actions without first obtaining the appropriate Board approval. *See, Chicago and N.W. Transp. Co. v. Kalo Brick & Tile Co.*, 450 U.S. 311 (1981). If the Board thereafter "finds that the rail carrier is violating [the law], the Board **shall** take appropriate action to compel compliance..." 49 U.S.C. § 11701(a) (emphasis added).

In this case, as noted in ¶ 10 above, Respondents have filed three Notices of Exemptions for trackage rights. These Notices of Exemption, taken together, constitute a grant of trackage rights over the entire properties of the HBT. Basically what is occurring is that the UPSP and the BNSF, who are each 50% owners of the HBT, have decided to divide the tracks and operations of the HBT between the two of them without seeking the required approval of the Board under 49 U.S.C. § 11323(a)(2), 11323(a)(6) and § 10903. Instead, Respondents have filed notices of exemption under 49 C.F.R. § 1180.2(d)(7) in an apparent effort to avoid the Board's scrutiny of their plan to dissolve the HBT and leave just a shell company. As stated above, UP and BNSF have been quoted and UP has stated itself that they plan to dissolve the HBT effective November 1, 1997. *See* Exhibits 1 and 2. Transactions of this nature cannot and should not be permitted under any class exemption which does not appropriately address the impact on the rail transportation policy.

A full investigation by the Board will show that the three trackage rights notices filed by the Respondents are an attempt to give away all of HBT's duties, operations, cars, engines, and other assets which will then allow Respondents to discontinue all of the operations of the HBT, leaving HBT as a shell company. All actions taken without public notice or the Board's scrutiny.

This is not the sort of outcome anticipated under a notice of exemption for trackage rights. Instead, these transactions fall squarely within the Board's jurisdiction under § 11323(a)(2), 11323(a)(6) and/or § 10903.[3]

Rather than being simply a case of a rail carrier (HBT) giving trackage rights to another rail carrier (UPSP or BNSF) and then both carriers continuing to provide rail service (i.e. the standard transaction for which the Notice of Exemption procedures at 49 C.F.R. § 1180.2(d)(7) were established), this is a situation whereby one rail carrier (HBT) is granting trackage rights to two carriers over its entire system and then the landlord carrier (HBT) intends on discontinuing its own operations. As such, the proposed transaction is analogous to several transactions with respect to the Kansas City Terminal Railway Company (KCT) which required Board approval under § 11323. For example, when KCT proposed to restructure its operations in a very similar manner as HBT proposes, KCT sought and obtained Board approval before undertaking those changes. *The Atchison, Topeka and Santa Fe Ry. Co. and Gateway Western Ry. Co. – Lease Exemption – Kansas City Terminal Ry. Co.*, Finance Docket No. 32238 (ICC served Feb. 17, 1994). In addition, when all remaining functions of the KCT were being transferred to another carrier and KCT was only keeping a residual common carrier obligation and its corporate name, Board approval was also required. *See, Kansas City Terminal Ry. Co. and The Atchison, Topeka and Santa Fe Ry. Co. – Contract to Operate Exemption – In Kansas City, Mo,* Finance Docket

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[3] Section 11323(a)(2) and (6) respectively provide that "[a] purchase, lease, or contract to operate property of another rail carrier by any number of rail carriers" and "[a]acquisition by a rail carrier of trackage rights over, or joint ownership in or joint use of, a railroad line (and terminals incidental to it) owned or operated by another rail carrier" … "may be carried out only with the approval and authorization of the Board." 49 U.S.C. § 11323(a). Alternatively, a rail carrier who intends to "discontinue the operation of all rail transportation over any part of its railroad lines" must file an application which must then be authorized by the Board. 49 U.S.C. § 10903(a)(1)(B).

No. 32896 (STB served Nov. 6, 1996) (The Board's ultimate decision on this proceeding has been held in abeyance pending a State court decision on the interpretation of contract terms.).

Furthermore, just as HBT in the past has done, or has been required to do, HBT and its respective shareholders should be required to seek the Board's approval for discontinuance of its operating authority. *See, Missouri Pacific Rd. Co. and Houston Belt & Terminal Ry. Co. – Construction and Operation – Exemption – Houston, Tx*, Finance Docket No. 30821 (Sub-No.1) (ICC served Nov. 10, 1996); *United Transportation Union v. Burlington Northern Rd. Co. and Houston Belt & Terminal Railway Company*, No. 40074 (ICC served March 25, 1987) (HBT and BN advised that Commission approval was required under § 11343); *Houston Belt & Terminal Ry. Co. – Discontinuance Exemption – In Harris County, Tx*, Docket No. AB-423 (Sub-No. 1X) (ICC served April 26, 1995); *Missouri Pacific Rd. Co. – Abandonment and Discontinuance of Operations Exemption – In Houston, Harris County, Tx; Houston Belt & Terminal Ry. Co. – Discontinuance of Operations Exemption – In Houston, Harris County, Tx*, Docket No. AV-3 (Sub-No 139X) and Docket No. AB-423 (Sub-No. 2X) (STB served Dec. 31, 1996).

Indeed, not only are the plain words of the statute clear, but it is also long standing precedent that a carrier that seeks to discontinue operations must either (1) seek authority from the Board, *Thompson v. Texas Mexican Railway Co.*, 328 U.S. 134, 143-144 (1946); *Chicago and N.W. Transp. Co. v. Kalo Brick & Tile Co.*, 450 U.S. 311 (1981); (2) sell those obligations to another carrier through a lease or line sale, *Hanson Natural Resources Company – Non-Common Carrier Status – Petition For A Declaratory Order*, Finance Docket No. 32248, slip. op at 20 (ICC Served Nov. 15, 1994)("a common carrier railroad may acquire, construct, or abandon a railroad line, or commence or discontinue operations thereover only if we issue either a PC&N or an exemption"); or (3) seek authority from the Board for an entire system abandonment, *Chicago*

*Rock Island and Pacific Railroad Company, Debtor (William M. Gibbons, Trustee) - Abandonment - Entire System*, 363 I.C.C. 150 (1980). If a carrier were allowed to discontinue its obligations in the manner in which UPSP, BNSF, and HBT propose, then nothing would prevent KCS, for example, from granting BNSF local trackage rights over its entire system (utilizing a Notice of Exemption under 1180.2(d)(2)) and then simply stopping its own service over all of its lines. Obviously such a transaction would significantly alter the competitive and operational aspects of the operations of a rail carrier and the Board would not allow this to happen without adequate scrutiny. Yet, this is precisely what HBT is attempting to do.

It seems more than coincidental that after previously seeking Board approval to discontinue its operations, Respondents are now attempting to pull the biggest "trick" of all on the already devastated shippers in Houston on the eve of Halloween. The Board must stop this flagrant attempt to circumvent appropriate review of this major transaction will which directly impact rail transportation and operations in Houston and affect Houston shippers and the Tex Mex.

## RELIEF REQUESTED

WHEREFORE, complainants respectfully request that the Board issue an Emergency Cease and Desist Order prohibiting UP, SP, BNSF, and HBT from discontinuing HBT's operations and dissolving the HBT without the Board's prior approval.

And WHEREFORE, Complainants request that the Board initiate an investigation of the actions of UP, SP, BNSF, and HBT as stated herein.

Respectfully Submitted, this 30th day of October, 1997.

Richard P. Bruening
Robert K. Dreiling
KANSAS CITY SOUTHERN INDUSTRIES
114 West 11th Street
Kansas City, Missouri 64105
Tel: (816) 983-1392
Fax: (816) 983-1227

Richard A. Allen
John V. Edwards
Zuckert, Scoutt & Rasenberger, LLP
888 17th Street, N.W.
Suite 600
Washington, D.C. 20006-3939
Tel: (202) 298-8660
Fax: (202)

Attorneys for The Texas Mexican Railway Company

William A. Mullins
Sandra L. Brown
TROUTMAN SANDERS LLP
1300 I Street, N.W.
Suite 500 East
Washington, D.C. 20005-3314
Tel: (202) 274-2950
Fax: (202) 274-2994

Attorneys for Kansas City Southern Railway Company

EXHIBIT 1

UNION PACIFIC RAILROAD COMPANY

October 28, 1997

To: MR. RON BIRD
COMMERCIAL METALS

As you may already know, the Houston Belt Terminal will dissolve effective November 1. At that time, Union Pacific will begin handling your business transactions. To discuss the specifics of how your transactions will be handled and the actions required to ensure a smooth transition, Union Pacific would like to invite you to a Communication Session at the Houston Airport Marriott.

Customers with company names starting A-L are encouraged to attend the 9 a.m. session while customers with company names starting M-Z are encouraged to attend the 2 p.m. session. Each session is expected to last approximately two hours.

When: October 30, 1997, 9 a.m. (Company Names A-L)
October 30, 1997, 2 p.m. (Company Names M-Z)

Where: Houston Airport Marriott - Ballroom A
18700 John F. Kennedy Blvd.
Houston, TX 77032
For directions, call (281) 443-2310

You should receive an information packet prior to the Communication Session detailing how to do business with Union Pacific after the conversion. Please bring your packet with you.

We look forward to seeing you on October 30.

Sincerely,

Jim Damman
*Vice President-National Customer Service Center*

UNION PACIFIC RAILROAD COMPANY

October 20, 1997

To: Mr. Ron Bird
COMMERCIAL METALS

As you may already know, the Houston Belt Terminal will dissolve effective November 1. At that time, Union Pacific will begin handling your business transactions. To discuss the specifics of how your transactions will be handled and the actions required to ensure a smooth transition, Union Pacific would like to invite you to a Communication Session at the Houston Airport Marriott.

Customers with company names starting A-L are encouraged to attend the 9 a.m. session while customers with names starting M-Z are encouraged to attend the 2 p.m. session. Each session is expected to last approximately two hours.

When: October 30, 1997, 9 a.m. (Company Names A-L)
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Houston, TX 77032
For directions, call (281) 443-2310

You should receive an information package prior to the Communication Session detailing how to do business with Union Pacific after the conversion. Please bring your packet with you.

We look forward to seeing you on October 30.

Sincerely,

Jim Damman
Vice President - National Customer Service Center

EXHIBIT 2

Houston Chronicle   Saturday, Oct. 25, 1997

# Railroads to split local short-haul line

## Move to dissolve Houston Belt & Terminal comes in for criticism

By CHARLES BOISSEAU
Houston Chronicle

With railroad tracks clogged and service problems making headlines nationwide, the city's two largest railroads are planning to carve up the jointly owned Houston Belt & Terminal Railway Co. — which some customers and rail experts fear could make the problems even worse.

The short-line railroad, which at one time was owned by five or more carriers, today is owned by just two: Union Pacific Railroad and the Burlington Northern and Santa Fe Railway Co.

On Nov. 1, the railroads plan to dissolve Houston Belt & Terminal's operations and split up its tracks and employees, spokesmen at both companies confirmed.

Customers north and east of the Galveston, Houston and Henderson line (which runs roughly parallel to Interstate 45) will go to Union Pacific and the others will go to Burlington Northern.

Some customers are worried that the dismantling of the railroad will give them fewer options, raise their costs and cause even more tie-ups.

"If you take the business that Houston Belt & Terminal is handling right now ... and you inject that into an already congested Union Pacific system, we're very concerned we're going to have problems," said Ron Bird, a transportation manager with Dallas-based Commercial Metals Co., which has a scrap metal facility at 2015 Quitman.

Bird worries that after Nov. 1, when his facility is served only by Union Pacific, he won't be able to send rail cars as easily and cheaply over the competing Burlington Northern line.

The move comes at a time when shipping groups are calling on the federal Surface Transportation Board to order new, neutral third-party railroads to provide switching services to help alleviate chronic congestion on Union Pacific's tracks. Instead, these railroads are going the other direction by eliminating such a carrier, Bird said.

The plan to split up Houston Belt & Terminal had been in the works before the rail congestion became acute, said John Bromley, spokesman with Omaha, Neb.-based Union Pacific. He said the need for small lines is not as great as in the past because numerous railroad mergers left only a few carriers to more easily divide traffic among themselves, he said.

Houston Belt & Terminal, founded in 1905, operates 250 miles of tracks in the industrial corridors of the city. It was formed to operate on tracks leading to individual customers — eliminating the need for multiple lines from rival railroads. It then brings the traffic to the big railroads for transport to the final destinations.

Last week, Houston Belt & Terminal completed the sale of its downtown Union Station and 18 surrounding acres to the Harris County-Houston Sports Authority for $10.7 million. After planned renovations, the aging Union Station will become the main entrance to the city's planned new baseball park.

Mark Arnold, attorney with Mayor Day Caldwell & Keeton and general counsel for the sports authority, said the purchase was unrelated to the decision to dissolve Houston Belt & Terminal. Bromley of Union Pacific agreed, noting the building was used only for offices.

Another, similar railroad is the Port Terminal Railway Association, a partnership between the Port of Houston Authority, and Union Pacific and Burlington Northern.

There are no plans to dissolve this railroad, Bromley said. Martha Williams, general counsel of the Port, said any such action would be difficult without the Port's approval because the Port owns most of the tracks.

Jim Sabourin, spokesman with Fort Worth-based Burlington Northern, said that dissolving Houston Belt & Terminal will allow more efficient switching of cars at south Houston yards, where Burlington Northern cars are frequently getting hung up in Union Pacific's current logjam.

Also, he said, all customers will continue to have access to both carriers because railroads have rights to operate over each other's tracks.

But some are skeptical that those rights would accord the same access as they have now.

Others are upset because the action apparently is being taken without any public comment or approval by the Surface Transportation Board, which regulates the business aspects of railroads.

Bromley said the railroads do not need government approval because they are leaving Houston Belt & Terminal in place as a shell compan but without any employees, meanin there is no sale or transaction th requires board approval.

"This is a matter that is being i ternally handled," Bromley said.

A staff attorney at the board's i Washington said it had no knowledg the carriers intended to dissolv Houston Belt & Terminal, or reason to show it.

Paul Broussard, a Houston tran portation and logistics consultan complained, "This is a common ca rier, serving the public and publ transportation, and yet they've elim nated that railroad without any inp from the public."

"It's just market dominance by rail carrier, it's total control by th railroad," he said.

Larry Fields, president of Lared based Texas and Mexican Railwa Co., said, "I don't see any way it's g ing to help. It will restrict the option that customers have, and I don't se it will benefit anyone except BN an UP."

Fields said he intends to criticiz the plan to eliminate Houston Belt Terminal at a hearing Monday i Washington before the Surfac Transportation Board, where he one of 80 speakers scheduled to tes tify.

The board called the all-day mee ing to put Union Pacific under th microscope and determine whethe it needs to take action to resolve th rail congestion — which began i Houston this summer and ha stretched to the West Coast and Mid west, slowing shipments of every thing from grain to automobiles.

EXHIBIT 3

SHIPPER STATEMENTS TO BE FILED AT A LATER DATE.

EXHIBIT 4

VERIFIED STATEMENT

OF

PATRICK L. WATTS

My name is Patrick L. Watts. I am the Vice President - Transportation of the Texas Mexican Railway Company head-quartered at 501 Crawford Street, Room 317, Houston, Texas 77002. I am submitting this statement in response to the plan of the Union Pacific Railroad Company (UP) and the Burlington Northern Santa Fe Railway Company (BNSF) to dissolve the Houston Belt and Terminal Railway Company (HB&T).

The UP and BNSF are planning to divide the ownership, tracks, dispatching, and customers of the HB&T amongst themselves effective November 1, 1997 without any prior submission of intent to federal, state, and local agencies. The first such public notification came in the way of a letter tele-faxed to customers by the UP on October 20, 1997. The first paragraph of this notification begins, "As you may already know, the Houston Belt Terminal will dissolve effective November 1. At that time, Union Pacific will begin handling your business transactions. To discuss the specifics of how your transactions will be handled and the actions required to ensure a smooth transition, Union Pacific would like to invite you to a Communication Session at the Houston Airport Marriott."

The next public notice was in an article written in the Houston Chronicle on October 25, 1997. The Chronicle reported:

> *John Bromley, spokesman with Omaha, Neb. – based Union Pacific... said the need for small lines is not as great as in the past because numerous railroad mergers left only a few carriers to more easily divide traffic among themselves. The railroads do not need government approval because they are leaving Houston Belt & Terminal in place as a shell company, but without any employees, meaning there is no sale or*

*transaction that requires board approval. This is a matter that is being internally handled.*

The Houston Belt & Terminal Railway Company was first formed in 1905. Its role over the past 92 years has been to provide rail service to shippers and then independently and neutrally marshal those shipments amongst the interstate and intrastate rail carriers that served Houston. This allowed the shippers served by the HB&T to have equal access to multiple rail carriers.

The Surface Transportation Board (STB) awarded the Texas Mexican Railway Company trackage rights and limited access[1] to Houston customers in *Union Pacific Corp., Union Pacific RR Co. and Missouri Pacific RR Co. - Control and Merger - Southern Pacific Rail Corp., Southern Pacific Trans. Co., St. Louis Southwestern Rw. Co., SPCSL Corp., and the Denver and Rio Grande Western Corp.*, Finance Docket No. 32760, Decision 44 (STB served Aug. 6, 1996). HB&T has been very neutral and helpful in our attempts to generate business via the rights granted in the UP/SP merger. Under Bill Mathis' (General Manager, HB&T) leadership, the HB&T employees have done an excellent job in allowing the TexMex to have equal treatment while operating across the HB&T. The HB&T has treated the TexMex as a valued customer and has even rooted for the "small guy" like TexMex.

Under HB&T as it exists today, if there was a problem in the manner that the TexMex was handled while operating on the HB&T trackage or with customer access, the TexMex could go to the HB&T Board of Directors (comprised of two representatives each of the BNSF

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[1] The STB granted trackage rights to Tex Mex in Houston over: (1) the HB&T line from the Quitman Street connection with SP to the Gulf Coast Junction connection with UP and (2) the HB&T line from its connection with SP at T&NO Junction (Tower 81) to its connection with UP at Settegast Junction. TexMex was also granted the right to use the following yards and other terminal facilities: (1) SP's Glidden Yard; (2) interchanges with PTRA at the North Yard, Manchester Yard, and Pasadena Yard; and (3) interchanges with HB&T at HB&T's New South Yard.

and UP) and attempt to leverage at least one other carrier for assistance and representation. If the HB&T is dissolved, any such dispute could easily fall on deaf ears in either Omaha or Ft. Worth. This will only further inhibit the TexMex's ability to provide reasonable transportation services to the rail customers of Houston as it is permitted under its trackage and access rights granted as part of the UP/SP merger.

The plan to split up the HB&T by the UP and BNSF is illustrated in the attached color map. The general dividing line is the GH&H Railroad (in gold). The customers are identified and divided with the UP's being in the color blue and the BNSF in the color green. The UP will acquire dispatching control over the entire area.

The UP, to my knowledge, has not provided any information as to any public benefit that their plan to dissolve the HB&T would add to their recovery plan. To the contrary, the UP's yards (Englewood and Settegast) are not as fluid as the UP has testified before the STB. Both rail yards are still holding trains outside of Houston due to congestion and derailment problems. If UP and BNSF are allowed to continue and dissolve the HB&T, this will further add to the congestion and confusion currently experienced on the Union Pacific system.

**VERIFICATION**

I, Patrick L. Watts, being first duly sworn, upon my oath state that I have read the forgoing verified statement and the contents thereof are true as stated.

Patrick L. Watts

Subscribed and sworn to before me this 30th day of October, 1997.

LUPITA A. LLANES
Notary Public, State of Texas
My Commission Expires 8-04-00

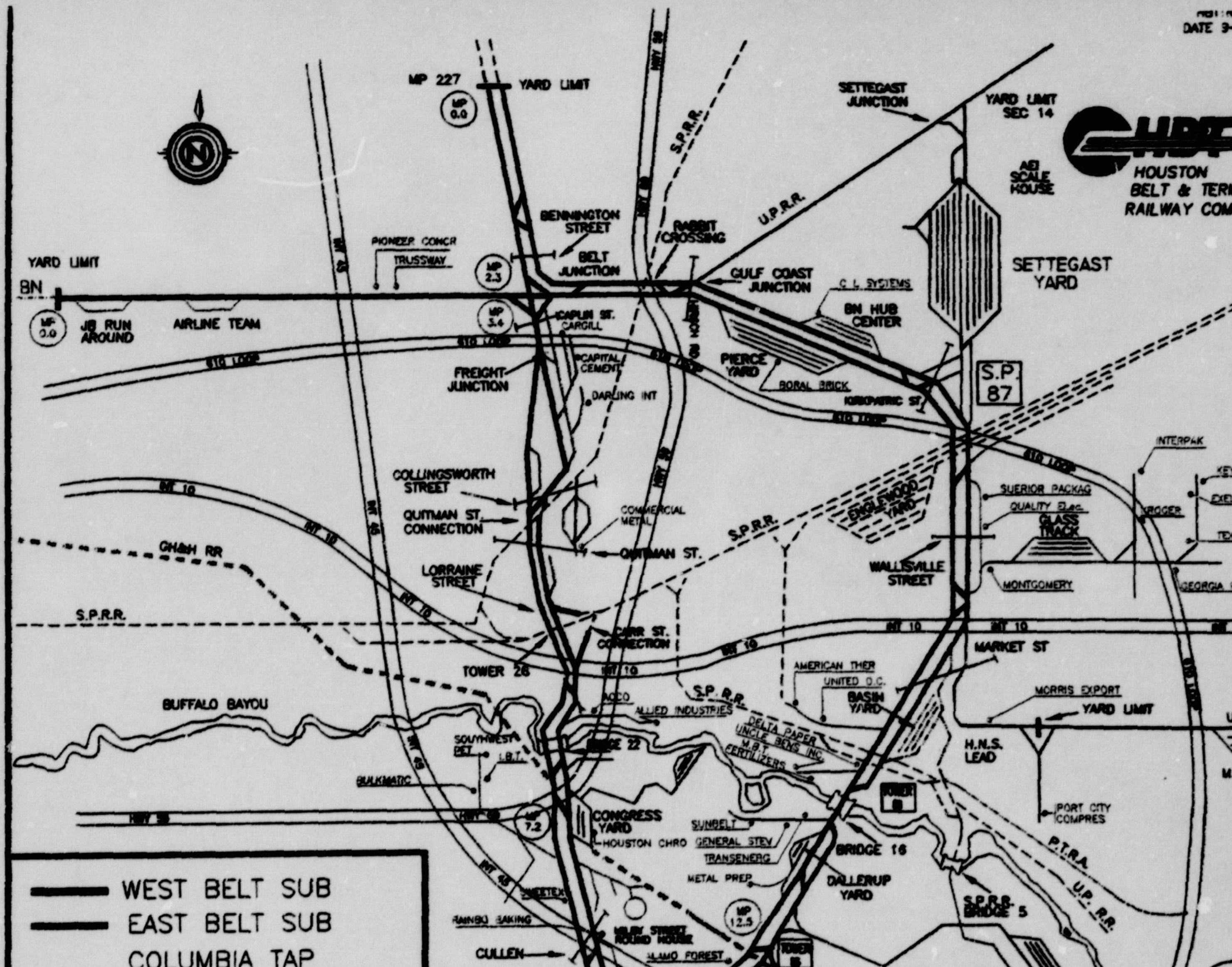
Notary Public

My Commission Expires:

CERTIFICATE OF SERVICE

I hereby certify that a true copy of the Petition for Emergency Cease and Desist Order and Complaint" was served this 30th day of October, 1997, by hand delivery to Counsel for each Respondent and by first class mail to offices of each Respondent.

Sandra L. Brown
Attorney for Kansas City Southern
Railway Company


DATE 9-
HOUSTON BELT & TERM RAILWAY COM
MP 227 YARD LIMIT
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SETTEGAST JUNCTION
YARD LIMIT SEC 14
AEI SCALE HOUSE
U.P.R.R.
S.P.R.R.
BENNINGTON STREET
RABBIT CROSSING
BELT JUNCTION
PIONEER CONCR
TRUSSWAY
YARD LIMIT
BN
MP 0.0
JB RUN AROUND
AIRLINE TEAM
MP 2.3
GULF COAST JUNCTION
C.L. SYSTEMS
SETTEGAST YARD
BN HUB CENTER
MP 3.4
CAPLIN ST.
CARGILL
CAPITAL CEMENT
610 LOOP
FREIGHT JUNCTION
PIERCE YARD
BORAL BRICK
KIRKPATRIC ST.
S.P. 87
DARLING INT
INTERPAK
COLLINGSWORTH STREET
QUITMAN ST. CONNECTION
COMMERCIAL METAL
QUITMAN ST.
ENGLEWOOD YARD
SUERIOR PACKAG
QUALITY ELec.
GLASS TRACK
KROGER
GH&H RR
LORRAINE STREET
WALLISVILLE STREET
MONTGOMERY
S.P.R.R.
IHT 10
CARR ST. CONNECTION
TOWER 26
MARKET ST
AMERICAN THER
UNITED O.C.
BASIN YARD
MORRIS EXPORT
YARD LIMIT
BUFFALO BAYOU
ALLIED INDUSTRIES
DELTA PAPER
UNCLE BENS INC.
M.B.T.
FERTILIZERS
SOUTHWEST PET
BRIDGE 22
H.N.S. LEAD
BULKMATIC
TOWER
PORT CITY COMPRES
CONGRESS YARD
MP 7.2
SUNBELT
GENERAL STEV
TRANSENERG
HOUSTON CHRO
BRIDGE 16
P.T.R.A.
METAL PREP
DALLERUP YARD
U.P. R.R.
S.P.R.R. BRIDGE 5
MP 12.5
RAINBO BAKING
CULLEN
ALAMO FOREST
TOWER
AMERICAN WAITE
GENERAL STEVE
JAMES BAKER CO.
ACTION-WHES
GH&H RR
BOOTH YARD
HARRISBURG JUNCTION
OLD SOUTH YARD
EAST BELT YARD
EAGLEBROOK
DOUBLE TRACK JUNCTION
MP 14.3
PRIME SOURCE
SEATTLE BOX
INTERPAK
SCHLUMBERGER
PRODUCE TERMINAL SEC 1-D
NEW SOUTH YARD
P.T.R.A.
MANCHESTER YARD
WEST BELT SUB
EAST BELT SUB
COLUMBIA TAP
GH&H RR
U.P.RR INDUSTRIES
BNSF.RR INDUSTRIES
MILE POST
NABISCO
GROCERY SUPPLY
YARD LIMIT
S.P.R.R.
U.P.R.R.
TOWER 81
MP 11.1
LABBCO
12.620'
610 LOOP
TEAM TRACK
NTERCOSTAL FRG.
DIXIE PIPE
COLUMBIA TAP
PIERCE JUNCTION
HOUSTON TEXAS
HARRIS COUNT

BEFORE THE
SURFACE TRANSPORTATION BOARD

---

IN THE MATTER OF UNION PACIFIC CORPORATION, UNION PACIFIC RAILROAD COMPANY, MISSOURI PACIFIC RAILROAD COMPANY, SOUTHERN PACIFIC RAIL CORPORATION, SOUTHERN PACIFIC TRANSPORTATION COMPANY AND ST. LOUIS SOUTHWESTERN RAILWAY

---

STB EX PARTE NO. 573

RAIL SERVICE IN THE WESTERN UNITED STATES

and

STB SERVICE ORDER NO. 1518

JOINT PETITION FOR SERVICE ORDER

---

SUPPLEMENTAL PETITION
OF THE
RAILROAD COMMISSION OF TEXAS

COMES NOW, The Railroad Commission of Texas (the "Railroad Commission") and files this its Supplemental Petition before the Surface Transportation Board (the "STB" or the "Board") and hereby petitions the STB for both emergency and permanent relief.

For emergency relief, the Railroad Commission requests the STB to broaden its current emergency measures by mandating an expansion of neutral switching in the Houston terminal area and establishing a through route to be controlled by the Texas Mexican Railway (the "TexMex") through Houston and on to Beaumont.

For permanent relief, the Railroad Commission requests the STB to require divestiture of Union Pacific Railroad ("UP") trackage necessary to implement the expanded neutral switching and the TexMex through route on a long-term basis.

Specifically, the Railroad Commission urges the STB,, pursuant to its authority under 49 U.S.C. §11123 and 49 U.S.C. §11327, to grant the following relief:

<u>Emergency Relief:</u>

(1) Continuation of conditions (1) through (4) as ordered in STB Service Order No. 1518 for an additional two-hundred forty (240) days;

(2) Emergency requirement for the joint and common use of expanded neutral switching services in the Houston terminal area;

(3) Emergency prescription of a through route ("clear path") for the TexMex through Houston;

(4) Emergency direction of the handling, routing, and movement of traffic over the former Missouri Pacific ("MP") line from Houston-Beaumont for the benefit of TexMex; and

(5) Emergency release of shippers (who are able and who choose to utilize any or all of the emergency measures to arrange for alternative shipping) from any existing contractual obligations to the UP which would preclude use of such emergency measures.

<u>Permanent Relief:</u>

(1) Divestiture of specific UP trackage to an expanded shared-asset switching facility in Houston;

(2) Divestiture of the clear path through Houston to the TexMex; and

(3) Divestiture of the former MP Houston-Beaumont line to TexMex.

(4) Grant of such additional relief as may be appropriate.

## I.

## THE RAILROAD COMMISSION'S INTEREST

On October 27, 1997, the Railroad Commission appeared before the STB at its public hearing in STB Ex Parte No. 573, **Rail Service in the Western United States.**

On November 18, 1997, the Railroad Commission filed a Petition to Intervene and To Be Heard at the December 3, 1997 Public Hearing in STB Service Order No. 1518, **Joint Petition for Service Order,** which request was granted by the STB in a Decision dated November 20, 1997.

In Texas, the Railroad Commission has conducted a series of public hearings on the current condition of rail service and safety as follows:

| | |
|---|---|
| September 16, 1997 | Austin, Texas |
| October 3, 1997 | Houston, Texas |
| October 17, 1997 | Fort Worth, Texas |
| October 31, 1997 | San Antonio, Texas |
| November 14, 1997 | El Paso, Texas |

At these public hearings, the Railroad Commission received testimony and comments from a diverse statewide cross-section of shippers, local governmental authorities, economists, railroad employees, unions, and railroad executives, as well as individual concerned citizens of the State of Texas. Through this Supplemental Petition, the Railroad Commission represents the voices of these shippers, governments, employees, unions, and citizens so that they are heard at the federal level.

The Railroad Commission's plan to alleviate the rail service crisis in Texas (the "Commission's Plan"), adopted in public session on November 21, 1997 and submitted to the STB herein, presents the voices of those constituencies.

## II.

## STATEMENT OF THE CASE

### A. BACKGROUND

The Railroad Commission requests that the STB initiate immediate efforts to implement both the emergency and the divestiture relief requested above in order to ensure that the current rail crisis in the Western United States will not only be alleviated but never repeated.

STB Emergency Service Order No. 1518, Joint Petition for Service Order ("Service Order"), recognized that a transportation emergency exists in the West and that the severe congestion in the Houston area and the operations of UP and the Southern Pacific Transportation Corporation ("SP") were specific concerns. Addressing these issues, the Service Order directed the implementation of certain short-term measures. Although the short-term solutions identified in the Service Order are unquestionably important and valuable steps, the Railroad Commission submits that efforts must be undertaken to address and resolve the fundamental problem underlying and driving what has been called a "debacle", "meltdown", "gridlock" and "the most serious rail crisis of the 20th century." Otherwise, the current emergency situation will be unnecessarily prolonged and destined to be repeated.

The Railroad Commission supports the extension of the emergency measures mandated in the Service Order but also believes that the scope of the emergency measures must be expanded to address the fundamental problem underlying the current crisis. Despite notable efforts to resolve UP's service problems, the overwhelming comments and evidence received by the Railroad Commission indicate that, at best, only marginal improvement in UP's service has occurred and that serious problems remain. UP has not realized any significant success in improving its rail delivery service because there has not been an adequate focus on, or effort to resolve, the problem that created, perpetuates, and will inevitably lead to a repeat of the current crisis.

Unless the Board undertakes to redress, both on an emergency and permanent basis, UP's virtual monopolization of the complex Houston rail infrastructure and its domination of the petrochemical and plastics industries in the Houston/Gulf Coast area, business in Texas and in the Western United States will continue to suffer significant financial loss.

When one company controls the business, as UP does in the case of chemical rail transportation in the Gulf Coast area, or has upwards of 80% of the business, as is the case of UP's plastic domination, there is little doubt of monopolization of that segment of the industry. This amount of domination is precisely what is reflected in filings with the STB by the Chemical Manufacturer's Association and the Society of the Plastics Industry at the time of the merger, and it is the choice piece of business from which UP's service problems emanated. The lack of any viable railroad transportation alternative led to this crisis.

**B. RELIEF REQUESTED**

In an effort to alleviate the current crisis and provide substantial protection against its recurrence, the Railroad Commission requests that the STB implement, on an emergency and permanent basis, three adjustments to rail operations in and around the Houston, Texas terminal area: (1) the expansions of a Port Terminal railroad to operate as a shared-asset facility to provide switching services in the Houston terminal area; (2) the establishment of a clear path through the Houston terminal area for the TexMex; and (3) the transfer of the former MP track from Houston to Beaumont to TexMex. These adjustments will provide shippers with critically-needed multiple line-haul options and create greater operating efficiencies.

The Railroad Commission acknowledges that the STB's authority to implement the requested permanent relief by ordering the divestiture of UP rail facilities may be limited in this proceeding. The STB has clear authority, however, under the provisions of 49 U.S.C. § 11123, inter alia, to "(1) direct the handling, routing and movement of traffic . . .' (2) require joint and common use of railroad facilities; (3) prescribe temporary through routes; . . ." As described in more detail below, the STB is therefore clearly authorized to direct the implementation of the Railroad Commission's proposed adjustments on an emergency basis.

We submit that the immediate implementation of the emergency relief requested above, and ultimately the divestiture of the identified UP facilities, will not only materially relieve the current emergency but also provide substantial protection against a repeat of the crisis.

## III.

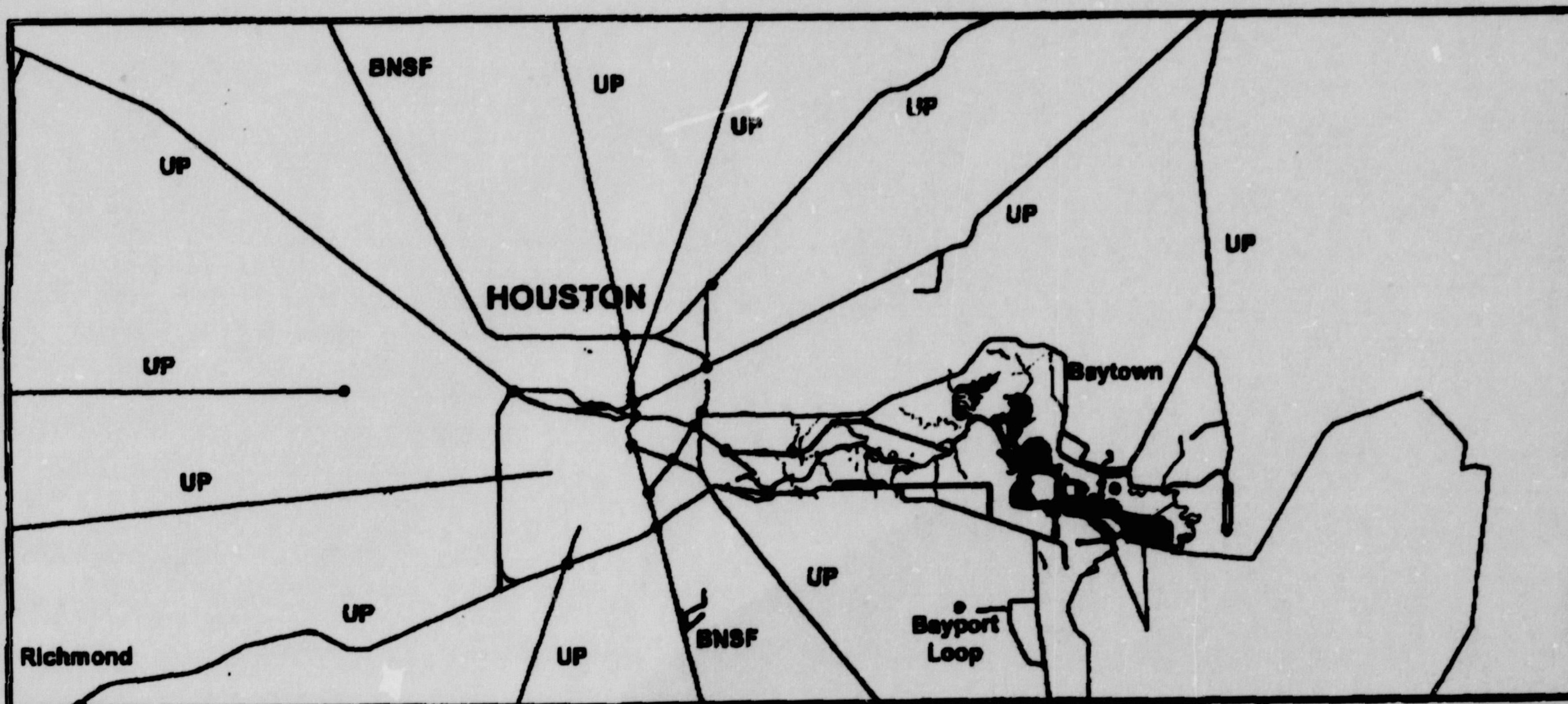
## UP HAS A VIRTUAL MONOPOLY ON THE RAIL INFRASTRUCTURE IN THE HOUSTON/GULF COAST AREA

### A. MANIFESTATION OF MONOPOLY CONDITIONS

The Railroad Commission is convinced that the UP service crisis is primarily attributable to UP's monopolization of the complex Houston rail network and its domination of the petrochemical and plastics industries in the Houston/Gulf Coast area. These monopoly conditions are manifested by the current crisis conditions due to the virtual absence of shipping alternatives for UP's captive shippers.

The attached map of the greater Houston area clearly depicts UP's monopolization of the Houston rail network. (See Map No. 1 on the next page). As is obvious from the UP lines in red and the BNSF lines in green, UP controls the entire rail infrastructure in Houston. UP has nine principal lines radiating

# CURRENT RAILROAD CONTROL
# HOUSTON, TEXAS




MAP NO. 1

**Rail Line Legend**

- = Union Pacific
- = Burlington Northern Santa Fe
- = Port of Houston Authority

December 1997

from Houston, while BNSF has only two. BNSF's lines run south to Galveston and north to Fort Worth, while UP's principal lines extend in all directions:

- Houston to Baytown (UP)
- Houston to Beaumont (SP)
- Houston to Beaumont (UP)
- Houston to Shreveport (SP)
- Houston to Dallas (SP)
- Houston to Fort Worth (UP)
- Houston to San Antonio (SP)
- Houston to Galveston (UP)
- Houston to Galveston (SP)

But the nine to two ratio between UP and BNSF does not tell the entire story because the two BNSF lines ***are not now directly connected***. From New South Yard and Pasadena Yard, BNSF has to operate over former Houston Belt & Terminal ("HB&T") lines, which are dispatched by UP. The only way that BNSF can avoid having to run over UP controlled trackage is to take the old Santa Fe route south to Alvin and then north to Temple, a circuitous route that makes BNSF even less competitive.

The result of UP's monopolization of the Houston rail network is that there are no alternative pathways through Houston for the TexMex. And because there are no alternative pathways, TexMex is caught in the congestive morass that is crippling UP, making it impossible for them to provide a satisfactory level of service.

There is no way to alleviate the UP service crisis except to create alternative pathways through Houston and between Houston and Beaumont that will permit TexMex to offer a level of service that will divert a sufficient volume of traffic from UP to allow it to recover from the crisis. If such pathways are created and captive shippers located on UP/SP trackage are allowed a choice of line-haul carrier, conditions will return to normal in the Houston/Gulf Coast area, making it possible for UP to shift locomotives, manpower, and other resources to the Central Corridor and other UP operating regions, allowing it to clear up the congestion there.

## B. CONSEQUENCES FOR SHIPPERS AND THE TEXAS ECONOMY

UP's control of the entire rail infrastructure in Houston and the resulting lack of alternative pathways through Houston for TexMex has had, and continues to have, devastating consequences for Texas shippers. The Center for Economic Development and Research of the University of North Texas conservatively estimates that the cost to date for Texas businesses, measured by lost sales, reduced output and higher shipping charges, is $762 million and that businesses, consumers and taxpayers in Texas will incur $623 million in additional costs in the next few months unless the services problems are quickly resolved. It is critical to Texas that this rail crisis end quickly. A copy of the November 24, 1997 study prepared by Bernard L. Weinstein, Ph.D. and Terry L. Clower, Ph.D. entitled *"The Impacts of the Union Pacific Service Disruptions on the Texas Economy: An Interim Report"* is attached hereto as Exhibit "A" and is incorporated herein for all purposes.

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Unfortunately, there is little, if any, evidence that efforts undertaken to date have produced or will produce any significant improvement in rail service in Texas.

The Railroad Commission has conducted several public hearings across the state in an effort to meaningfully assess the current condition of rail service and safety in Texas. The overwhelming weight of the comments received at these hearings from a diverse cross-section of shippers, local governments, economists, railroad employees, unions, and railroad executives indicate that the rail service and safety emergency that has existed for several months continues in Texas without any significant abatement. As evidence of the source of continuing problems, recent reports from both TexMex and BNSF indicate that during the week of November 16-22, it took nearly 24 hours for TexMex and BNSF trains to traverse the Houston area on UP controlled trackage, instead of the two to three hours historically required. BNSF is apparently being forced to use its circuitous route south to Alvin and north to Temple for most of its trains, adding nearly a hundred extra miles for much of its traffic. The TexMex, however, has no alternative route.

The Railroad Commission has contacted, at the time of filing this Supplemental Petition, a number of shippers and shipper groups to ascertain the current state of rail service on UP in Texas. A few shippers report minor improvements, but the overwhelming majority claim either that things have not improved or that they have actually grown worse. An analysis of UP's weekly performance report to the STB indicates only marginal improvements in recent weeks in certain categories and deterioration in other categories.

As long as UP is allowed to maintain its monopoly of the Houston rail network, the Railroad Commission submits that shippers will not soon experience any appreciable relief from the current crisis and will almost certainly be subjected again to these emergency conditions.

## IV.

## THE RAILROAD COMMISSION'S PROPOSAL FOR ALLEVIATING THE UP SERVICE CRISIS

On November 21, 1997, the Railroad Commission approved and adopted a Plan for Alleviating the Union Pacific Service Crisis, which it now proposes to the STB as an appropriate means of resolving the current crisis and for remedying, on a permanent basis, rail service in the Houston/Gulf Coast area.

The Commission's Plan suggests three adjustments to rail operations in and around the Houston, Texas terminal area which will improve greatly the flow of rail transportation to, through, and out of the Houston, Texas area. The Railroad Commission believes that the implementation of these three adjustments will not only materially relieve the current rail service emergency but also will provide substantial protection against a repeat of the current rail service crisis.

First, the Commission Plan recommends the expansion of a Port Terminal Railroad to operate as a shared-asset facility to provide neutral switching services in the Houston terminal area. Second, the Commission Plan recommends the establishment of a clear path through the Houston terminal area for the TexMex. Third, the Commission Plan recommends the transfer of the former Missouri Pacific track from Houston to Beaumont to the TexMex.

The Railroad Commission requests that the STB implement all three of these recommendations from the Commission's Plan immediately.

## A. AN EXPANDED PORT TERMINAL RAILROAD

The first important step to alleviating the UP service crisis is the transfer of certain of UP's port area industrial trackage to an expanded switching facility, herein called the new Port Terminal Railroad ("PTR"), that would provide neutral switching to port area industries.

The new PTR could be publicly owned and privately operated, privately owned and publicly operated, or privately owned and privately operated. Under the private ownership alternative, it could be owned by the railroads serving Houston, by investors, or by shippers located on the trackage which it operates.

The PTR would acquire trackage on both sides of the Houston Ship Channel and also the Houston Belt and Terminal's East Belt Line. Transfer of the UP trackage to PTR would allow the PTR to provide neutral switching services to large numbers of captive shippers who have been seriously harmed over the past six months because they have not had an alternative to UP's service.

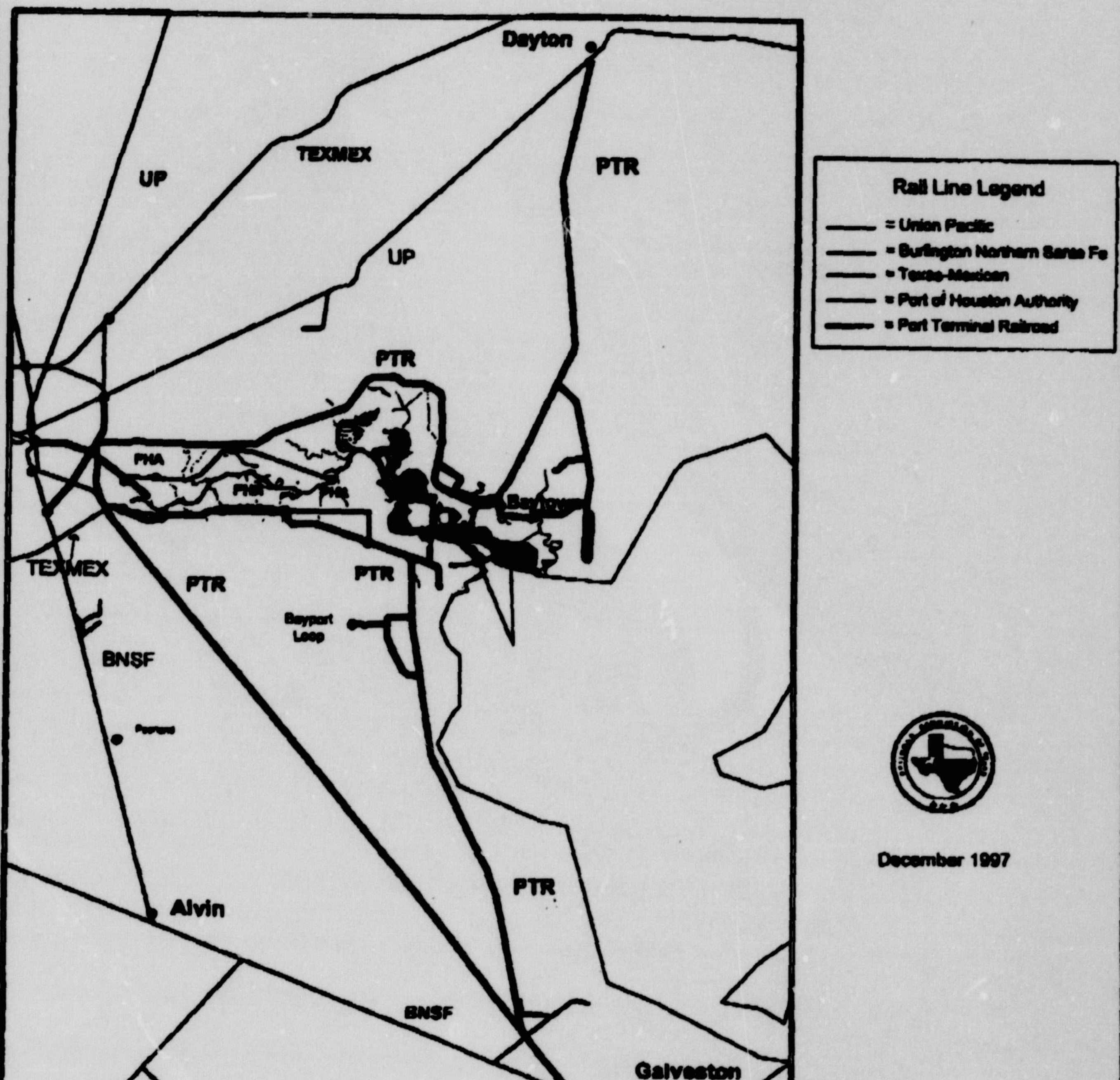
Under the Commission Plan, the UP trackage to be transferred to the PTR is shown on Map No. 2 (see Map No 2 on next page) and includes track segments as follows: UP line from Houston to Baytown; SP line from Baytown to Dayton; SP line from Englewood Yard to Galveston; UP line from Katy Neck to Galveston; and the Clinton Drive Industrial Lead. Additionally, the HB&T trackage from Double Track Junction to Englewood Yard (the "East Belt") would be transferred to PTR, including East Belt Yard, Dallerup Yard, Basin Yard, and Glass Yard, plus industrial leads.

To accomplish the expansion of neutral switching facilities in Houston, the Railroad Commission urges the STB to mandate divestiture of UP's trackage depicted on Map No. 2 to facilitate its transfer to the PTR.

Thus, UP trackage and the HB&T's East Belt would be integrated with the existing port area trackage that is owned by the Port of Houston Authority and operated by the present Port Terminal Railroad Association (the "PTRA") to create a comprehensive network of rail lines, lead tracks, and yards serving the booming industrial area extending from Dayton to Baytown to Galveston, including both sides of the Houston Ship Channel.

Basis for this element of the Railroad Commission's Proposal. The Commission's Plan for expanded neutral switching in the Houston/Gulf Coast area builds on the success of the existing PTRA operation, which has provided excellent service at competitive rates to large numbers of shippers. In fact, the well managed PTRA operation has been so successful that the existing PTRA

# HOUSTON TERMINAL AREA SHOWING PROPOSED EXPANSION OF PORT TERMINAL RAILROAD




**Existing Port Trackage shown in black**
**New Port Trackage shown in blue**

MAP NO. 2

organization could be basis for an expanded Port Terminal Railroad.

Divestiture of UP port area trackage to an expanded Port Terminal Railroad will allow captive shippers to have access to TexMex and BNSF, as well as UP. The ability of shippers to choose between line-haul carriers will ensure that serious future operating problems on any one carrier, such as those experienced by UP for the past six months, will not have significant, long-term impacts on the ability of shippers to receive inbound raw materials and distribute finished products. As soon as a shipper realizes he is being hurt by a particular carrier's inability to perform, he will simply divert his shipments to a competing carrier.

In addition to providing shippers with multiple line haul options, an expanded Port Terminal Railroad will be able to create greater operating efficiencies by handling a much larger volume of traffic through coordinated specialized terminal facilities. For example, the UP Strang Yard could be used by the expanded PTR for making up outbound trains, while PTRA's Pasadena Yard could be used for receiving and classifying inbound trains.

The expansion of neutral switching to industries located near the Port of Houston will benefit all shippers because it will provide them the access to BNSF, a Class I railroad with a comprehensive network that spans the Western two-thirds of the United States. More importantly, the only way to ensure that the present service crisis is never repeated is to give shippers access to a third railroad with its own trackage that has connections with the major railroads east of the Mississippi River. The

Commission's Plan assumes this third carrier will be TexMex, along with its affiliate, KCS.

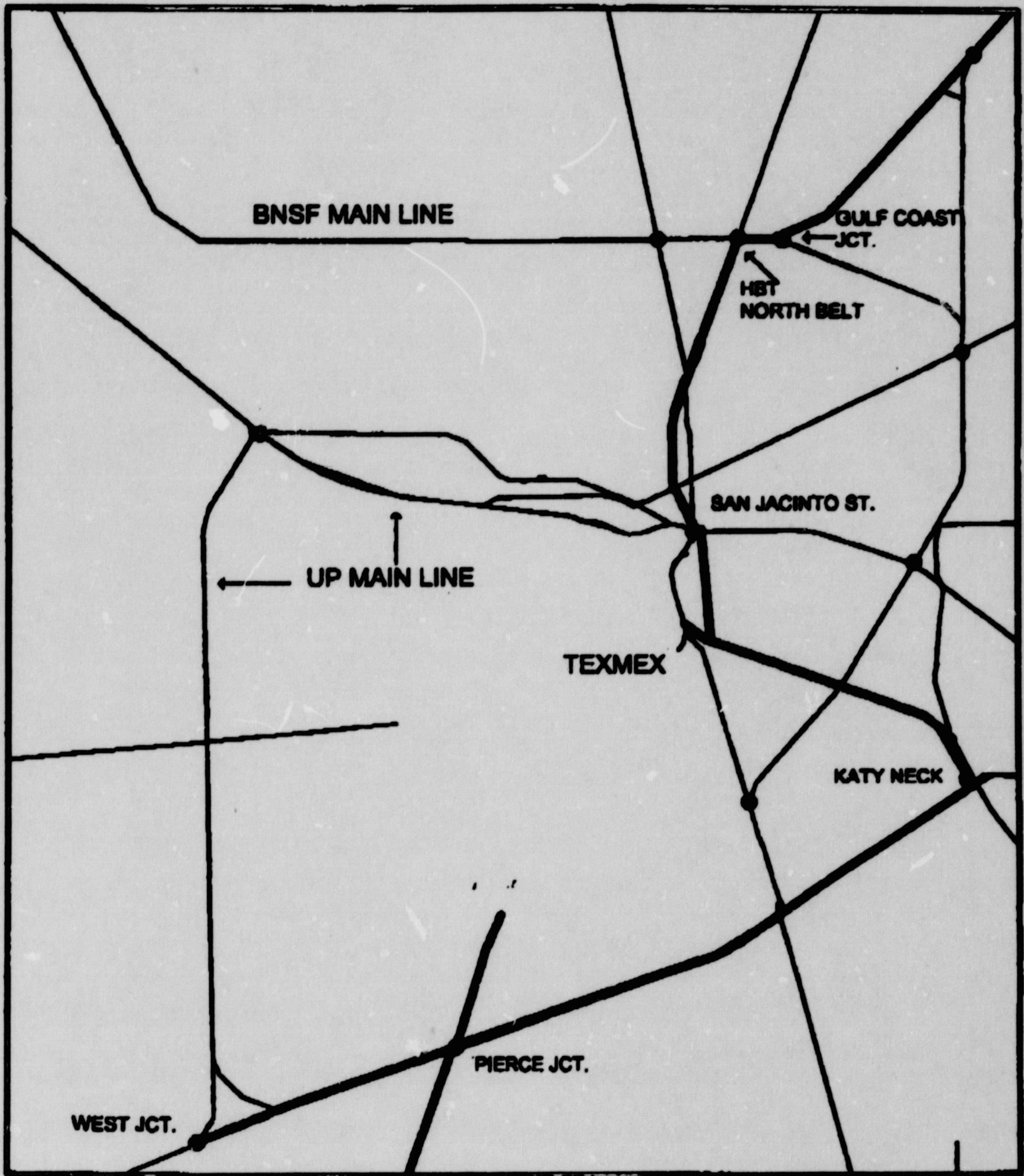
## B. A CLEAR PATH THROUGH HOUSTON FOR THE TEX MEX

The second important step to alleviating the UP service crisis is to provide a clear path through the complex and congested Houston rail network for the TexMex.

It is contrary to the public interest for UP to control all of the urban trackage in the greater Houston area because it is the UP's dominance of the rail infrastructure in Houston that has been the predominant cause of the near paralysis of rail operations in the Houston/Gulf Coast area over the past six months. By giving the TexMex its own route through Houston and allowing BNSF to use that route for trains operating between Houston and New Orleans, it is unlikely there will ever again be a situation where train operations in the Houston area become congested to the point of near immobility.

The clear path through the Houston terminal area that is proposed in the Commission Plan is depicted on Map No. 3 and includes segments of UP trackage as follows: Pierce Junction to Katy Neck; Katy Neck to San Jacinto Street; San Jacinto Street to HB&T North Belt; and HB&T North Belt to Gulf Coast Junction. These four segments of UP trackage would be acquired by TexMex and connections would be made between them so that they together constitute an integrated route through Houston. (See Map No.3 on next page).

# CLEAR PATH THRU HOUSTON
# FOR TEXMEX




Rail Line Legend

- = Union Pacific
- = Burlington Northern Santa Fe
- = Port Terminal Railroad
- = Texas-Mexican

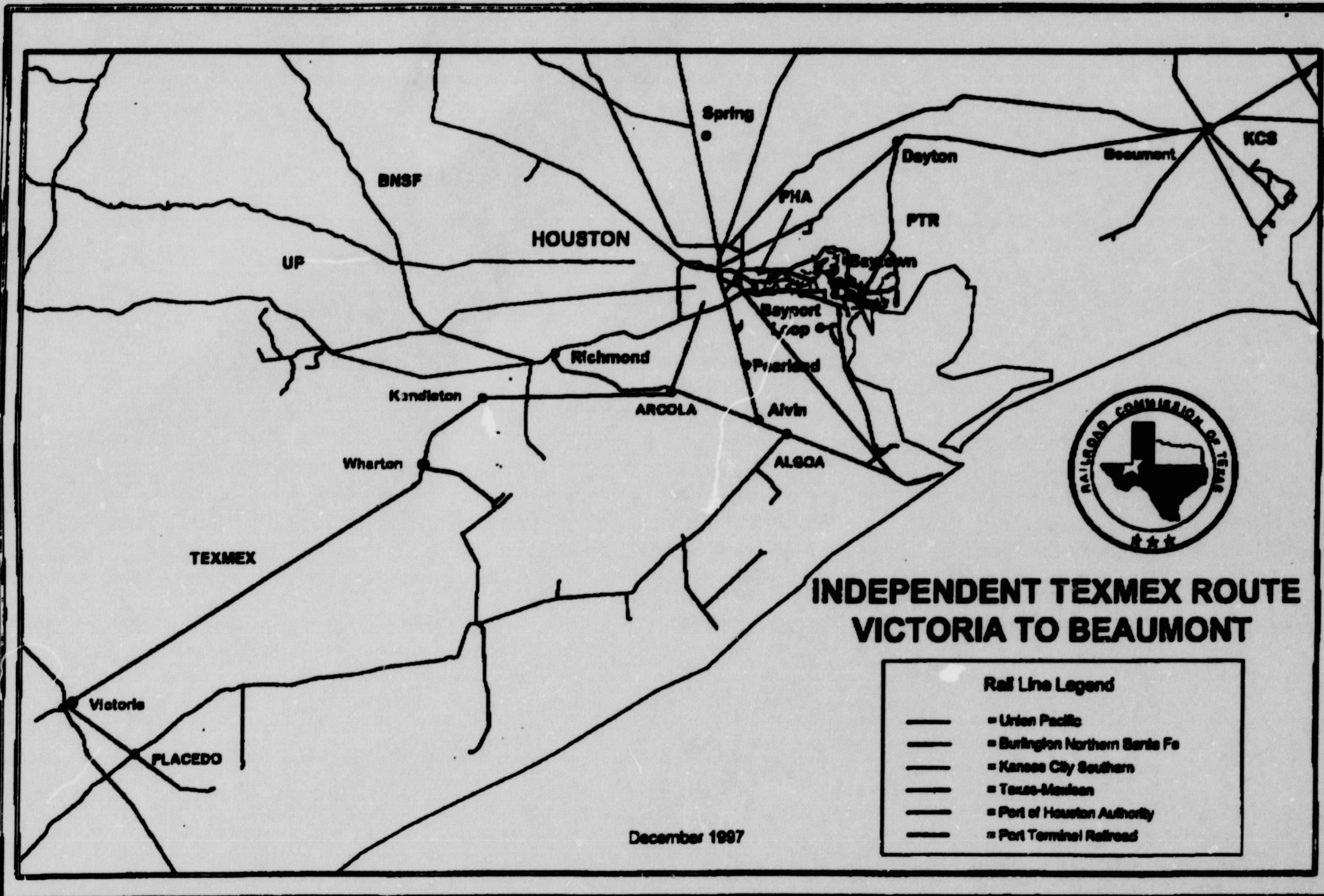
December 1997

MAP NO. 3

To accomplish the establishment of a clear path through Houston for the TexMex, the Railroad Commission urges the STB to mandate divestiture of UP's trackage depicted on Map No. 3 to facilitate its transfer to TexMex.

In addition to clearing a path through Houston as described above, any long-term route planning for the TexMex may well include a different route from Victoria to Houston. The new Victoria-Houston route for TexMex might include reconstruction of the abandoned SP line from Victoria to Wharton, acquisition of the unused SP line from Wharton to Kendleton, and construction of a new line from Kendleton to Thompsons, where a connection would be made to the Houston Lighting and Power line that extends from Thompsons to Arcola. The Victoria-Houston line is depicted on Map No. 4. (See Map No. 4 on next page). By adding UP's Arcola to Pierce Junction line segment, this new Victoria-Houston line could link up with the clear path through Houston proposed above. Pending the completion of such a Victoria-Houston line, TexMex must rely on trackage rights over UP from Placedo to Algoa and over BNSF from Algoa to Houston.

**Basis for the "clear path" element of the Railroad Commission's proposal.** The Railroad Commission's proposal to create a clear path for TexMex through Houston should have minimal negative impacts on UP's operations because the line segments that would comprise the TexMex clear path appear to be of marginal value to UP. To the extent that UP has a need to operate over those line segments, UP could have trackage rights.


INDEPENDENT TEXMEX ROUTE
VICTORIA TO BEAUMONT
Rail Line Legend
= Union Pacific
= Burlington Northern Santa Fe
= Kansas City Southern
= Texas-Mexican
= Port of Houston Authority
= Port Terminal Railroad
December 1997
RAILROAD COMMISSION OF TEXAS
Spring
BNSF
HOUSTON
UP
PHA
Dayton
PTR
Beaumont
KCS
Baytown
Bayport
Loop
Richmond
Pearland
ARCOLA
Alvin
ALGOA
Wharton
TEXMEX
Victoria
PLACEDO

MAP NO

The clear path through Houston will prevent TexMex's trains from being caught up in the terrible congestion that is plaguing both UP and BNSF. By giving TexMex its own trackage in Houston, there will no longer be the now common twenty-four delays that have severely impacted TexMex's ability to provide satisfactory service, while causing its operating costs to exceed its revenues. Instead, trains will move through the Houston area in two to three hours, with the same crew that got on at the origin terminal.

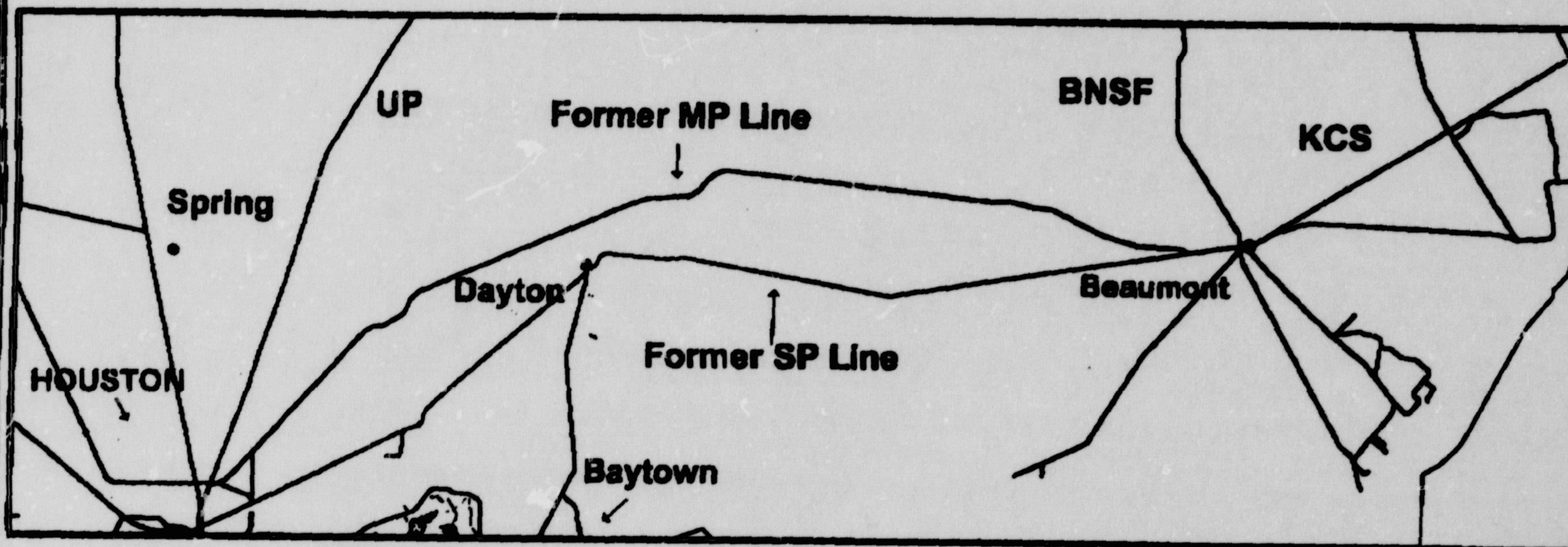
By giving TexMex a larger role in the Houston market, and allowing it to operate autonomously, completely apart from UP and BNSF, shippers will have an insurance policy against the failure of the two interdependent industry giants to perform at levels that are acceptable and necessary for Houston/Gulf Coast area companies that are primarily dependent on rail transportation.

## C. TRANSFER OF THE FORMER MP HOUSTON-BEAUMONT LINE TO TEXMEX

A third important step to alleviating the UP service crisis is to transfer the former Missouri Pacific ("MP") Houston-Beaumont line to TexMex.

As shown on <u>Map No. 5</u>, UP currently controls two lines from Houston to Beaumont: the former SP line through Dayton; and the former MP line through Sour Lake. (See <u>Map No. 5</u> on next page). For six months, TexMex trains have experienced great delays operating over its trackage rights on UP's two lines between Houston and Beaumont. The delays have substantially increased operating costs for TexMex, while significantly delaying shipments. Further, the

# HOUSTON - BEAUMONT LINES




December 1997

**Rail Line Legend**

- = Union Pacific
- = Burlington Northern Santa Fe
- = Kansas City Southern
- = Texas-Mexican

MAP No. 5

delays have prevented TexMex from providing shippers with alternatives to UP's service.

The Commission Plan visualizes that the former MP line be transferred to TexMex so that TexMex could have a controlled route from Victoria to Beaumont (see Map No. 4 infra). It recommends that TexMex be put in a position where it is no longer at the mercy of UP and that shippers be given additional routing options when UP cannot satisfactorily perform. Under the Commission's Plan, TexMex could acquire the MP Houston-Beaumont line and would immediately grant trackage rights to BNSF over the line for the entire distance between Houston and Beaumont, giving BNSF an alternate route. Critically, to ensure BNSF of prompt, efficient, and fair handling of BNSF trains, TexMex would dispatch the MP Houston-Beaumont line from a centralized traffic control office in Houston.

To ensure UP that it has sufficient capacity in the Houston-Beaumont-Lake Charles-New Orleans corridor after the transfer of the MP line to TexMex, UP would also be given trackage rights over the line. Those trackage rights would complement UP's existing trackage rights over Kansas City Southern ("KCS") between DeQuincy, Louisiana and Beaumont. The UP has satisfactorily utilized the DeQuincy-Beaumont line segment since it acquired Missouri Pacific fifteen years ago; therefore, the proposal that UP have trackage rights over the MP Houston-Beaumont line segment should not present a problem in terms of efficient train handling. Since there is no on-line industry of any substance on the MP line, the transfer of the line to a different railroad should have no direct adverse commercial implications for UP. Nevertheless, UP would be given access to any future industries located on the line.

To accomplish the transfer of the MP Houston-Beaumont Line, the Railroad Commission urges the STB to mandate divestiture of UP's ownership of the MP Houston-Beaumont line to facilitate its transfer to TexMex.

Proceeds from the transfer of the MP line could be used by UP to double track its remaining SP line from Houston to Beaumont; however, if UP elects to retain trackage rights over the MP line, UP may wish to do no more than build additional passing sidings at strategic locations on the line.

Basis for this element of the Railroad Commission's Proposal. The Commission Plan to transfer the MP Houston-Beaumont line should have no negative operational impacts on the UP, but it will have very positive operational impacts on the performance of the TexMex and its affiliate, KCS, allowing them to provide shippers with an efficient alternative for moving north and east from the Houston/Gulf Coast area.

Once TexMex has control of its own route between Beaumont and Houston, trains will be dispatched promptly and moved expeditiously. Passing sidings will be used for their intended purposes rather than for storing trains that cannot be accommodated in Houston/Gulf Coast area yards because of congestion (as has been the case with UP over the past six months).

The combination of a clear path through Houston and an independently owned and operated line from Houston to Beaumont will allow TexMex to serve as an "escape route" for Houston/Gulf Coast area shippers that are receiving unacceptable service from UP and BNSF.

## V.

## SPECIFIC RELIEF REQUESTED

### A. CONTINUING STB SERVICE ORDER NO. 1518

On October 31, 1997, the STB, acting pursuant to authority granted in 49 U.S.C. § 11123, determined in the Service Order that a transportation emergency existed in the Western United States and ordered certain temporary emergency measures in an attempt to resolve the emergency.

On November 21, 1997, the Railroad Commission, based on the evidence which it had received at its most recent public hearing in El Paso, Texas on November 14, 1997, concluded that the rail service emergency continues in Texas without any significant abatement. To date, the Railroad Commission has not received any convincing indication that either UP's Service Recovery Plan or STB's Service Order has produced demonstrable improvement in Texas.

Therefore, the Railroad Commission submits that, pursuant to the authority granted to it in 49 U.S.C. §11123 (c) (1), the STB should extend the emergency actions mandated on October 31, 1997 for an additional two hundred forty (240) days.

Without any intent to limit the scope of the STB's extension of its emergency provisions, or exercise of its emergency authority, the Railroad Commission specifically requests that certain of the remedial measures adopted on October 31, 1997 be extended for two hundred forty (240) days including:

1. <u>TexMex to Serve Houston Through HBT and PTRA.</u> The Texas Mexican Railway (TexMex) will be authorized to accept traffic routed to it by Houston shippers that are switched by the Houston Belt Terminal Railroad's (HBT) successors and by the Port Terminal Railroad Association (PTRA). UP/SP, which agreed at the oral hearing "to suspend contract obligations . . . where it could be shown that it would benefit the customer and would not add to the problems," shall release from their contracts all shippers capable of being switched by HBT and PTRA at Houston that desire to be served by TexMex. All rates and charges applicable to shipments routed to TexMex under this authority will be those agreed upon between TexMex and the individual shipper.

2. <u>TexMex Trackage Rights.</u> To mitigate congestion over UP/SP's "Sunset Route," TexMex is authorized to utilize trackage rights over the Algoa route south of Houston, between Placedo, TX (Milepost 224.3) and Algoa, TX (Milepost 343.1) (a distance of 118.8 miles), to the extent it chooses to do so. In this connection, we will require BNSF to grant TexMex trackage rights over its portion of the Algoa route between Alvin (Milepost 28.6) and Algoa (milepost 24.4) (Galveston Subdivision) and between Alvin (Milepost 0.0) and T&NO Junction (Milepost 19.4) (Houston Subdivision), a total distance of 23.6 miles.

3. <u>The Caldwell to Flatonia Line.</u> To facilitate rerouting of traffic around Houston, UP/SP is required to remain in effect its temporary grant of trackage rights to BNSF via the Caldwell-Flatonia-Eagle Pass line, and to permit BNSF to interchange Laredo run-through traffic with TexMex at Flatonia if it desires to do so.

4. <u>Track Access.</u> In accordance with the more detailed explanation below (omitted here), UP/SP shall facilitate the existing operations of BNSF and TexMex in the Houston area, and shall maintain open use of mainlines and sidings on the Houston-to-Memphis and the Houston-to-Iowa Junction routes.

## B. EXPANDING STB SERVICE ORDER NO. 1518

On November 21, 1997, the Railroad Commission, based on consideration of the record before it, concluded that the rail service emergency in Texas is unlikely to be resolved without further action of the STB in addition to the initial temporary conditions which the STB imposed on October 31, 1997.

We urge the STB to act to address the fundamental problem underlying the current emergency -- UP's virtual monopolization of the Houston rail infrastructure. The Railroad Commission therefore urges the STB to expand the scope of the emergency measures in its Service Order No. 1518 to include full implementation of the Commission's Plan immediately.

If, and to the extent that, full implementation exceeds the time-line scope of these proceedings, the Railroad Commission reserves the right to reurge the Commission's Plan, as it may be amended from time to time, in such other STB dockets as may be appropriate.

However, the Railroad Commission submits that implementation of all three adjustments recommended in the Commission's Plan can be initiated on an emergency basis within the powers granted to the STB in 49 U.S.C. § 11123 in particular:

> **§ 11123. Situations requiring immediate action to serve the public**
>
> (a) When the Board determines that shortage of equipment, congestion of traffic, unauthorized cessation of operations, or other failure of traffic movement exists which creates an

emergency situation of such magnitude as to have substantial adverse effects on shippers, or on rail service in a region of the United States . . . the Board may . . .

(1) direct the handling, routing, and movement of the traffic of a rail carrier and its distribution over its own or other railroad lines;

(2) require joint or common use of railroad facilities;

(3) prescribe temporary through routes; . . .

The Commission's Plan insofar as it expands STB's Service Order is as follows:

1. **AN EXPANDED PORT TERMINAL RAILROAD.** The STB should immediately mandate that the existing Port Terminal Railroad Association ("PTRA") assume switching operations over the former HB&T's East Belt Line and the SP Galveston line. In addition, the STB should allow PTRA to operate UP's Strang Yard, in conjunction with PTRA's Pasadena Yard, and to designate one yard for all inbound traffic and one yard for all outbound traffic for all shippers located between Manchester Yard and Seabrook, including the Bayport Loop. The imposition of this condition represents merely an incremental expansion of the area of neutral switching currently being handled by the PTRA. The STB can commence the implementation of this measure on an emergency basis under its authority to require joint or common use of railroad facilities. 49 U.S.C. § 11123 (a) (2).

The Railroad Commission respectfully suggests that the STB adopt conditions as follows:

__PTRA to Provide Switching To Shippers on the SP Galveston Line and HB&T East Belt Line__. Port Terminal Railroad Association ("PTRA") is authorized to assume control of the HB&T East Belt Line from Double Track Junction to Englewood Yard (including all industrial leads and connecting secondary trackage) and the SP Galveston Line from Englewood Yard to Seabrook (including the Clinton Drive Industrial Lead, the Bayport Loop, and all industrial leads and connecting secondary trackage). PTRA also shall be allowed to assume control of Strang Yard on the Galveston Line and East Belt Yard, Dallerup Yard, and Basin Yard on the East Belt Line. PTRA shall coordinate those yards with PTRA's yards to achieve maximum switching efficiency. Dispatching and supervision of train operations on the East Belt Line and Galveston Line shall be the responsibility of PTRA.

PTRA shall provide switching services to all customers located on the East Belt Line and the Galveston Line, utilizing its own locomotives and crews. Whatever additional locomotives and crews are needed by PTRA to perform those switching services shall be provided by UP, BNSF, and TexMex, in accordance with previous PTRA practices.

Also, to the extent the STB has the power to do so, it should impose the following related condition:

TexMex shall be admitted to full membership in the PTRA, but shall be required to bear its fair share of the cost of PTRA operations. The Port of Houston Authority also shall be admitted to full membership in the PTRA.

2. **A CLEAR PATH THROUGH HOUSTON FOR THE TEXMEX**. The STB should immediately mandate trackage rights and dispatching control over the designated clear path to TexMex. TexMex can exercise this dispatching control from a control point at Holmes-South Main (West Junction). TexMex can install a centralized traffic control system on this route within thirty days. In the meantime, TexMex should be allowed to place a representative in UP's Harriman Dispatching Center to direct train movements over the clear path.

The imposition of this condition is merely a logical extension of the additional access rights which the STB granted to TexMex in Service Order and those trackage rights conditions initially imposed as a condition to the Union Pacific-Southern Pacific merger for the benefit of TexMex. STB can commence the implementation of this measure on an emergency basis under its authority to prescribe temporary through routes. 49 U.S.C. § 11123 (a) (3).

The Railroad Commission respectfully suggests that the STB adopt conditions as follows:

New TexMex Route Through Houston. To provide a clear path through Houston for TexMex and BNSF trains, TexMex is authorized to assume control of the SP Harrisburg Line from West Jct. to Katy Neck, the UP Houston Subdivision Line from Katy Neck to Congress Avenue Yard (the former GH&H), and the HB&T West Belt Line from Congress Avenue Yard to Belt Jct. Until such time as TexMex can install a CTC system on the route between West Junction and Belt Junction (anticipated to be thirty days), TexMex shall be allowed to place a representative in UP's Harriman Dispatching Center to direct train movements over the route. TexMex is authorized to immediately construct (1) a connection at Katy Neck to link the Harrisburg Line with the GH&H Line and (2) a connection at Tower 81 to link BNSF's Algoa-Houston line with the Harrisburg Line.

BNSF Use of TexMex Controlled Trackage. TexMex shall immediately enter into a dispatching agreement with BNSF for expedited handling of BNSF trains over West Junction to Belt Junction.

3. **TRANSFER OF THE MP HOUSTON-BEAUMONT LINE TO TEXMEX.**

The STB should immediately transfer dispatching control over the MP Houston-Beaumont line to TexMex. Because the TexMex as well as the BNSF currently enjoy trackage rights over this MP Houston-Beaumont line, this implementation of this emergency measure requires merely the transfer of dispatching control over such line. TexMex can install a centralized traffic control system on this route within thirty days. In the meantime, TexMex should be allowed to place a representative in UP's Harriman Dispatching Center to direct train movements between Houston and Beaumont.

The STB can commence the implementation of this measure on an emergency basis under its authority to direct the handling, routing, and movement of the traffic of a rail carrier and its distribution over its own or other railroad lines. 49 U.S.C. § 11123 (a)(1).

The Railroad Commission respectfully suggests that the STB adopt conditions as follows:

> <u>TexMex Control of MP Line from Houston to Beaumont</u>. To provide TexMex and BNSF with a congestion free route eastward from Houston, TexMex is authorized to assume control of UP's former Missouri Pacific line from Houston (Gulf Coast Jct.) to Beaumont. Until such time as TexMex can install a CTC system on the line between Gulf Coast Jct. and Beaumont (anticipated to be thirty days), TexMex shall be allowed to place a representative in UP's Harriman Dispatching Center to direct train movements over the line.
>
> <u>BNSF Use of TexMex Controlled Trackage</u>. TexMex shall immediately enter into a dispatching agreement with BNSF for expedited handling of BNSF trains over the MP line from Gulf Coast Junction to Beaumont.

4. **EMERGENCY CONTRACT SUSPENSIONS**. The STB should order emergency release from the contractual obligations to UP for those shippers located on the former HB&T's East Belt Line and the SP Galveston Line who wish to and who are able to arrange alternative shipping arrangements with other railroads for the duration of the emergency. To achieve the full benefit of the implementation of the Railroad Commission's three recommendations, the STB must persuade the UP to extend its prior agreement made at the October 27, 1997 to cover these three additional emergency measures. STB <u>Service Order</u>.

## VI.

## PRAYER FOR RELIEF

WHEREFORE, THE RAILROAD COMMISSION OF TEXAS respectfully prays that the Surface Transportation Board: (1) extend the emergency determined in STB Service Order for an additional two hundred forty (240) days; (2) continue in effect conditions 1 through 4 of STB Service Order for the duration of such extension; (3) mandate emergency joint or common use of expanded neutral switching activities by the Port Terminal Railroad Association; (4) prescribe emergency temporary through route by establishing a clear path through Houston for TexMex; (5) direct emergency handling, routing and movement of traffic over the former MP line from Houston-Beaumont for the benefit of TexMex; (6) provide emergency release from shipper obligations to UP to facilitate the emergency measures described above; (7) mandate permanent divestiture of the UP trackage shown on Map No. 2 to an expanded shared-asset switching facility in Houston; (8) mandate permanent divestiture of the clear path through Houston shown on Map No. 3 to TexMex; (9) mandate permanent divestiture of the former MP Houston-Beaumont line to TexMex; and that the STB grant such other and further relief for which the Railroad Commission may be entitled.

DATED AND SIGNED at Austin, Texas on November 29, 1997 to be effective as of its filing on December 1, 1997.

Respectfully submitted,

Lindil C. Fowler, Jr
General Counsel

Kenneth W. Nordeman
Assistant Director, General Law

Attorneys for
The Railroad Commission of Texas

**CERTIFICATE OF SERVICE**

I hereby certify that on November 29, 1997, I have caused the Supplemental Petition of the Railroad Commission of Texas to be served on the parties of record simultaneously with its filing with the STB on December 1, 1997.

Kenneth W. Nordeman

**Exhibit A**

# THE IMPACTS OF THE UNION PACIFIC SERVICE DISRUPTIONS ON THE TEXAS ECONOMY: AN INTERIM REPORT

Prepared for the Railroad Commission of Texas by

Bernard L. Weinstein, Ph.D. and
Terry L. Clower, Ph.D.

Center for Economic Development and Research
The University of North Texas
Denton, Texas

November 24, 1997

## Background and summary of findings

Since last July, the Union Pacific Railroad has experienced severe service disruptions that have resulted in delays, lost production, and higher shipping costs for a large number of businesses who depend on rail to move their products. Though the entire western U.S. has been affected by the UP's problems, Texas has been hit harder than any other state. This is not surprising considering the Union Pacific is the largest railroad in Texas and thousands of businesses are served by no other rail carrier.

Bulk commodity shippers, such as petrochemical plants, grain merchants, quarries and forest products companies, have been most inconvenienced as have electric utilities who depend on the UP to deliver coal from Montana and Wyoming to fire their generators. But retailers of consumer goods such as furniture and general merchandise are also being effected by the UP's November 1st suspension of part of their intermodal service (i.e., cargo containers and truck trailers) between Chicago and Texas.

Responding to shippers' complaints, on October 27th the Surface Transportation Board (STB) of the U.S. Department of Transportation conducted a 12-hour hearing to determine if federal intervention was required to alleviate the Union Pacific's service disruptions. Testimony was received by more than 60 witnesses, including the chairman of the Railroad Commission of Texas (RRC). Following the hearing, the STB found that a "transportation emergency" existed in the western U.S. that was having adverse effects on shippers and overall rail service. On October 31st, the Board issued an order allowing the Texas-

Mexican Railway Company to accept traffic from Houston shippers currently under contract with the Union Pacific in an effort to alleviate some of the most serious tie-ups in south Texas and the Port of Houston. The Board also ordered the UP to facilitate the operations of the Tex-Mex and the Burlington Northern Santa Fe Railway (BNSF) in the Houston area and to maintain open use of the main lines and sidings on its Houston-to-Memphis and Houston-to-Iowa routes. To date, however, it doesn't appear that the STB's intervention has done much to improve rail freight service in Texas or the rest of the western U.S.

Without question, the Union Pacific's logistical problems are imposing significant incremental costs on Texas manufacturers, growers and shippers that will eventually be passed on to businesses and consumers both in-state and out-of-state. ***We conservatively estimate the costs to date for Texas businesses, measured by lost sales, reduced output and higher shipping charges, at $762 million. We have also identified $623 million in additional costs to businesses, consumers and taxpayers in Texas that will be incurred within the next few months unless the Union Pacific can quickly remediate its service delivery problems.***

The following discussion describes, illustrates and—where possible—quantifies these costs and also posits some long-term consequences for the state and its shippers if the UP's problems aren't resolved in an expeditious manner.

The chemical industry

The Gulf Coast's $105 billion chemical industry has probably been hit harder than any other manufacturing sector by the UP's service problems since virtually all bulk chemicals are shipped by rail. Furthermore, large chemical companies typically own or lease their own rail cars. Thus, diverting shipments to trucks and barges imposes significant incremental costs to chemical companies.

A recent survey by the Chemical Manufacturers Association (CMA) found that 213 major production facilities along the Gulf Coast had been affected by disruptions in service, placing a large number of jobs at risk. (Employment at these facilities exceeds 95,450). According to 31 responding companies, the average monthly costs of service disruptions during the summer totaled $34.1 million and are now running at $62.3 million per month. About two-thirds of the total costs arise from lost sales or production while another 23 percent is attributed to higher freight and shipping costs. The remaining incremental costs are attributed to lost rail car utilization, additional inventory carrying costs, the higher cost of raw materials purchased from other producers, the cost of tracing rail cars, and other administrative expenses.

***At a minimum, the Gulf Coast chemical industry-- located principally in Texas-- has incurred costs of $289.2 million in lost production and higher freight charges since the UP's service problems began in June. The actual figure is probably closer to $500 million for the Gulf Coast and $350***

***million for Texas*** since a number of companies did not respond to the CMA's survey.

What's more, because industrial chemicals are essential raw materials for many other industries-- including agriculture, automobiles, construction, food processing, pharmaceuticals, plastics and electronics-- production delays and higher shipping costs attending the UP service disruptions are no doubt being felt by other sectors of the state and national economies. Though these costs are indeterminate at this time, inevitably they will show up in higher prices to wholesalers, distributors and consumers over the next six to twelve months.

Agriculture

In 1996, the value of U.S. crop production totaled $86.3 billion, and the cost of transporting these crops to food processors was approximately $4 billion. For the state of Texas, cash receipts to farmers totaled $5.3 billion in 1996 and transportation costs came to about $250 million. As with chemicals, the nation's farmers and grain shippers depend largely on the railroads to get their crops to markets, both domestic and foreign. Agricultural shippers and receivers generally have limited access to alternative providers of transportation services because many are located beyond effective trucking distances from these markets. In addition, western growers and shippers have little access to waterway transportation, with the result that up to 80 percent of grains and cereals are shipped by rail in some states.

Grain shipments by the Union Pacific have slowed markedly in recent months. According to Association of American Railroads, the UP loaded 6,104 rail cars with grain during the first week of November-- 41 percent less than the 10,343 for the same week a year ago. The Burlington Northern, partly because of the UP tie-ups, has also seen a drop-off in grain shipments-- 8,475 cars per week versus 10,892 a year ago. Some elevator operators report waiting 30 to 60 days to receive rail cars.

During the STB's October 27 hearing, the National Grain and Feed Association reported that grain elevators were filled to capacity, particularly in Kansas, Oklahoma and Texas, and that local cash prices were declining because of a lack of storage. Some shippers cited numerous instances of rail cars that had been loaded with grain and billed but were sitting idle on their tracks for weeks because the Union Pacific was unable to provide locomotive power. Members from the Texas Panhandle reported that some customers were refusing to buy Texas-origin grain for fear of not receiving timely shipments.

During the late fall, more than 50,000 carloads of grain typically flow through Texas Gulf Cost ports on their way to foreign markets. Undoubtedly, exports through these ports will be lower this year because of the UP's service disruptions (see discussion of international trade below).

***A conservative estimate of the losses incurred by Texas' farmers and grain shippers from lower prices, foregone sales opportunities and higher freight costs is $100 million to date.*** These costs will eventually show up at the dinner table, not only for households in Texas but in all other parts of the U.S. as well.

Paper and forest products

The forest products and paper industry records total annual sales of approximately $200 billion and generates seven percent of all U.S. manufacturing output. Annually, the industry exports in excess of $17 billion of product. It is also the fourth largest user of rail transportation in the country, moving an average of 24,000 carloads in a given week. The industry is responsible for 70 percent of all railroad boxcar traffic and also fills thousands of containers carrying finished goods for domestic and offshore distribution.

The American Forest and Paper Association (AF&PA) reports that many of member companies have seen their businesses disrupted by the UP's problems. These disruptions have ranged from longer transit times to paper mill shutdowns. Some companies claim delivery problems have caused mill inventories to rise, resulting in extra warehousing costs, increased emergency delivery costs, and--ultimately--higher prices to customers.

East Texas is a major producer of timber, paper, plywood, particle board and other forest products with many manufacturing operations dependent on the Union Pacific for inbound raw materials as well as outbound product. Not surprisingly, a number of East Texas forest products companies are reporting delays and lost sales because of the UP's problems. For example, Champion International, with four manufacturing operations in East Texas, has experienced service problems with shipments destined to southern California. Transit times have increased to as long as 45 days, and the company claims business is being lost to competitors not dependent on UP service.

In Texas, forest products and paper companies shipped about $10 billion of processed goods in 1996. ***If the Union Pacific service disruptions have reduced sales of Texas' forest products companies by 5 percent since July, losses to date have totaled approximately $208 million.***

Cement, concrete and other building materials

Cement manufacture is tremendously reliant on rail transportation, both for inputs and product shipment. Aggregate must be hauled from quarries to cement kilns, while coal and/or coke are typically burned as kiln fuels. The Union Pacific's service disruptions have severely burdened the region's cement and concrete companies.

For example, Cemex USA, the second largest cement company in Texas and captive to the Union Pacific, has seen a 52 percent reduction in outbound trains since July. Consequently, sales have been reduced by 1/3 to 1/2 at rail supplied terminals, resulting in revenue losses in the hundreds of thousands of dollars per month as customers shift to other suppliers. Cemex also reports the loss of a contract to supply limestone to a TxDOT highway project because of an inability to maintain delivery schedules.

Pioneer Concrete of Texas has been virtually abandoned by the Union Pacific for the hauling of aggregate and has been forced to rely on trucks instead. Pioneer estimates that lost sales and higher shipping costs have cost the company $2.7 million since June 1st, with no relief in sight. Other Houston-area cement and concrete companies report similar difficulties. North Texas Cement, located in Midlothian, is incurring lost profits and higher fuel costs of $113,000 per month because of slow coal and coke deliveries by the UP. In part because of the Union Pacific disruptions, cement has been on allocation in most parts of Texas for the past six months.

Glass manufacturers in Texas and other parts of the U.S. are paying more for soda ash because most of the producers are located in the Green River basin of Wyoming and captive to the UP. Shippers have turned to trucks since the car shortage began on the UP several months ago and are paying the higher freight costs.

Producers of cement, pre-cast concrete, limestone, soda ash and other building materials usually enter into one-year contracts to supply their products to customers at fixed delivered costs. Thus they're having to absorb the higher freight charges incurred as a result of the UP's problems for the time being. But when these contracts are renegotiated over the next six to 12 months, producers will attempt to recover not only their higher shipping costs but their foregone earnings. Higher costs for building materials, in turn, will ripple through the construction industry and boost the nation's overall inflation by some percentage.

Texas could be hit especially hard, since the state is in the midst of a building boom. Last year, manufacturers of construction materials recorded total shipments of approximately $5 billion. ***Assuming a five percent loss of***

***business due to UP service disruptions, we estimate the foregone sales of Texas' cement, concrete and other building products at $104 million.***

Taxpayers may also feel the pinch of the UP's problems because roads and other infrastructure projects consume huge quantities of cement, pre-cast concrete and other building materials. For instance, the Texas Department of Transportation currently spends about $3 billion for highway construction and repair annually. ***Should construction costs rise five percent because of higher material costs, Texas' taxpayers will have to spend an additional $150 million to realize the same level of road improvement.***

<u>Electric utilities</u>

About 50 percent of Texas' electric power generation comes from coal or lignite-fueled boilers, and most of the coal burned in the state is transported by rail from the Powder River Basin in Wyoming and Montana by the Union Pacific and the Burlington Northern. Although BNSF's coal shipments have remained on schedule, overall deliveries to utilities served by the UP have been curtailed or delayed since the company reduced the number of coal cars on its system by 19 percent in September in an effort to alleviate delays in shipping for other industries. Consequently, Houston Lighting & Power, City Public Service Company of San Antonio, the Lower Colorado River Authority (LCRA), Entergy, and Central Power & Light have all had to draw down their on-site stockpiles in order to meet customer demand. In some cases, stockpiles have been reduced to a 10 to 15 day supply. Entergy has filed a lawsuit against the Union Pacific for breach of contract, and the LCRA has threatened similar action.

Some Texas utilities have turned to other sources for coal or switched to natural gas to meet demands for power generation. City Public Service in San Antonio-- heavily dependent on the Union Pacific -- is importing coal from Colombia through the Port of Corpus Christi to help fuel its three coal-fired units. In Austin, the LCRA has had to spend $8 million so far this year to buy higher-cost natural gas and purchased power.

About half of Texas' coal-fired generators depend on out-of-state coal, while the others burn Texas-mined lignite that's easier to deliver. Fortunately, sufficient gas-fired generating capacity exists to make up for any shortfalls resulting from interruptions in coal deliveries.

The Gas Services Division of the Railroad Commission of Texas has examined a scenario in which Texas' coal fired plants dependent on out-of-state coal face a 50 percent reduction in supplies during the five month winter heating season of 1997-98, from November through March. Making up the shortfall would require these utilities to purchase an additional 131 billion cubic feet (Bcf) of natural gas for consumption on gas-fired power plants. This would represent an increase in Texas gas demand of 9.6 percent and total U.S. gas demand of 1.3 percent.

Unfortunately, substituting gas for coal is an expensive proposition, since natural gas prices on a Btu equivalent basis are about twice that of coal. With spot gas prices currently running about $3 per thousand cubic feet, *additional*

***fuel purchases this winter could total $393 million and would be passed through almost immediately to businesses and households in the fuel adjustment portions of their bills.*** If this winter turns out to be exceptionally cold, gas prices could be even higher than $3; and in a worse-case scenario gas deliveries could actually be put on allocation, as has happened in the past.

Retail trade and small business

As part of the strategy to clear gridlock on its system, the UP suspended intermodal service, which hauls general merchandise, between the Midwest and Texas on November 1st. Some retailers and small businesses who previously relied on the UP to deliver their goods are paying premiums for trucking service or doing without. Toys, furniture, consumer electronics and other products may be in short supply during the holiday season, reducing retail sales in Texas and elsewhere in the U.S.

Retail trade at general merchandise, apparel and furniture/home furnishings stores in Texas was approximately $40 billion in 1996. Stores typically record about 20 percent of their total retail sales during the holiday season. ***If Texas merchants realize even a one percent loss in sales due to the UP's inability to deliver goods in time for holiday shopping, retail trade will be depressed by $80 million. In addition, state sales tax collections will decline by $ 5 million and local sales tax receipts will be down $800,000.***

Automobile dealers in Texas who depend on the Union Pacific have reported shipping times for new cars and light trucks doubling or tripling since August. This has been particularly harmful to smaller auto stores who do not keep much inventory on hand. In some cases, cars are being received more than a month past invoice, which means dealers wind up paying interest to the manufacturers on cars they haven't even received.

Presumably, automobile and light truck dealers will be able to recover lost sales once the UP solves its delivery problems. But in the short term, ***sales commissions are lower and interest charges are higher than they would be if deliveries of vehicles were on schedule.***

International trade disruptions

International trade is of growing importance to the health of both the Texas and U.S. economies. Indeed, according to the U.S. Department of Commerce, about 40 percent of the nation's growth over the past year can be attributed to exports and imports. If anything, international trade is probably even more important to the Texas economy.

The Union Pacific's logistical problems have disrupted activity at two of the nation's busiest ports– Los Angeles and Houston. At the Port of Los Angeles, which along with Long Beach accounts for 25 percent of all ocean-going container traffic, some vessels have been diverted because of congested terminals. Delays in loading and unloading cargo vessels are having the dual effect of increasing shipping costs and reducing the fees received by the Port.

The Port of Houston is affected somewhat differently since commodities, as opposed to containers, account for most of the volume. In 1996, the Port of Houston moved 86.5 million tons of cargo with a value of $34.1 billion. Chemicals, petroleum products, plastics, fertilizers, cereals and machinery constituting the major commodities and products. Though the Port of Houston has made no estimates of lost business, ***it's likely that several billions of dollars of shipments have been diverted from Houston and other Texas ports as a result of the UP's problems.***

Union Pacific's service problems are particularly disruptive to NAFTA trade. The UP's lines stretch from the Canadian border to the Mexican border, and the UP recently acquired a Mexican concession through a joint venture. About 60 percent of U.S.-Mexico rail traffic crosses the border in Texas, with the Union Pacific accounting for the lion's share. The UP and the Tex-Mex share the huge gateway to Mexico at Laredo, which alone accounts for about 80 percent of rail shipments between Texas and Mexico. UP is also the primary railroad serving the Port of Houston, another important gateway for NAFTA trade.

In effect, the Ports of Laredo and Houston have become "chokepoints" for NAFTA-related trade. Because of the UP's problems, cargo is piling up at both ports, and shippers have been forced to use more expensive truck transport to get their products to and from Mexico. If the Laredo and Houston gateways aren't unclogged soon, the rapid growth of U.S.-Mexico trade may be impaired with an attendant loss of jobs and income in both countries.

## Other costs to the Texas and national economies from the Union Pacific service problems

The UP's system-wide problems are disrupting "just-in-time" delivery schedules for many industries. By reducing the amount of inventory on hand, businesses have realized substantial cost savings that have helped to hold down retail price increases. Indeed, effective inventory control is one of the reasons inflation has been muted during the economic expansion of the 1990s. As discussed earlier, the ultimate cost of lost production, delays and additional freight charges will be higher prices at wholesale and retail for food, construction materials and a wide range of manufactured goods. Some economists have estimated the UP's problems could boost the consumer price index (CPI) by one- to two-tenths of a percent over the next year.

The trucking business has clearly benefited from the UP's delivery problems, as most shippers have no other alternative for moving their products. According to the American Trucking Association, truck tonnage has reached an all-time high in recent months. With few rigs or drivers available to serve new customers, trucking companies are boosting their rates. At the same time, increased truck traffic is making Texas' (and the nation's) highways less safe while accelerating wear-and-tear on the pavement and roadbed. Higher TxDOT outlays for repair and maintenance of Texas' highways will soon follow.

Some Texas businesses, who've been unable to deliver product in a timely fashion because of the UP's problems, worry about a permanent loss of customers. Only time will tell if markets lost in the past few months can be quickly recaptured if and when the UP brings order to its system. Some commodity shippers, such as aggregate producers, are concerned the UP may abandon them entirely because of the low profitability associated with their business.

Finally, there are costs associated with the continuation of the Union Pacific's virtual monopoly on commodity shipments in the state of Texas. For the long-term, a spin-off of some of the UP's routes, open-access on others, and the establishment of an independent terminal operator at the Port of Houston may be the only ways to ensure more competition and better rail service for shippers in Texas and other western states.

**SUMMARY OF**

**THE RAILROAD COMMISSION'S PROPOSAL**

**FOR ALLEVIATING THE UP SERVICE CRISIS**

On November 21, 1997, the Railroad Commission approved and adopted a Plan for Alleviating the Union Pacific Service Crisis, which it has proposed to the Surface Transportation Board as an appropriate means of resolving the current crisis and for remedying, on a permanent basis, rail service in the Houston/Gulf Coast area.

Map No. 1 depicts Union Pacific's virtual monopolization of the Houston rail network.

The Commission's Plan suggests three adjustments to rail operations in and around the Houston, Texas terminal area which will improve greatly the flow of rail transportation to, through, and out of the Houston, Texas area. The Railroad Commission believes that the implementation of these three adjustments will not only materially relieve the current rail service emergency but also will provide substantial protection against a repeat of the current rail service crisis.

First, the Commission Plan recommends **the expansion of a Port Terminal Railroad to operate as a shared-asset facility to provide neutral switching services in the Houston terminal area.** Second, the Commission Plan recommends **the establishment of a clear path through the Houston terminal area for the TexMex.** Third, the Commission Plan recommends **the transfer of the former Missouri Pacific track from Houston to Beaumont to the TexMex.**

## A. AN EXPANDED PORT TERMINAL RAILROAD

The first important step to alleviating the UP service crisis is the transfer of certain of UP's port area industrial trackage to an expanded switching facility, herein called the new Port Terminal Railroad ("PTR"), that would provide neutral switching to port area industries.

The new PTR could be publicly owned and privately operated, privately owned and publicly operated, or privately owned and privately operated. Under the private ownership alternative, it could be owned by the railroads serving Houston, by investors, or by shippers located on the trackage which it operates.

The PTR would acquire trackage on both sides of the Houston Ship Channel and also the Houston Belt and Terminal's East Belt Line. Transfer of the UP trackage to PTR would allow the PTR to provide neutral switching services to large numbers of captive shippers who have been seriously harmed over the past six months because they have not had an alternative to UP's service.

Under the Commission Plan, the UP trackage to be transferred to the PTR is shown on Map No. 2 and includes track segments as follows: **UP line from Houston to Baytown; SP line from Baytown to Dayton; SP line from Englewood Yard to Galveston; UP line from Katy Neck to Galveston;** and the **Clinton Drive Industrial Lead.** Additionally, the HB&T trackage from Double Track Junction to Englewood Yard (the "East Belt") would be transferred to PTR, including East Belt Yard, Dallerup Yard, Basin Yard, and Glass Yard, plus industrial leads.

To accomplish the expansion of neutral switching facilities in Houston, the Railroad Commission urges the STB to mandate divestiture of UP's trackage depicted on Map No. 2 to facilitate its transfer to the PTR.

Thus, UP trackage and the HB&T's East Belt would be integrated with the existing port area trackage that is owned by the Port of Houston Authority and operated by the present Port Terminal Railroad Association (the "PTRA") to create a comprehensive network of rail lines, lead tracks, and yards serving the booming industrial area extending from Dayton to Baytown to Galveston, including both sides of the Houston Ship Channel.

**Basis for this element of the Railroad Commission's Proposal.** The Commission's Plan for expanded neutral switching in the Houston/Gulf Coast area builds on the success of the existing PTRA operation, which has provided excellent service at competitive rates to large numbers of shippers. In fact, the well managed PTRA operation has been so successful that the existing PTRA organization could be basis for an expanded Port Terminal Railroad.

Divestiture of UP port area trackage to an expanded Port Terminal Railroad will allow captive shippers to have access to TexMex and BNSF, as well as UP. The ability of shippers to choose between line-haul carriers will ensure that serious future operating problems on any one carrier, such as those experienced by UP for the past six months, will not have significant, long-term impacts on the ability of shippers to receive inbound raw materials and distribute finished products. As soon as a shipper realizes he is being hurt by a particular carrier's inability to perform, he will simply divert his shipments to a competing carrier.

In addition to providing shippers with multiple line haul options, an expanded Port Terminal Railroad will be able to create greater operating efficiencies by handling a much larger volume of traffic through coordinated specialized terminal facilities. For example, the UP Strang Yard could be used by the expanded PTR for making up outbound trains, while PTRA's Pasadena Yard could be used for receiving and classifying inbound trains.

The expansion of neutral switching to industries located near the Port of Houston will benefit all shippers because it will provide them the access to BNSF, a Class I railroad with a comprehensive network that spans the Western two-thirds of the United States. More importantly, the only way to ensure that the present service crisis is never repeated is to give shippers access to a third railroad with its own trackage that has connections with the major railroads east of the Mississippi River. The Commission's Plan assumes this third carrier will be TexMex, along with its affiliate, KCS.

## B. A CLEAR PATH THROUGH HOUSTON FOR THE TEX MEX

The second important step to alleviating the UP service crisis is to provide a clear path through the complex and congested Houston rail network for the TexMex.

It is contrary to the public interest for UP to control all of the urban trackage in the greater Houston area because it is the UP's dominance of the rail infrastructure in Houston that has been the predominant cause of the near paralysis of rail operations in the Houston/Gulf Coast area over the past six months. By giving the TexMex its own route through Houston and allowing BNSF to use that route for trains operating between Houston and New Orleans, it is unlikely there will ever again be a situation where train operations in the Houston area become congested to the point of near immobility.

The clear path through the Houston terminal area that is proposed in the Commission Plan is depicted on <u>Map No. 3</u> and includes segments of UP trackage as follows: **Pierce Junction to Katy Neck**; **Katy Neck to San Jacinto Street**; **San Jacinto Street to HB&T North Belt**; and **HB&T North Belt to Gulf Coast Junction**. These four segments of UP trackage would be acquired by TexMex and connections would be made between them so that they together constitute an integrated route through Houston. To accomplish the establishment of a clear path through Houston for the TexMex, the Railroad Commission urges the STB to mandate divestiture of UP's trackage depicted on <u>Map No. 3</u> to facilitate its transfer to TexMex.

In addition to clearing a path through Houston as described above, any long-term route planning for the TexMex may well include a different route from Victoria to Houston. The new Victoria-Houston route for TexMex might include reconstruction of the abandoned SP line from Victoria to Wharton, acquisition of the unused SP line from Wharton to Kendleton, and construction of a new line from Kendleton to Thompsons, where a connection would be made to the Houston Lighting and Power line that extends from Thompsons to Arcola. The Victoria-Houston line is depicted on <u>Map No. 4</u>. By adding UP's Arcola to Pierce Junction line segment, this new Victoria-Houston line could link up with the clear path through Houston proposed above. Pending the completion of such a Victoria-

Houston line, TexMex must rely on trackage rights over UP from Placedo to Algoa and over BNSF from Algoa to Houston.

**Basis for the "clear path" element of the Railroad Commission's proposal.** The Railroad Commission's proposal to create a clear path for TexMex through Houston should have minimal negative impacts on UP's operations because the line segments that would comprise the TexMex clear path appear to be of marginal value to UP. To the extent that UP has a need to operate over those line segments, UP could have trackage rights.

The clear path through Houston will prevent TexMex's trains from being caught up in the terrible congestion that is plaguing both UP and BNSF. By giving TexMex its own trackage in Houston, there will no longer be the now common twenty-four delays that have severely impacted TexMex's ability to provide satisfactory service, while causing its operating costs to exceed its revenues. Instead, trains will move through the Houston area in two to three hours, with the same crew that got on at the origin terminal.

By giving TexMex a larger role in the Houston market, and allowing it to operate autonomously, completely apart from UP and BNSF, shippers will have an insurance policy against the failure of the two interdependent industry giants to perform at levels that are acceptable and necessary for Houston/Gulf Coast area companies that are primarily dependent on rail transportation.

## C. TRANSFER OF THE FORMER MP HOUSTON-BEAUMONT LINE TO TEXMEX

A third important step to alleviating the UP service crisis is to transfer the former Missouri Pacific ("MP") Houston-Beaumont line to TexMex.

As shown on Map No. 5, UP currently controls two lines from Houston to Beaumont: the former SP line through Dayton; and the former MP line through Sour Lake. For six months, TexMex trains have experienced great delays operating over its trackage rights on UP's two lines between Houston and Beaumont. The delays have substantially increased operating costs for TexMex, while significantly delaying shipments. Further, the delays have prevented TexMex from providing shippers with alternatives to UP's service.

The Commission Plan visualizes that the former MP line be transferred to TexMex so that TexMex could have a controlled route from Victoria to Beaumont (see Map No. 4 **infra**). It recommends that TexMex be put in a position where it is no longer at the mercy of UP and that shippers be given additional routing options when UP cannot satisfactorily perform. Under the Commission's Plan, TexMex could acquire the MP Houston-Beaumont line and would immediately grant trackage rights to BNSF over the line for the entire distance between Houston and Beaumont, giving BNSF an alternate route. Critically, to ensure BNSF of prompt, efficient, and fair handling of BNSF trains, TexMex would dispatch the MP Houston-Beaumont line from a centralized traffic control office in Houston.

To ensure UP that it has sufficient capacity in the Houston-Beaumont-Lake Charles-New Orleans corridor after the transfer of the MP line to TexMex, UP would also be given trackage rights over the line. Those trackage rights would complement UP's existing trackage rights over Kansas City Southern ("KCS") between DeQuincy, Louisiana and Beaumont. The UP has satisfactorily utilized the DeQuincy-Beaumont line segment since it acquired Missouri Pacific fifteen years ago; therefore, the proposal that UP have trackage rights over the MP Houston-Beaumont line segment should not present a problem in terms of efficient train handling. Since there is no on-line industry of any substance on the MP line, the transfer of the line to a different railroad should have no direct adverse commercial implications for UP. Nevertheless, UP would be given access to any future industries located on the line.

To accomplish the transfer of the MP Houston-Beaumont Line, the Railroad Commission urges the STB to mandate divestiture of UP's ownership of the MP Houston-Beaumont line to facilitate its transfer to TexMex.

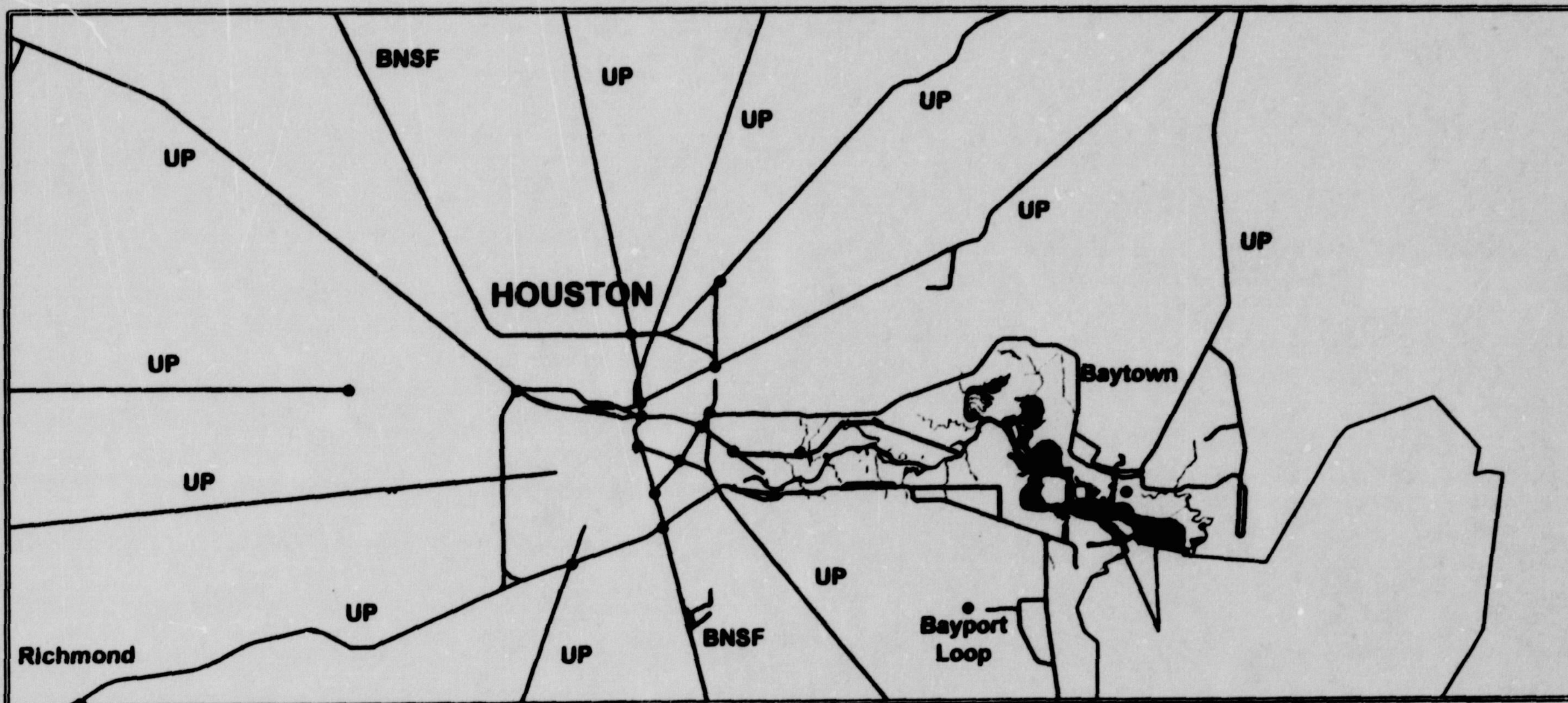
Proceeds from the transfer of the MP line could be used by UP to double track its remaining SP line from Houston to Beaumont; however, if UP elects to retain trackage rights over the MP line, UP may wish to do no more than build additional passing sidings at strategic locations on the line.

**Basis for this element of the Railroad Commission's Proposal**. The Commission Plan to transfer the MP Houston-Beaumont line should have no negative operational impacts on the UP, but it will have very positive operational impacts on the performance of the TexMex and its affiliate, KCS, allowing them to provide shippers with an efficient alternative for moving north and east from the Houston/Gulf Coast area.

Once TexMex has control of its own route between Beaumont and Houston, trains will be dispatched promptly and moved expeditiously. Passing sidings will be used for their intended purposes rather than for storing trains that cannot be accommodated in Houston/Gulf Coast area yards because of congestion (as has been the case with UP over the past six months).

The combination of a clear path through Houston and an independently owned and operated line from Houston to Beaumont will allow TexMex to serve as an "escape route" for Houston/Gulf Coast area shippers that are receiving unacceptable service from UP and BNSF.

# CURRENT RAILROAD CONTROL
# HOUSTON, TEXAS



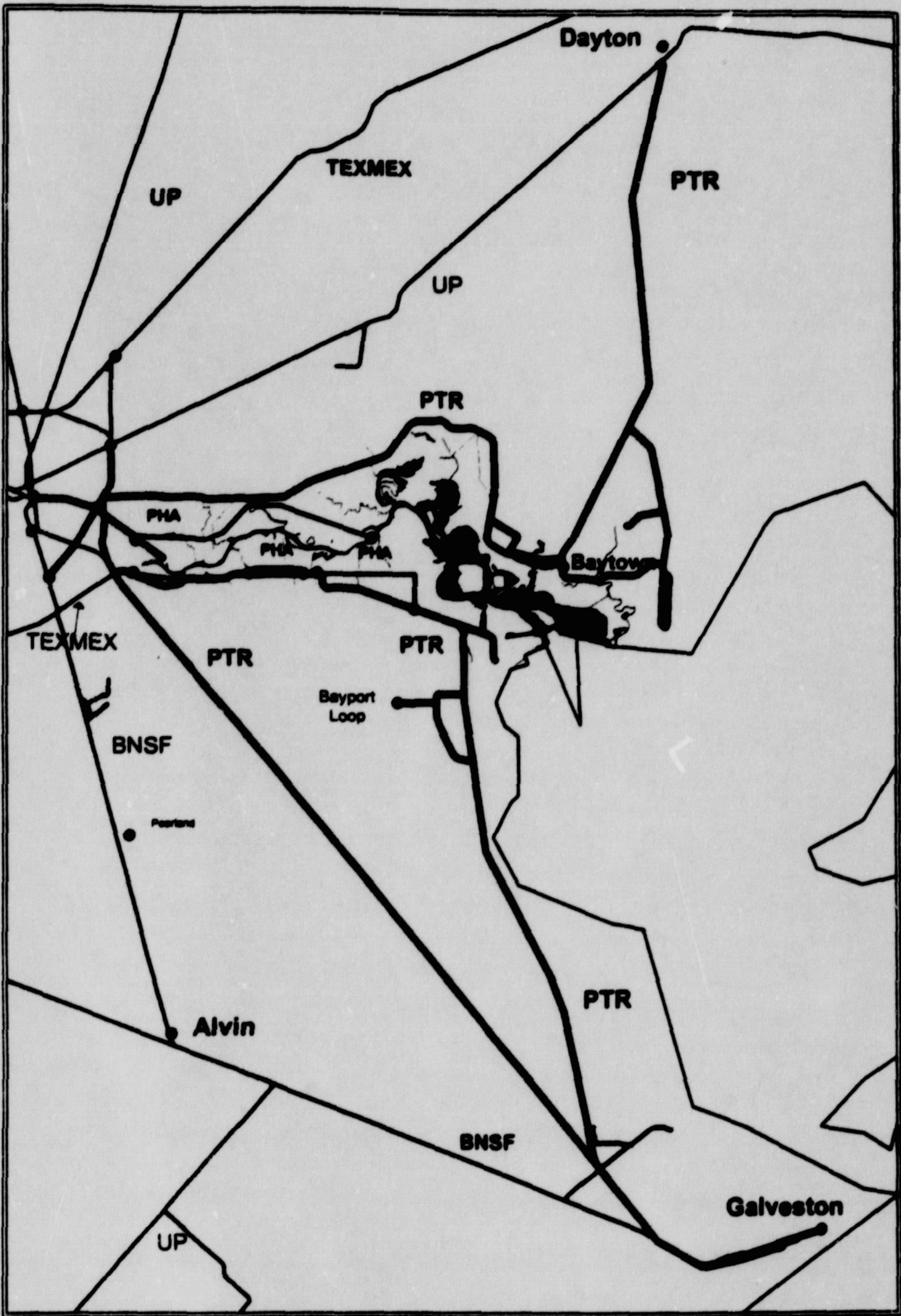

Rail Line Legend

= Union Pacific
= Burlington Northern Sante Fe
= Port of Houston Authority

December 1997

MAP No. 1

# HOUSTON TERMINAL AREA
# SHOWING PROPOSED EXPANSION
# OF PORT TERMINAL RAILROAD




**Rail Line Legend**

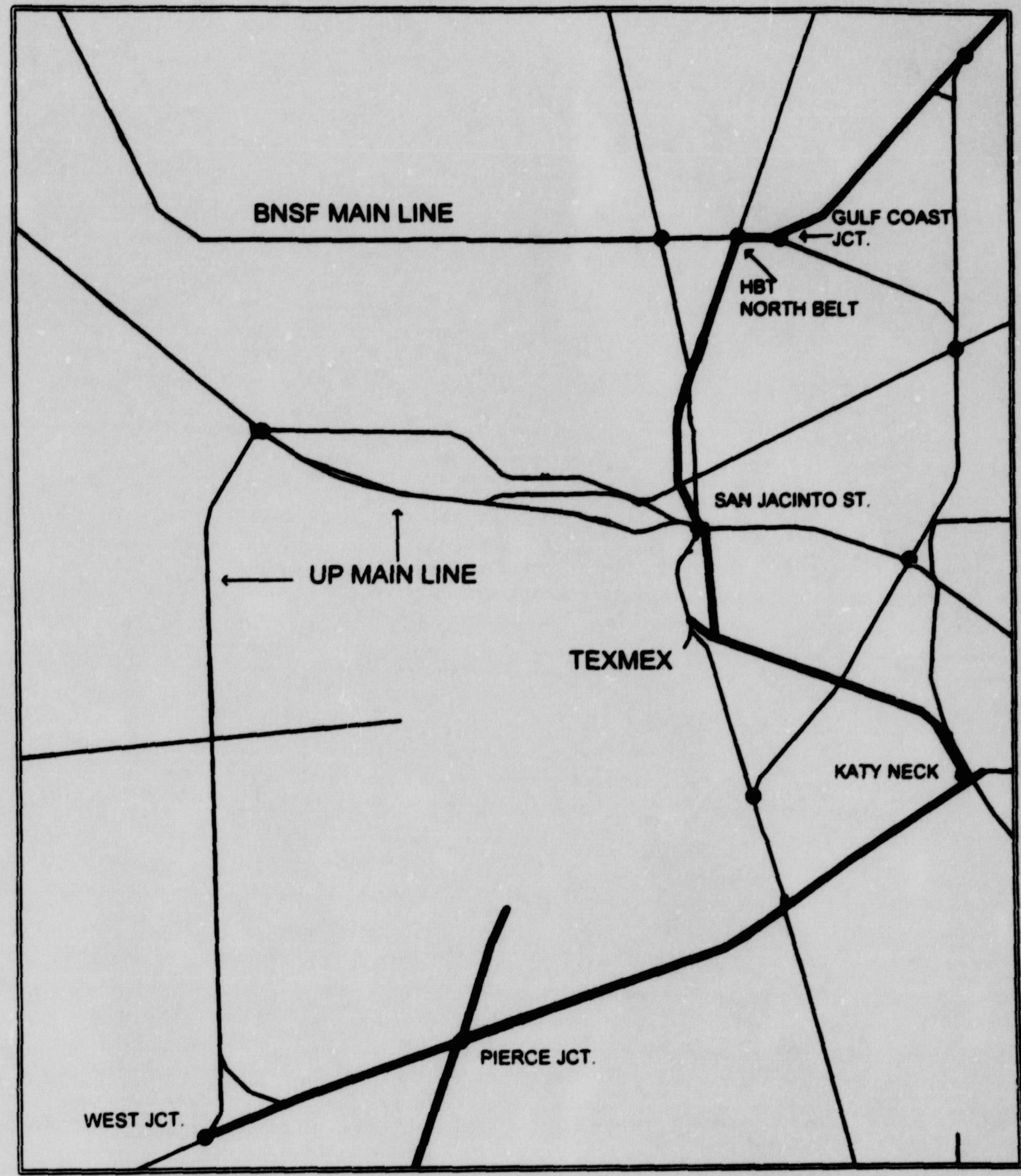
- = Union Pacific
- = Burlington Northern Sante Fe
- = Texas-Mexican
- = Port of Houston Authority
- = Port Terminal Railroad

December 1997

**Existing Port Trackage shown in black**
**New Port Trackage shown in blue**

**MAP No. 2**

# CLEAR PATH THRU HOUSTON
# FOR TEXMEX

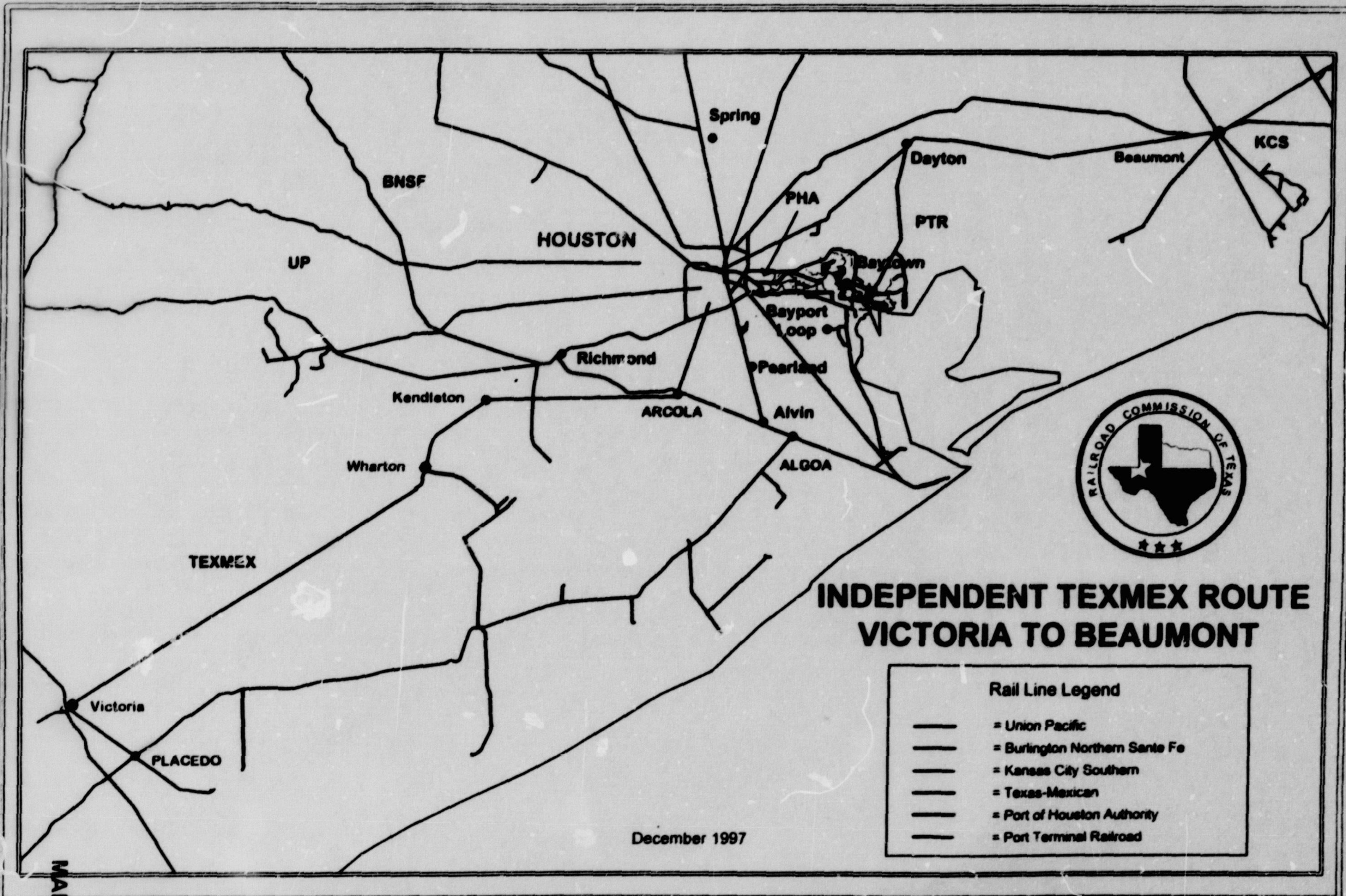



**Rail Line Legend**

- = Union Pacific
- = Burlington Northern Sante Fe
- = Port Terminal Railroad
- = Texas-Mexican

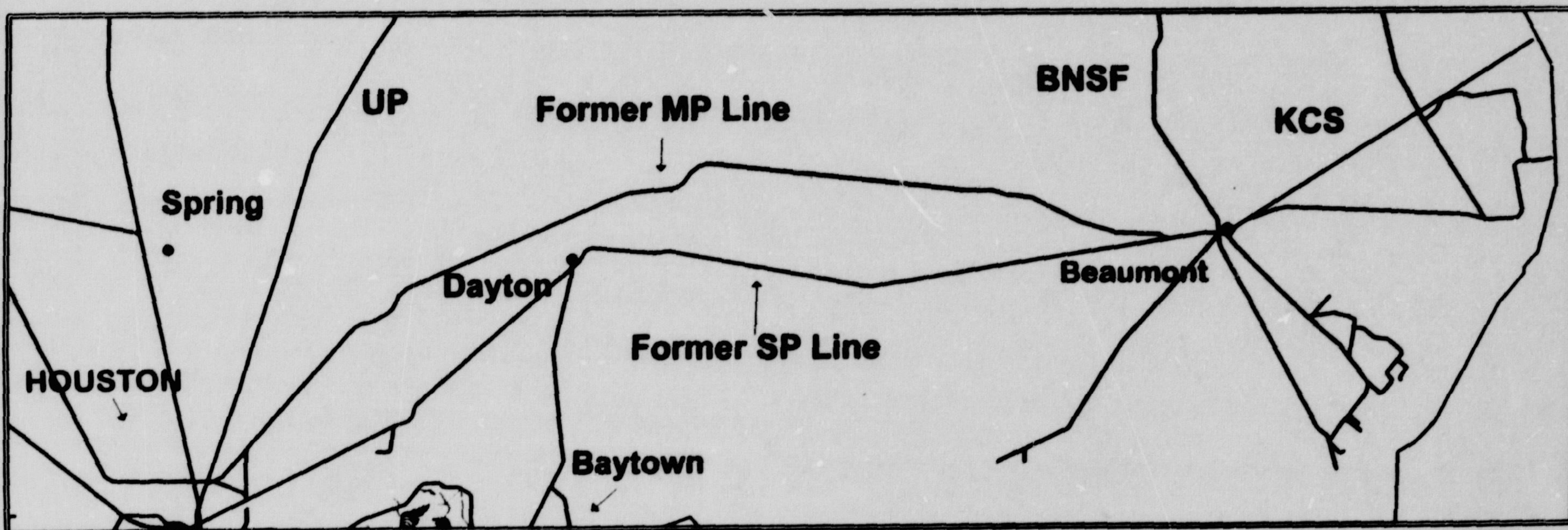
December 1997

**MAP No. 3**


Spring
Dayton
Beaumont
KCS
BNSF
PHA
PTR
HOUSTON
UP
Baytown
Bayport
Loop
Richmond
Pearland
Kendleton
ARCOLA
Alvin
ALGOA
Wharton
TEXMEX
Victoria
PLACEDO
RAILROAD COMMISSION OF TEXAS
INDEPENDENT TEXMEX ROUTE
VICTORIA TO BEAUMONT
Rail Line Legend
= Union Pacific
= Burlington Northern Santa Fe
= Kansas City Southern
= Texas-Mexican
= Port of Houston Authority
= Port Terminal Railroad
December 1997

MAP No. 4

# HOUSTON - BEAUMONT LINES




RAILROAD COMMISSION OF TEXAS

December 1997

Rail Line Legend

= Union Pacific
= Burlington Northern Sante Fe
= Kansas City Southern
= Texas-Mexican

MAP No. 5

Citation | Search Result | Rank 4 of 4 | Database
1/19/98 HSTNCHRON 18 | HSTNCHRON
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1998 WL 3555785

Houston Chronicle


Monday, January 19, 1998

NEWS

Editorials

# CLOGGED TRACKS / Plan offers promise for clearing Texas' railway backup

Staff

The merger between Union Pacific and Southern Pacific railroads has been, in short, the marriage from hell. Problems stemming from the merger have resulted in a financial nightmare for Texas shippers.

Numerous promises and deadlines made by UP officials to unclog their railways and improve service came too little and too late. While UP cars were backed up on the tracks, Texas businesses were losing an estimated $100 million monthly. To date, economists estimate the problems have cost Texas' economy $1 billion. Meanwhile, solutions offered by the federal Surface Transportation Board, the agency that regulates railroad companies, have been akin to trying to stop the bleeding of a deep wound with bandages. They haven't worked. And the problems for Texas shippers are getting worse, not better.

However, there is a viable solution on the table that offers promise. Conceived by the Texas Railroad Commission, the plan calls for the STB to order UP to divest hundreds of miles of track, including a line running from Houston to Beaumont and expand the operations of a neutral switching railroad, such as the Port Terminal Railroad Association, to handle local traffic in the Houston area.

On the surface, the Railroad Commission's proposal seems fair. The plan offers far more options to Texas' frustrated shippers than UP's monopoly. As well, it keeps the Port of Houston Authority competitive with the Port of New Orleans and other area ports that have capitalized on UP's service problems here.

In considering the Railroad Commission's plan, the STB should also be mindful of the increased trucking traffic resulting from the North American Free Trade Agreement. That traffic is expected to triple. There is no way Texas highways can withstand that 18-wheeler traffic without costly upgrades.

The solution to Houston's clogged railways is apparent: the STB needs to give other railroad carriers more access to UP's tracks. There is general agreement between the major players - the Railroad Commission, the Port Authority, Burlington Northern Santa Fe Railway Co. and Texas Mexican Railway Co. - that something needs to be done to ease the backup. Details of the plan need to be worked out. The bottom line, as Railroad Commission Chairman Charles Matthews pointed out, is that Texas shippers, the business community and citizens deserve nothing less than a fully functional, competitive railroad.

The bottom line is also that a solution is likely to cost shippers and consumers money. But it is likely to cost them far less than the current mess.

---- INDEX REFERENCES ----

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**BEFORE THE**
**SURFACE TRANSPORTATION BOARD**

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**FINANCE DOCKET NO. 33461**
**SOUTHERN PACIFIC TRANSPORTATION COMPANY**
**— TRACKAGE RIGHTS EXEMPTION —**
**HOUSTON BELT & TERMINAL RAILWAY COMPANY**

**FINANCE DOCKET NO. 33462**
**UNION PACIFIC RAILROAD COMPANY**
**— TRACKAGE RIGHTS EXEMPTION --**
**HOUSTON BELT & TERMINAL RAILWAY COMPANY**

**FINANCE DOCKET NO. 33463**
**BURLINGTON NORTHERN AND SANTA FE RAILWAY COMPANY**
**— TRACKAGE RIGHTS EXEMPTION —**
**HOUSTON BELT & TERMINAL RAILWAY COMPANY**

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**VERIFIED STATEMENT**
**OF**
**PATRICK L. WATTS**

My name is Patrick L. Watts. I am the Vice President - Transportation of the Texas Mexican Railway Company ("Tex Mex"), headquartered at 501 Crawford Street, Room 317, Houston, Texas 77002. As the Board is aware, I filed a Verified Statement as part of Tex Mex's *Complaint and Request for Cease and Desist Order*, Finance Docket No. 33507, projecting harm that the dissolution of the Houston Belt & Terminal Railway Company ("HBT") would cause Tex Mex. This statement will highlight only a few of the most recent problems that Tex Mex has, in fact, experienced as a result of the dissolution of the HBT by the Union Pacific Railroad Company ("UP") and the Burlington Northern and Santa Fe Railway Company ("BNSF").

In my Verified Statement in Finance Docket No. 33507, I stated that dissolution of the HBT would cause the Tex Mex irreparable harm; specifically, that "if UP and BNSF are allowed to continue and dissolve HBT, this will further add to the congestion and confusion currently experienced on the Union Pacific system." Everything that I projected in that statement has since come true. Houston continues to be in a near-gridlocked condition. For example, it often takes the Tex Mex 18 to 24 hours to operate a train between Dyersdale Junction and West Junction in Houston, a distance of only approximately 13 ½ miles. Normally, moving a train between those two points should take only 3 hours. Furthermore, we have had many situations where trains will move two miles or less during an entire 12-hour crew shift due to the Houston congestion.

Despite these frequent problems, UP's October 31, 1997 Opposition to Tex Mex's Complaint and Request for Cease and Desist Order contained a Verified Statement from Mr. J. B. Mathis which proclaimed, "[T]his restructuring will benefit every railroad operating through Houston, including Tex Mex, by making train operations through Houston much smoother and faster." That statement has been shown by actual experience to be completely in error. The Tex Mex not only has not seen any improvements, instead it has seen continued increases in congestion and degradation in service levels in the Houston and Gulf Coast areas.

As recently as a few days ago, a westbound Tex Mex train [MSHCPJ-22, Shreveport to Corpus Christi] arrived at Settegast Junction at 11:00 a.m. on Friday, January 23, 1998, and did not depart West Junction until 5:35 a.m. on January 24, 1998. While the MSHCPJ-22 set out some rail cars at Basin Yard and picked up 13 rail cars at Dallerup Yard it still took 18 ½ hours to travel the 13 ½ miles. Under normal circumstances, this move, which includes two work events (set out and pick up of cars) while moving the train just across town, should only take four hours. Obviously, it is not indicative of "smoother and faster" operations through Houston that what should be a four hour movement required more than 18 hours.

In Mr. Mathis' Verified Statement, he said of past HBT dispatching that, "since our [HBT] dispatchers do not know what is happening on UP/SP or BNSF tracks beyond the junction, we have no way of planning our operations to ensure that trains can move smoothly." Even if that was true, HBT still dispatched Tex Mex trains more efficiently than UP now does. Tex Mex trains traveling through Houston have suffered significantly longer delays subsequent to UP's takeover of the dispatching operations in Houston than occurred when HBT dispatched our trains. A prime example occurred on January 27, 1998. Tex Mex's MSHCPJ-27 train arrived at Dyersdale, TX at 5:50 p.m. on the 27th. However, UP trains were tied up without crews on duty and were blocking both mains on the double track. As a result, Tex Mex's MSHCPJ-27 train was delayed at Dyersdale 10 ½ hours.

With the demise of the HBT and the takeover of Basin Yard by the UP, Tex Mex and its customers have encountered numerous other operational problems, including problems interchanging with the PTRA. Prior to the abolition of the HBT, the Tex Mex would set out and pick up cars at Basin Yard. From Basin Yard, the HBT would then interchange Tex Mex cars to the PTRA at PTRA's North Yard, which is immediately adjacent to Basin Yard. (In fact, the PTRA utilized much of HBT's Basin Yard through an agreement between HBT and PTRA.) Because the PTRA and HBT utilized the same computer system called TIES (Terminal Information Exchange System),[1] this set out and pick-up was done efficiently and with few problems. Now, as a result of the UP taking over the HBT and using a different computer system than the PTRA, the pick-up and set out is sporadic and inefficient. Indeed, UP has lost and misrouted numerous cars. For example, there have been instances where

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[1] This shared computer system, which was partially funded through a grant by the FRA in 1979, facilitated switching information between the two terminal switching companies.

loaded Shell Company cars, arriving at Houston via the Tex Mex, are never interchanged to the PTRA and delivered to the customer as they should be. Instead, the cars have been routed back to the origin by UP as empty cars. When these Shell cars arrive back at their origin, shown as an empty but in fact loaded, both Shell and the Tex Mex are harmed. These problems and delays were not experienced when the HBT was still in existence.

Finally, UP's dissolution of the HBT has recently resulted in UP refusing even to allow the Tex Mex to operate over the HBT's East Belt Line in order to interchange with PTRA. UP has claimed that for operational reasons Tex Mex is no longer permitted to operate over the East Belt. Instead, UP directs the Tex Mex over the West Belt Line and requires Tex Mex to set out the PTRA cars it is moving at Congress Yard rather than setting them out at Basin Yard, on the East Belt, where Tex Mex is supposed to interchange them to PTRA. All of the cars which UP has forced the Tex Mex to set out at Congress Yard instead of at Basin Yard are still sitting in Congress Yard and have not been moved by the UP to Basin Yard as originally intended.

The foregoing statement provides only a few of the many examples that illustrate that the benefits of dissolving HBT proclaimed by Mr. Mathis and UP have not been realized. I am attaching to this statement as Appendix 1 a narrative describing some of the many other problems that UP's dissolution of HBT has caused Tex Mex since UP took over HBT's dispatching operations. As the list clearly demonstrates, the problems caused by UP's takeover of HBT are frequent and substantial. Each is more than just an inconvenience; each costs Tex Mex time and money and impedes efficient rail service to Tex Mex's customers. In fact, Tex Mex has suffered a loss of more than $800,000 from additional expenses incurred to date.

UP and Mr. Mathis proclaimed proudly on the eve of UP's dissolution of HBT that the change would cause service in Houston would improve tremendously for all railroads, including Tex Mex. Just the opposite has occurred. Congestion in Houston has gotten worse. Tex Mex's trains have been delayed longer and longer while waiting to enter or leave the Houston terminal area and while waiting for dispatching clearances. If UP continues to plead that its takeover of HBT's dispatching operations has benefited UP operationally, then the UP has clearly been discriminating against the Tex Mex.

## VERIFICATION

STATE OF TEXAS )
) ss.
COUNTY OF )

Patrick L. Watts, being duly sworn, deposes and says that he is the Vice President-Transportation of the Texas Mexican Railway Company; that he has knowledge of the matters contained in the foregoing Petition(s) to Declare Exemptions Void Ab Initio and to Revoke Exemptions; and that the statements made in that Petition are true and correct to the best of his knowledge and belief.

Patrick L. Watts

Patrick L. Watts

Subscribed and sworn to before me this 29 day of January, 1998.

LUPITA A. LLANES
Notary Public, State of Texas
My Commission Expires

Lupita A. Llanes

Notary Republic

STB FD-32760(SUB30) 7-8-98 A ID-189672 

# Proposal For Gulf Coast Service Improvement

The

Burlington Northern and Santa Fe Railway Company

February 4, 1998

# BNSF Gulf Coast Service Proposal
# Issues Addressed

- BNSF goals in addressing service congestion and adding capacity to Houston/Gulf area:
  - Speed up service recovery period for shippers
    - UP's directional running will help, but not quickly enough, to resolve Houston area service/congestion problems for shippers, BNSF and TM
  - Make changes which will prevent a reoccurrence of current congestion problems
    - Provide clear "escape routes" for all carriers
  - Make changes which will permit BNSF and TM to implement effective competitive service for shippers as an alternative to UP post-merger
  - Mutual agreement between carriers to resolve issues is preferable to government intervention

# BNSF Gulf Coast Service Proposal
# Changes In Train Dispatching

- Establish coordinated and joint dispatch functions at a consolidated dispatch center in UP's Spring, TX facility
  - Include UP, BNSF, TM and KCS involvement as appropriate
- Why?
  - Can be done quickly, providing near term relief
  - Will speed up Houston area service recovery period for shippers
  - Provides a long term solution, which can assist in preventing a reoccurrence of current congestion problems
  - Will permit BNSF and TM to provide Houston area shippers with improved competitive options vis-a-vis UP, in line with UP/SP merger conditions

# BNSF Gulf Coast Service Proposal
# Coordinated Dispatch Center

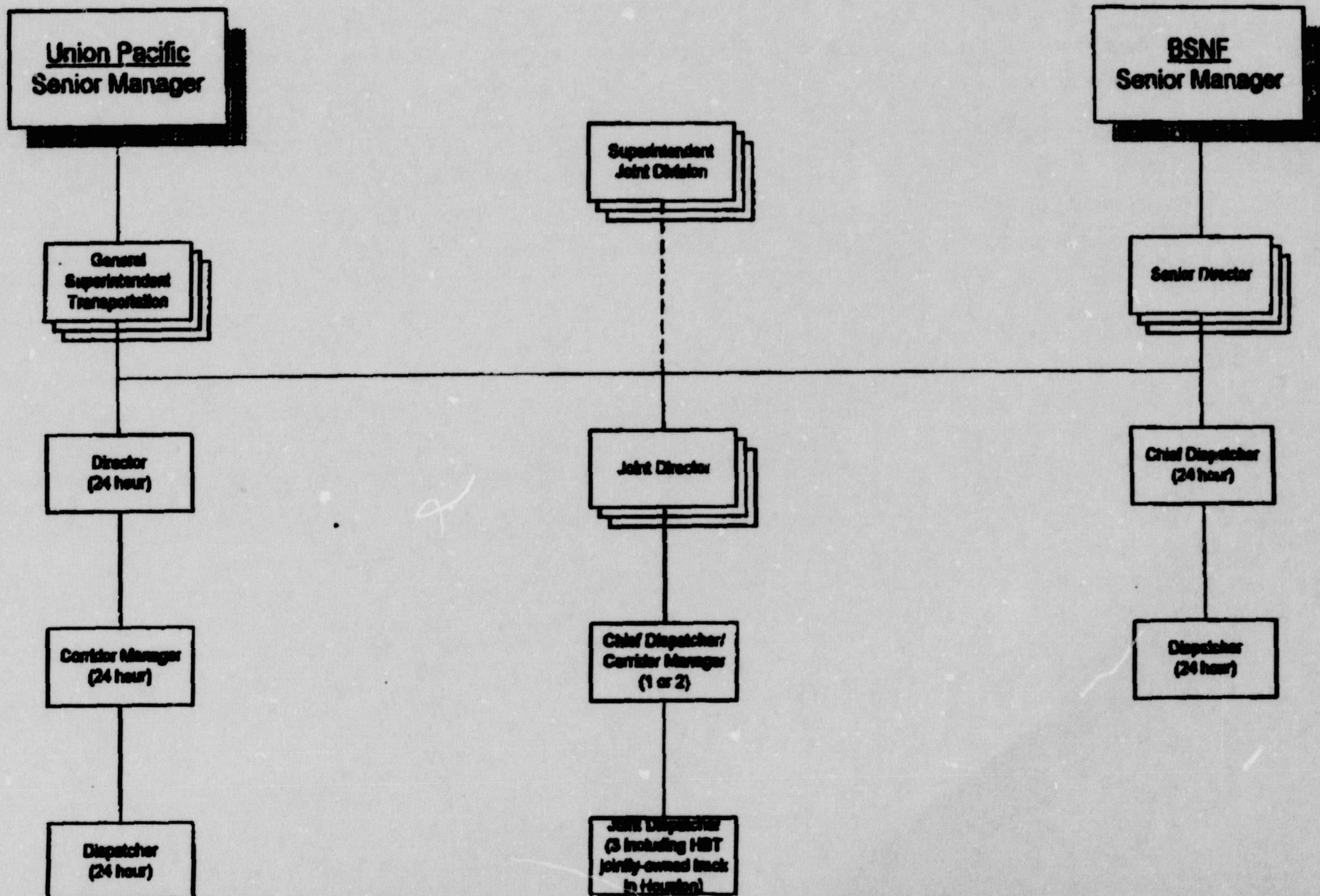
- BNSF and UP, with TM and KCS involvement, would coordinate train dispatch in the Spring Center along the Gulf Coast between Avondale, LA and Brownsville, TX
  - Congestion, service problems for BNSF, TM, and UP have been magnified by lack of dispatch coordination
    - Each carrier is not aware of or linked into what trains other carriers are running into and out of the Texas Gulf shared facilities
    - Results include stalled trains, "dead on the law" crews, idle power, delayed cars, and facilities used for "parking", not running, of trains
- <u>VISION</u>: Carrier owning route will control dispatch, but information exchange between carriers will permit coordination of trains into and out of Houston terminals, promoting movement and preventing congestion

# BNSF Gulf Coast Service Proposal
# Joint Dispatch Plan

- BNSF and UP, with TM involvement, would jointly manage a neutral dispatching function in the Spring Center for specific critical routes the carriers jointly use in providing quality service to Houston area shippers
- Involved routes:
  - UP and SP routes, Houston-Beaumont, TX
  - UP's SP route, Beaumont-Iowa Junction, LA
  - BNSF route, Iowa Junction-Avondale, LA
  - HBT East and West Belts
  - PTRA, now dispatched from Harriman Center, Omaha
- Joint Division Superintendent equally accountable to BNSF and UP Needs to be TM also

# Consolidated Dispatching Center

## Preliminary Proposal



# BNSF Gulf Coast Service Proposal
# How Will Shippers Be Impacted?

- Proposal can provide for nearterm relief and results, in response to current problems
- Improved transit times and service consistency on all carriers through better coordination on movements into, out of the Houston/Gulf Coast area
- Customers can begin returning business to rail handling now diverted to other modes, saving money
- Customers can begin trimming private car fleets as service levels come back to historical (or better) levels, compared with last nine months, further reducing costs to shippers and congestion for carriers

# BNSF Gulf Coast Service Proposal
# Achievable Implementation Timeline

- Coordinated and Joint dispatching center at Spring can be implemented within 30 days
  - STB approval is not needed

# BNSF Gulf Coast Service Proposal
# Next Steps

- BNSF and UP met on January 26, 29, and February 2 to discuss the dispatch proposals, with general agreement on their direction
  - Initial benefits of a consolidated dispatch center at Spring could begin being realized within 30 days of agreement
- Other issues to be resolved:
  - BNSF and UP are discussing proposals for joint operation of Houston-Avondale route
    - Structure of joint operations, including dispatch
    - Providing a "neutral" switching service between customers' facilities and roadhaul BNSF, UP trains for those customers accessible to both carriers

# BNSF Gulf Coast Service Proposal
# How Will TexMex Be Impacted?

- January 21 RCT Houston Meeting: TexMex Requests
  - Clear routes through Houston
    - Addressed by Coordinated Dispatch proposal, which anticipates TexMex involvement
  - Membership on PTRA Board
    - BNSF would support, along with membership by Houston Port Authority
  - Access to Houston Yard capacity
    - BNSF does not have yard space to provide TexMex at South Yard
    - View as issue between TexMex and UP

BNSF

ROBERT D. KREBS
*Chairman, President and*
*Chief Executive Officer*

**Burlington Northern Santa Fe Corporation**

PO Box 961052
Fort Worth TX 76161-0052
2650 Lou Menk Drive 2nd Floor
Fort Worth TX 76131-2830
817-352-6400
817-352-7100 Fax

February 6, 1998

Mr. Richard K. Davidson
Chairman
Union Pacific Corporation
1717 Main Street
Suite 5900
Dallas, TX 75201-4605

Dear Dick:

I have reviewed the proposal that was forwarded with your letter of February 4. I am sorry to say that it does not adequately address the concerns we have voiced in our recent meetings regarding BNSF's inability to compete for traffic in the Gulf area; nor does it go far enough toward solving the service problems in the Gulf that are plaguing both BNSF's and UP's customers.

I agree that it is desirable to establish a central dispatching office controlling BNSF and UP lines in and around Houston, with a provision for the key lines used by us both, including the Houston Belt & Terminal and PTRA, to be handled by a neutral party reporting jointly to us. This, together with a formalized arrangement for us to directly receive cars originating on the southern side of the Houston ship channel, should help to reduce congestion in the Houston area and should improve the service that both of us provide to our customers.

As we told you when we met, we also believe that significant changes to the operations pertaining to the former SP Houston to New Orleans line are necessary if we both are to meet our customers' expectations, and if BNSF, in particular, is to be able to keep the promise we made regarding our ability to compete for traffic when we supported your merger. Your proposal, which calls for BNSF and UP to swap interests in our respective lines resulting in a 50/50 interest between Dawes and Avondale, is in line with our discussions. However, the description of how the lines would be operated is contrary to the principle of true joint control that we discussed. It has become clear to us over the last year that BNSF must have an equal say in the way operations are structured and carried out in order to attract and properly service customers on this line. It is also clear that we will never be on an equal footing unless we are able to offer service to all industries, just as you do today. We have offered to pay a reciprocal switch charge for cars handled to and from industries between Houston and Iowa Junction at all locations on the former SP main line and branches that were not included in the merger conditions as "two to one" points. As you know, reciprocal switching agreements are commonplace throughout our industry and can be established quickly.

As we explained at our meeting earlier this week, the true joint facility arrangement that we proposed for the Houston/Avondale line puts BNSF at a considerable financial disadvantage. The revenues we will lose by the elimination of the millage rate presently paid by UP for using our track between Iowa Junction and Avondale are far greater than our millage rate payments to you between Houston and Iowa Junction. We are agreeable to being disadvantaged initially because we believe this is the only type of operation that will take care of all our customers, and because we hope, over time, that BNSF will successfully attract enough business to make up for the lost millage revenue.

You and I have been talking about joint dispatching and operating concepts in one form or another since November. In the meantime, we have seen no material improvement in the operations in Houston and along the Gulf Coast. Because of UP's congestion and dispatching problems, shippers continue to suffer from both of our railroads' inabilities to provide reasonable service. Using the format that you included with your letter, I have attached an outline of what I believe to be the best way for us to fix the service problems. We are anxious to work out the details to implement the dispatching and operating improvements as soon as possible. My understanding is that we can do this without reopening your merger case, and if we can reach agreement, we are ready to put as much of the proposal as we can in place next month when we know traffic will pick up.

We now have enough experience to conclude that the present arrangements, due to the congestion and unique characteristics of Houston and the Gulf Coast area, will not work. If we cannot reach an agreement that closely parallels our proposal, we will most likely ask the STB to reopen your merger case and to order divestiture of the eastern portion of the SP system. This is not our preferred outcome, because it puts at risk the rights that we negotiated as part of your original case. However, if we do not make substantial progress next week, I intend to raise this possibility at the National Industrial Transportation League meeting in Houston next Friday.

Sincerely,

Enclosure

## BNSF PROPOSAL FOR JOINT OWNERSHIP AND DISPATCHING

1. UP and BNSF swap interests in their respective lines, with each party having a 50 percent interest in the main line, sidings and Dayton, Beaumont, Echo, Lake Charles, Lafayette and Avondale yards on the former SP Lafayette Subdivision between Dawes (MP 352.8) and West Bridge Junction (MP 10.5).

2. BNSF grants UP overhead trackage rights between Beaumont and Navasota, with rights to enter/exit at Navasota, Cleveland and Conroe, at the same mill rate contained in the BNSF Settlement Agreement. BNSF and UP will agree on a formula for UP capital contribution to improvements to this route based upon the number of trains operated by UP across the line.

3. All local industries on the line between Dawes and Avondale and on former SP branches connecting to the line not presently open to both parties will be opened subject to the customary reciprocal switching charge in the area, paid into the joint facility.

4. Neither BNSF nor UP can admit a third party or provide haulage without the other's approval on the 50/50 lines.

5. On the 50/50 lines, capital additions and betterments, maintenance capital (track replacement), ordinary maintenance, and operations will be split on a usage basis.

6. BNSF and UP agree on a consolidated regional dispatching center encompassing BNSF, UP, HB&T and PTRA lines, and including KCS and Tex-Mex participation as appropriate.

7. Field management of the 50/50 lines will be done on a neutral basis, with the manager in charge reporting equally to designated UP and BNSF representatives.

8. BNSF and UP agree to establish reasonable joint service standards, including a joint service standards committee, on the 50/50 lines.

9. Local switching and terminal operations on the 50/50 lines will continue to be performed by BNSF and UP personnel. They, however, will report to the neutral management in charge of the line.

10. Through trains will use owner crews and remain in the owner's account.

COVINGTON & BURLING
1201 PENNSYLVANIA AVENUE, N. W.
P.O. BOX 7566
WASHINGTON, D.C. 20044-7566
(202) 662-6000

FACSIMILE: (202) 662-6291

LECONFIELD HOUSE
CURZON STREET
LONDON W1Y 8AS
ENGLAND
TELEPHONE: 44-171-495-5655
FACSIMILE: 44-171-495-3101

BRUSSELS OFFICE
KUNSTLAAN 44 AVENUE DES ARTS
BRUSSELS 1040 BELGIUM
TELEPHONE: 32-2-549-5230
FACSIMILE: 32-2-502-1598

ARVID E. ROACH II
DIRECT DIAL NUMBER
(202) 662-5388
DIRECT FACSIMILE
(202) 778-5388

February 18, 1998

BY HAND

Hon. Vernon A. Williams
Secretary
Surface Transportation Board
Room 711
1925 K Street, N.W.
Washington, D.C. 20423-0001

Re: Service Order No. 1518

Dear Secretary Williams:

Since late last year, Union Pacific has been discussing with Burlington Northern Santa Fe the importance of creating a true joint dispatching center for UP and BNSF lines in Houston and in the areas surrounding Houston -- including the lines between Houston and New Orleans -- with unified personnel, unified technology, and full access by the joint dispatchers to information about the movements of the trains of both railroads. Last Thursday, UP and BNSF reached agreement on the establishment of such a joint dispatching center. A copy of the parties' agreement is attached hereto.

The agreement involves a number of elements of mutual, agreed-upon consideration:

First, as noted, BNSF has agreed to enter into the joint dispatching center, encompassing all the BNSF and UP/SP rail lines highlighted on the map attached to the agreement. Tex Mex and KCS are also welcome to participate, and it would be very helpful if they would; UP has repeatedly urged them to do so, but thus far they have refused.

Second, BNSF will grant UP overhead trackage rights over the BNSF line between Beaumont and Navasota, Texas, with the additional right to enter and exit at Cleveland and Conroe, Texas. This will improve Houston-area rail operations by allowing UP to bypass the Houston terminal for trains moving between points north and east of Houston.

Third, the parties will "swap" 50% ownership interests in (a) BNSF's former-SP line between Iowa Junction and Avondale, Louisiana, which BNSF purchased in 1996 as part of the UP/SP-BNSF settlement agreement in the UP/SP merger case, and (b) UP/SP's adjoining former-SP line between Houston and Iowa Junction, and will manage and operate this overall through line in much the same fashion that they do with joint facilities in the Powder River Basin. This will, among other things, resolve problems of lack of coordination in the imposition of "maintenance windows" on this line, which, in UP's view, have contributed significantly to UP's service problems.

Fourth, as an incident to BNSF's acquisition of a half interest in the former-SP Houston-Iowa Junction segment, and appurtenant branches, shippers that had been exclusively served by UP will be opened to service by BNSF. This involves more than 70 shipper facilities and some $40 million in annual gross revenues.

Fifth, the agreement clarifies limitations on UP's liability for expenditures that have been and may in the future be made to upgrade the Iowa Junction-Avondale line to the standard that was agreed upon in the 1996 sale agreement. BNSF had contended that the sale-agreement standard had not been complied with, and UP had strongly disagreed with this contention. That dispute has now been fully resolved.

We are frank to say that UP entered into this agreement with reluctance. Granting BNSF the right to serve all shipper facilities on the Houston-Iowa Junction line and appurtenant branches (including the Dayton and Port Arthur branches) will be costly, and was absolutely not justified by any competitive impact of the UP/SP merger or any issue with regard to BNSF's clear competitiveness under its merger-case trackage rights. But UP concluded that this significant commercial concession was warranted by the overriding need to coordinate and improve BNSF and UP operations in the Houston area, including achieving optimally efficient operation of an integrated line between Houston and New Orleans.

The Houston/Gulf congestion problem has proven more severe and intractable than anyone imagined when it emerged last year. It is now clear that the railroad physical plant in the Houston/Gulf area -- and particularly the SP plant -- is taxed to its limit by the high traffic volumes and complex switching requirements of the chemical and other customers in this area. As the Board recognized in the Decision it served yesterday in this docket, much of the solution to this problem lies with the continuing attainment of the efficiencies of the UP/SP merger. UP has now completed the complex processes of (a) arriving at Houston-hub and associated labor implementing agreements, (b) implementing UP's TCS computer system on SP lines in the Houston/Gulf area, and (c) implementing directional running between Houston and Memphis. Each of these transitions has been difficult and has caused interim disruptions -- indeed, the transition to smooth directional running is still underway -- but their ultimate result will unquestionably be a tremendous improvement in operations. There is also an urgent ongoing need for capital investments in the area, and UP has committed more than $570 million to that end during this year and next year. But in addition to all these essential steps, UP concluded that joint dispatching was also a critical element in reaching a clear assurance that the congestion problems in this area will be overcome.

Parts of the UP-BNSF agreement will go into effect without any need for Board action. These include the joint dispatching, which will be implemented as soon as the necessary technology can be put in place and the necessary training completed, and no later than 30 days from February 12; the opening of all industries on the Houston-Iowa Junction line and appurtenant branches to BNSF, which will go into effect as soon as practical, and, again, in all events within no more than 30 days from February 12; and the resolution of the dispute as to UP's liability for expenditures to upgrade the Iowa Junction-Avondale line, which is also effective immediately. The Beaumont-Navasota trackage rights will be the subject of a class exemption, to be filed shortly. Finally, the ownership "swap" will require Board action, and the parties expect to file an appropriate joint request for such action in the near future.

UP's entry into this agreement demonstrates its profound commitment to do whatever is necessary to overcome the service crisis which, since last fall, has affected the Houston-area rail system -- and indeed, for parts of the period, much of the West. We are confident that we are now on track to completely overcoming that unprecedented and extraordinarily persistent and difficult crisis.

Sincerely,

Arvid E. Roach

Arvid E. Roach II

Attorney for Union Pacific Railroad Company

cc: Hon. Linda J. Morgan (courtesy copy)
Hon. Gus A. Owen (courtesy copy)
Melvin F. Clemens, Jr., Director, Office of Compliance and Enforcement (courtesy copy)
All Parties of Record

# TERM SHEET AGREEMENT
# COVERING OWNERSHIP AND OPERATION
# OF LINES IN AND AROUND HOUSTON, TX

## I. GENERAL CONCEPT

1. UP and BNSF agree that they will jointly own and operate the former SP Lafayette Subdivision between Dawes (MP 352.8) and Avondale (MP 14.9) (the "50/50 Line"), on a basis similar to that found in the Powder River Basin Agreement except for dispatching. Trackage between MP 14.9 and 10.5 owned by UP and by BNSF shall be jointly dispatched and used by both parties without charge but otherwise shall be subject to typical joint facility provisions.

2. BNSF will grant UP overhead trackage rights between Beaumont and Navasota.

## II. SPECIFIC TERMS COVERING JOINT OWNERSHIP AND DISPATCHING OF FORMER LAFAYETTE SUB

1. UP and BNSF will exchange 50 percent interests in their respective main lines, including operating sidings used for meeting and passing trains, which constitute the former SP Lafayette Subdivision, with each party having a 50 percent interest in the resulting operating corridor. A listing of such operating sidings is provided at Exhibit A.

2. It is the intention of the parties that UP and BNSF shall have the right to serve all present and future industries or facilities originating or terminating traffic on the 50/50 Line and on former SP branches and spurs connecting to the 50/50 Line or any new branches or spurs connecting to these lines. These industries and facilities shall be open to BNSF on the same basis that BNSF serves "2-to-1" customers per Section 5 of the Settlement Agreement, as amended and supplemented, or on a haulage basis for the fee called for in Section 8j of the Settlement Agreement, and calculated as shown on the Example attached as Exhibit B.

3. Except for existing rights, neither BNSF nor UP can admit a third party or provide haulage without the other's approval on the 50/50 Line; provided, however, that either party may use the Louisiana & Delta Railroad as its agent to provide service over the 50/50 Line without obtaining the approval of the other party. As of the date hereof, UP shall not impose or enforce any requirement (a) contained in any agreement entered into after execution of

the Settlement Agreement and (b) covering traffic which BNSF had access to under the terms of the Settlement Agreement, that the L&DRR pay any additional rental or other fee if traffic is routed via BNSF.

4. On the 50/50 Line, capital additions and betterments will be split on a user (i.e., 50/50) basis, and maintenance capital (track replacement), ordinary maintenance, and operations will be split on an annualized usage basis (gross ton miles). Except as to capital additions and betterments agreed to by the parties prior to the date of this Term Sheet Agreement as payable out of the Capital Improvements Fund established by the Settlement Agreement, capital additions and betterments will be subject to the mutual agreement of the parties in the same manner as they are agreed to under procedures established in the Powder River Basin Agreement.

5. Capital costs of projects which benefit only one party shall be paid for solely by such party. If, for any reason, the other party desires to use such facility it will pay 50% of the actual cost plus interest.

6. Exchange is subject to TexMex' existing trackage rights. TexMex trackage rights charges shall be paid to UP for UP's sole benefit. TexMex usage of the line shall be considered UP usage for purposes of allocating liability, calculating UP and BNSF's respective usage shares, etc. The parties' contracts with Amtrak shall not be affected by this Term Sheet Agreement. Amtrak usage of the 50/50 Line shall be considered the usage of the respective owner of the segment in question prior to the exchange of ownership for all purposes including, but not limited to, compensation, liability, and all other provisions of the parties' respective contracts with Amtrak.

7. BNSF and UP agree on a consolidated regional dispatching center encompassing BNSF, UP, HB&T and PTRA (between Bridge 5A and Deer Park) lines, and including KCS and TexMex participation as appropriate, as described in Exhibit C.

8. Field management, facility maintenance, and improvements to the 50/50 Line will continue to be performed by UP or BNSF on segments each owned prior to the exchange of ownership.

9. BNSF and UP agree to establish reasonable joint service standards, including a joint service standards committee for operations pursuant to this Term Sheet Agreement.

10. UP shall not be required to pay for any expenditures made by BNSF to meet the line condition standard in Section 10c of the Settlement Agreement and Section 6(b) of the Purchase and Sale Agreement up to the amount in the escrow account (principal of $10.5 million plus interest). After the expenditures equal the amount in the escrow account, further expenditures shall be allocated pursuant to this Term Sheet Agreement. The cash and interest in the escrow account will be divided between the parties pursuant to their agreement settling the dispute over the condition of the Iowa Jct. to Avondale segment of the 50/50 Line.

## III. SPECIFIC TERMS COVERING BEAUMONT-NAVASOTA TRACKAGE RIGHTS

1. BNSF will grant UP overhead trackage rights between Beaumont and Navasota at the same mill rate and the same general terms as provided for such trackage rights in the Settlement Agreement.

2. UP shall have the right to enter/exit at Cleveland and Conroe.

3. UP will make capital contributions to capacity related improvements to the trackage rights line on a usage basis (gross ton miles).

## IV. STRANG/PASADENA INTERCHANGE

1. UP shall continue interchange of traffic originating between Sinco and Bayport through the PTRA at Pasadena for movement by BNSF. BNSF will be responsible for PTRA charges resulting from this service. The parties agree to reconsider this issue in 6 to 8 weeks after UP's directional operations and terminal changes are in place and operational. The adequacy of interchange service provided subsequent to the reinstatement of the prior interchange after such reconsideration shall be subject to review by the Service Standards Committee. The Pasadena interchange shall be reinstated in the event the Service Standards Committee finds that interchange service standards have not been met for a reasonable period of time.

## V. OTHER

1. The parties agree to cooperate with each other and make and prosecute diligently whatever filing or applications, if any, are necessary to implement the provisions of this Term Sheet Agreement.

2. The parties agree to use their best efforts to promptly complete definitive agreements reflecting the intent and provisions of this Term Sheet Agreement.

3. Unresolved disputes and controversies concerning any of the terms and provisions of this Term Sheet Agreement shall be submitted for binding arbitration under Commercial Arbitration Rules of the American Arbitration Association which shall be the exclusive remedy of the parties.

4. The provisions of Section II.2, Industry Access, Section II.7, Joint Dispatching Center, and Section III, Beaumont-Navasota Trackage Rights, shall be effective and implementation shall begin as soon as practical but no later than 30 days from execution, and remain in effect thereafter, and the remaining provisions of this Term Sheet Agreement shall be implemented as soon as possible upon receipt of required governmental approval or exemption, if any.

5. The parties intend that the undertakings in this Term Sheet Agreement constitute legally enforceable obligations.

AGREED TO:

UNION PACIFIC RAILROAD COMPANY

By: James V Dolan
Title: Vice President - LAW
Date: Feb 12 1998

THE BURLINGTON NORTHERN AND SANTA FE RAILWAY COMPANY

By:____________________
Title:____________________
Date:____________________

2. The parties agree to use their best efforts to promptly complete definitive agreements reflecting the intent and provisions of this Term Sheet Agreement.

3. Unresolved disputes and controversies concerning any of the terms and provisions of this Term Sheet Agreement shall be submitted for binding arbitration under Commercial Arbitration Rules of the American Arbitration Association which shall be the exclusive remedy of the parties.

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5. The parties intend that the undertakings in this Term Sheet Agreement constitute legally enforceable obligations.

AGREED TO:

UNION PACIFIC RAILROAD COMPANY

By:____________________
Title:____________________
Date:____________________

THE BURLINGTON NORTHERN AND SANTA FE RAILWAY COMPANY

By: [signature]
Title: Vice President, UP/SP Lines
Date: February 12, 1998



RECEIVED TIMEFEB. 12. 6:26PM PRINT TIMEFEB. 12. 6:27PM

FEB 13 '98 08:54

# EXHIBIT A
## OPERATING SIDINGS

I. **BNSF Segment**

(a) Salix
(b) Raceland Jct.
(c) Schriever
(d) Berwick
(e) Bayou Sale
(f) Baldwin
(g) New Iberia
(h) Cade
(i) Lafayette (only track 902, not Lafayette yard)
(j) Crowley Siding
(k) Midland
(l) Roanoke

II. **UP Segment**

(a) Fauna
(b) Crosby
(c) Dayton
(d) Ames
(e) Devers
(f) China
(g) Connell
(h) Francis
(i) N. Echo
(j) S. Echo
(k) Brimstone
(l) Lockmore
(m) Iowa Siding (to be constructed)

**EXHIBIT B***

| Between: | Mileage | Roundtrip | Charges<br>On/Off+Miles+Recip=Total/Car |
|---|---|---|---|
| Origin and Destination | 15 | 30 | $100 + $15 + $130 = $245 |
| Reciprocal Switch (per load) within Switching District | -- | -- | NA + NA + $130 = $130 |

* Provided for illustrative purposes only. Charges subject to annual adjustment in accordance with the Settlement Agreement.

# Exhibit C

**Consolidated Dispatching Center**

a) The lines to be dispatched by the Consolidated Dispatching Center are shown on the map attached hereto. Each railroad will control, manage and dispatch its own lines and the 50/50 Line will be dispatched jointly. BNSF shall be provided necessary office space and facilities in the Consolidated Dispatch Center.

b) See attached organizational chart for management structure.

c) A Joint Director, reporting to Service Standards Committee, will be retained by UP and BNSF's respective Vice Presidents-Transportation. Each railroad shall submit the names of two potential candidates and then mutually agree on the person to fill the position. BNSF and UP will mutually agree upon a process to change the Joint Director which permits either to remove the incumbent. The parties shall agree upon a written description of the Joint Director's job duties, two of which will include responsibility for ensuring compliance with (1) dispatching protocol standards and (2) standards for the gathering and distribution of cars to/from industries on the 50/50 Line, former SP branches and spurs, to either railroad. The Joint Director's job description and performance shall be reviewed/evaluated periodically by both railroads. Either railroad shall have the right to remove the Joint Director at its sole discretion.

d) Until UP implements CAD III, UP will support its dispatching using Digacon. UP's server is located in Omaha and during emergency outages UP will take control of its lines and the 50/50 Line from Omaha. During emergency outages BNSF will control its lines from Ft. Worth.

e) BNSF and UP agree that KCS/Tex Mex should be offered the opportunity to dispatch their lines in the Gulf Coast area from the Consolidated Dispatching Center.

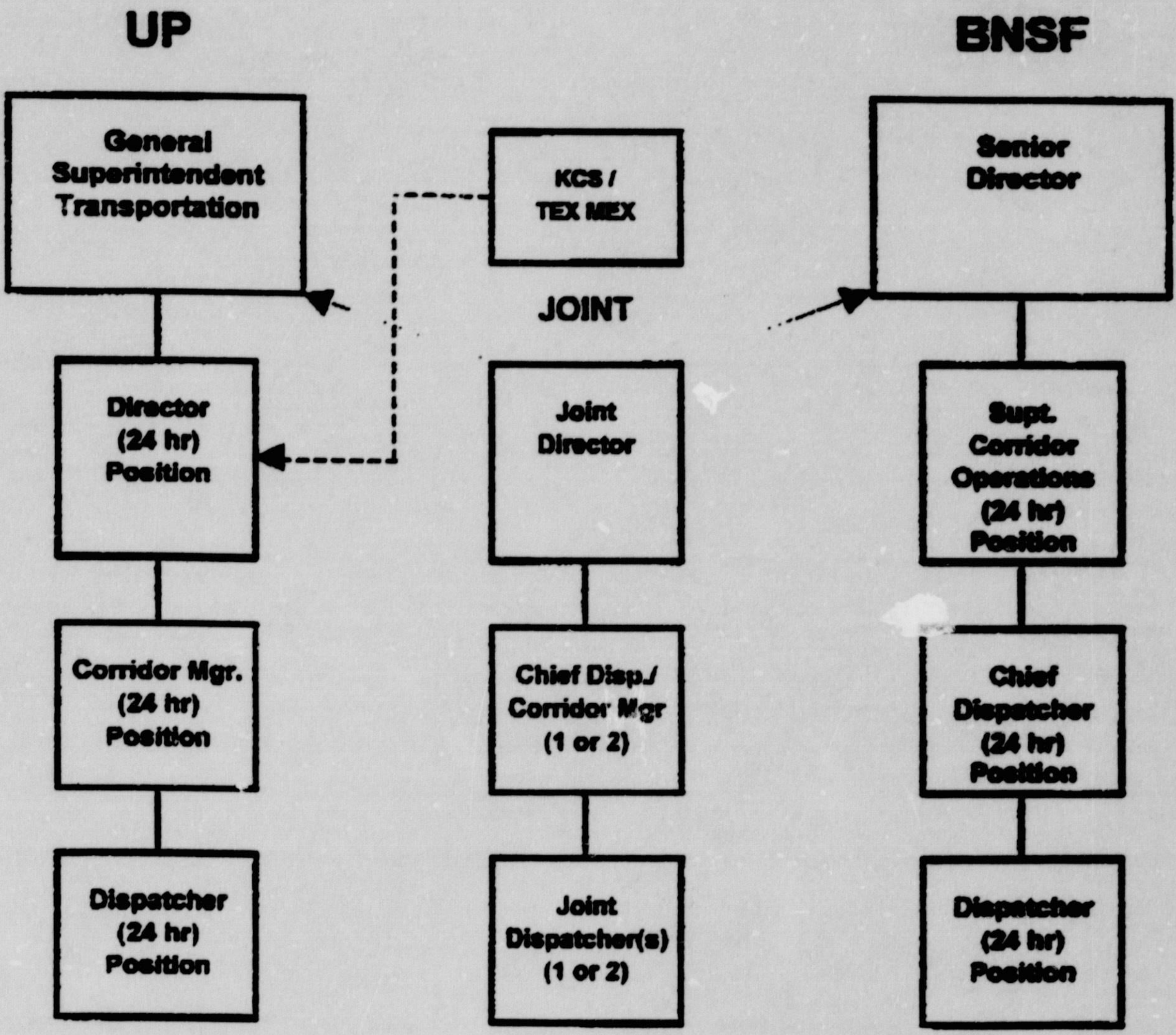
f) Cost allocation shall be subject to customary joint facility arrangements.

g) Consolidated Dispatching Center will be located in the first floor of UP's Spring, Texas, regional offices. UP will develop and furnish proposed office layout.

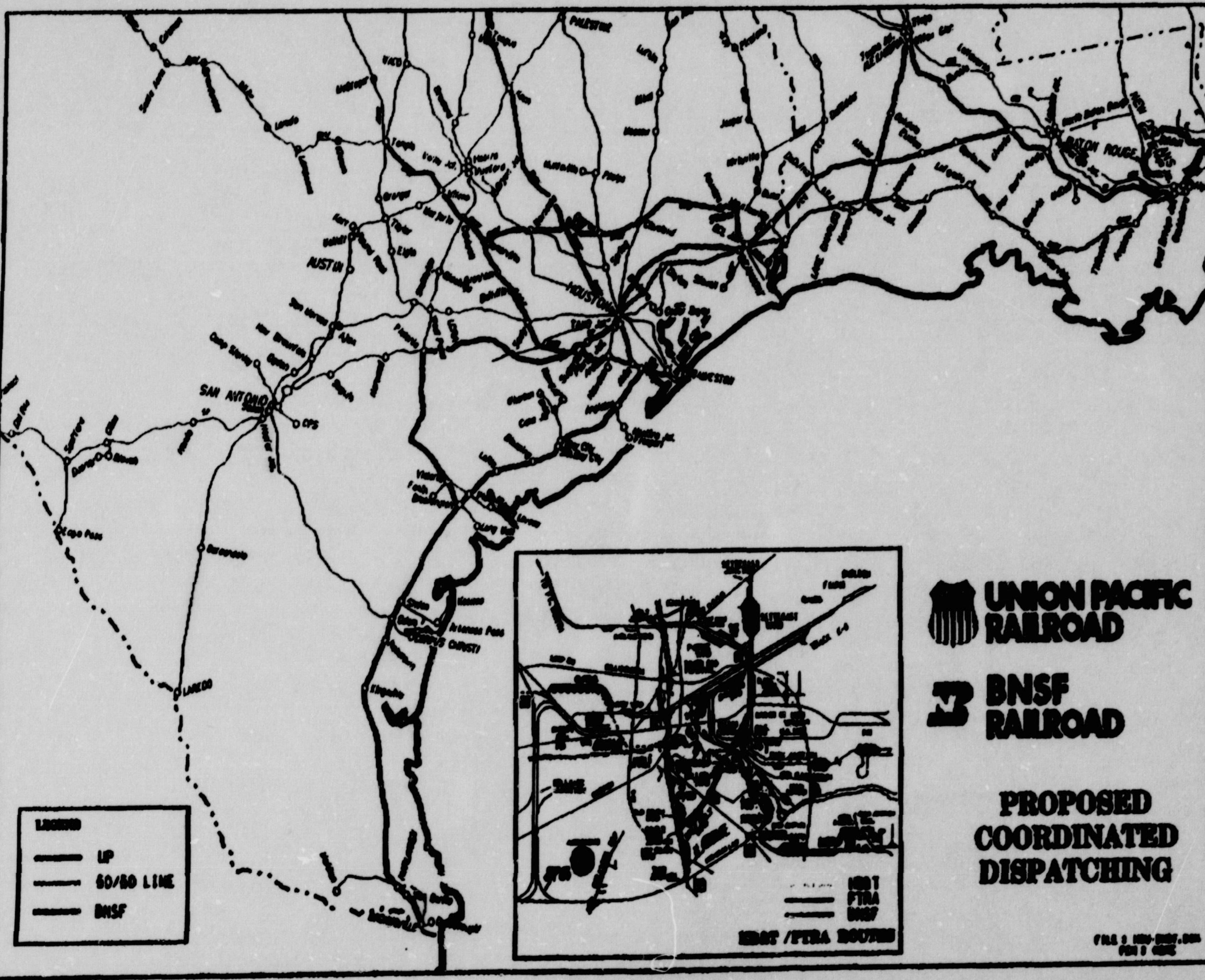
# CONSOLIDATED DISPATCHING CENTER

## HOUSTON, Texas

### Organization Chart




February 12, 1996


UNION PACIFIC RAILROAD
BNSF RAILROAD
PROPOSED COORDINATED DISPATCHING
LEGEND
UP
50/50 LINE
BNSF
SAN ANTONIO
AUSTIN
HOUSTON
BATON ROUGE
CORPUS CHRISTI
LAREDO
PALESTINE
WACO
Eagle Pass
Victoria
Aransas Pass
Temple
Taylor
Elgin
CPS

**Greater Houston Partnership** **March 3, 1998**

## Resolution of the Board of Directors To Resolve Houston's Current and Future Freight Rail Service Issues

### *Statement of Position*

The Board of Directors of the Greater Houston Partnership insists on immediate, bold and meaningful action by the Surface Transportation Board to resolve the current rail service crisis gripping much of the Houston-Gulf Coast and causing continuing, devastating impact on the economy and business community.

We conclude from all available information on the issue that the current service disruptions may not be satisfactorily resolved among the participants in the best long term interests of the Houston area unless the Surface Transportation Board indicates an interest in acting swiftly and forcefully.

The freight rail service failures have caused obvious and significant threats to the Houston economy, the competitiveness of its industry and port and raise serious concerns about the future capacity of the rail system to adequately and efficiently support the expansion of the Gulf Coast economy and the hundreds of millions dollars in public and private investments in infrastructure and commerce.

### *Criteria for Freight Rail Service*

The Greater Houston Partnership recommendations for improved near term and long term freight rail services are based upon the following principles:

1. The performance of the freight rail system in the Houston Gulf Coast international port/industrial complex must be in the top tier of United States cities, equal to that provided to the nation's west and east coasts. The system must offer "best in class" competitive value and costs; train speeds, flows and intermodal connectivity; operational safety; responsiveness and reliability.

2. Rail system operators must have the financial, physical and logistical ability to expand system capacity to accommodate economic growth and the resulting shipping needs of the Houston port/industrial complex.

3. Rail system operators in the Houston complex must have the resource capabilities to respond to changing industry mixes and changing distribution patterns.

### *Recommendation—Short Term*

Using these principles, the Greater Houston Partnership recommends the following actions be taken immediately to address the near-term freight rail service problems:

### *Recommendation—Long Term*

The Greater Houston Partnership is greatly concerned with the ability of the freight rail system to adequately accommodate the longer term needs of the community resulting from industrial expansion. With a strong sense of the need to respect property rights and with a firm belief in the long term benefits of competition, the Greater Houston Partnership recommends the Surface Transportation Board take the following steps:

1. The Surface Transportation Board should order all railroads involved, working with affected parties, to determine and implement the most effective approach to providing a neutral switch operation in as large an area as is practical.

2. The Surface Transportation Board should assure that the rail system service for the Houston metropolitan area is designed to attract adequate investment to expand capacity to serve our growing market.

3. The Greater Houston Partnership calls for the creation of a regional freight rail facilities and services master plan to help guide development in the best interest of shippers and the community at large. This master plan should identify and propose resolutions to all of the multi-modal interface issues and seek to maximize freight rail service for the Port and industrial areas of the community.

UNION PACIFIC RAILROAD

NEWS RELEASE

Communications Dept.
1416 Dodge Street
Omaha, NE 68179
(402) 271-3475

# Union Pacific, Burlington Northern Santa Fe Open Joint Dispatching Center

Contact: Jim Sabourin (BNSF)
(817-352-6412)

John Bromley (UP)
(402-271-3475)

**UNION PACIFIC, BURLINGTON NORTHERN SANTA FE OPEN JOINT DISPATCHING CENTER**

**SPRING, Texas, March 13, 1998** -- The Burlington Northern and Santa Fe Railway Company (BNSF) and Union Pacific Railroad (UP) today announced that a joint regional dispatching center for Gulf Coast operations will begin operating Sunday, March 15, in Spring, a Houston suburb.

The center will control train operations between Houston and New Orleans over more than 340 miles of track to be jointly owned by both railroads, as well as main line trackage formerly operated by the Houston Belt & Terminal Railroad and a portion of the Port Terminal Railroad Association in Houston. The center is designed to improve coordination of train operations and communication among all the railroads serving the Houston area, as well as improve the efficiency of yards serving the area.

UP and BNSF agreed Feb. 13 to establish the joint dispatching center and to exchange half interests in the two pieces of the former Southern Pacific line between Houston and New Orleans. As part of the agreement, both railroads will now have access to all customers, including chemical, steel, gas and other companies, along the entire line, including former SP branch lines and spurs along the route. The agreement carries out the Surface Transportation Board mandate that railroads operating in the Houston area work together to find joint solutions to rail congestion problems of the last several months.

W. T. Slinkard of Denver, CO, a former Southern Pacific train management officer, has been appointed to supervise the center as the neutral joint director. Reporting to Slinkard will be four corridor managers, two from UP, and two from BNSF as well as two supervisors of terminal operations and two train dispatcher territories, one each from UP and BNSF. The train dispatchers will all be located in the same room, operating from the same system. They will be located in Spring, currently the location of UP's southern regional office and Houston Command Center.

In conjunction with the joint dispatching center, a consolidated dispatching center will be established at Spring where UP and BNSF dispatchers will control their respective lines along the entire Gulf Coast region from New Orleans through Houston to Brownsville and radiating north and south from Houston. Provisions have also been made for Texas Mexican Railway dispatchers to operate out of the consolidated center, which is expected to begin operating by the end of April. Coordination with the joint dispatching center should further assist in expediting Gulf Coast train operations.

Union Pacific is filling its dispatching positions with personnel from its Omaha Harriman Dispatching Center. Similarly, about 20 dispatchers from BNSF's Network Operations Center in Fort Worth will be relocating to Spring. BNSF and the American Train Dispatchers Department of the Brotherhood of Locomotives Engineers reached a cooperative agreement that permitted the dispatchers to transfer. Dispatchers from both the Houston Belt & Terminal Railroad and the Port Terminal Railroad Association will be located at the center also.

To help further ease the congestion along the Gulf Coast, BNSF is leasing 15 high horsepower and 15 medium horsepower locomotives to UP to be used in service beginning March 15 between Houston and New Orleans, and between Houston and Pine Bluff, AR. While UP anticipates leasing the locomotives for several months, the temporary loss of these units is not expected to adversely impact BNSF service.

-0-

news releases | safety news | speeches | update line

UNION PACIFIC RAILROAD

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COVINGTON & BURLING
1201 PENNSYLVANIA AVENUE, N. W.
P.O. BOX 7566
WASHINGTON, D.C. 20044-7566
(202) 662-6000

FACSIMILE (202) 662-6291

J. MICHAEL HEMMER
DIRECT DIAL NUMBER
(202) 662-5578

DIRECT FACSIMILE NUMBER
(202) 778-5578

mhemmer@cov.com

LECONFIELD HOUSE
CURZON STREET
LONDON W1Y 8AS
ENGLAND
TELEPHONE: 44-171-495-5655
FACSIMILE: 44-171-495-3101

KUNSTLAAN 44 AVENUE DES ARTS
BRUSSELS 1040 BELGIUM
TELEPHONE: 32-2-549-5230
FACSIMILE: 32-2-502-1598

March 16, 1998

***HAND DELIVERY***

The Honorable Vernon A. Williams
Secretary
Surface Transportation Board
1925 K Street, N.W.
Mercury Building, Room 711
Washington, D.C. 20423-0001

Re: Ex Parte No. 573, Rail Service in the Western United States

Dear Mr. Williams:

Enclosed is the twenty-second weekly report of indicators of Union Pacific's service recovery efforts. Except as noted, the data are seven-day averages through the week ending March 13, 1998. The detailed Coal Report and the Major Terminal Processing Report are being provided under seal to the Board and will be provided to parties to the proceeding upon their entering into appropriate confidentiality agreements.

As we predicted in last week's letter, Union Pacific's overall service level was adversely affected this week by the Midwest blizzard, by a huge backlog of traffic for the Laredo Gateway and by torrential rains and service interruptions on CSX east of New Orleans. However, the railroad continued to use all reasonable efforts to clear congestion from the directional running corridor linking Texas with Southern Missouri and Memphis.

In this week's letter, we will discuss the progress that has been made in that corridor, which is significant. We will then discuss the Laredo crisis and steps UP and KCS/Tex Mex/TFM cooperatively agreed to take to address it. We will also discuss the effects of the blizzard and UP's efforts to clean up in its wake. In light of these discussions, we will review this week's measurements. Finally, we report on BNSF and UP implementation of neutral dispatching.

within two weeks as the northern area recovers from the blizzard and the southern area completes movement of long-delayed trains.

**Joint Dispatching**

As described in the attached press release, BNSF and UP yesterday implemented neutral dispatching in the Gulf Coast area. The new joint dispatching center controls the former SP mainline between New Orleans and Houston, as well as HB&T trackage and a portion of the PTRA. A neutral joint director will supervise the center, overseeing corridor managers and dispatchers from both railroads using a common dispatching system. By the end of April, BNSF and UP will expand consolidated dispatching to include hundreds of miles of additional trackage extending north of Houston and all the way to the Mexican border. Tex Mex is still invited to participate, and space is available for its personnel.

Sincerely,

Mike Hemmer

Arvid E. Roach II
J. Michael Hemmer

cc: The Honorable Linda J. Morgan *(courtesy copy)*
The Honorable Gus A. Owen *(courtesy copy)*
Melvin F. Clemens, Jr., Director
Office of Compliance and Enforcement *(courtesy copy)*
All Parties of Record

BEFORE THE
SURFACE TRANSPORTATION BOARD

---

Ex Parte No. 573

RAIL SERVICE IN THE WESTERN UNITED STATES

---

Service Order No. 1518

JOINT PETITION FOR SERVICE ORDER

---

# UNION PACIFIC'S REPORT ON HOUSTON AND GULF COAST INFRASTRUCTURE

---


CARL W. VON BERNUTH
RICHARD J. RESSLER
Union Pacific Corporation
1717 Main Street
Suite 5900
Dallas, Texas 75201-4605

JAMES V. DOLAN
PAUL A. CONLEY, JR.
Union Pacific Railroad Company
1416 Dodge Street
Omaha, Nebraska 68179
(402) 271-5000

ARVID E. ROACH II
J. MICHAEL HEMMER
PAMELA L. MILES
Covington & Burling
1201 Pennsylvania Avenue, N.W.
P.O. Box 7566
Washington, D.C. 20044-7566
(202) 662-5388

Attorneys for Union Pacific Corporation and Union Pacific Railroad Company


May 1, 1998

The new tracks will provide the capacity to accept additional trains in the yard, reducing the need to disrupt operations on the mainline.

- **Construct centralized local management facility** ($5.0 million)

UP plans to locate the management of Englewood and Settegast yards in one office in order to manage these yards -- located within sight of each other -- as one facility. UP would construct a management center that would combine terminal management with a common crew on-duty point near these two yards.

2. Through Routes and Connections

To facilitate train movements through the Houston terminal, UP will make improvements to its lines and the HBT lines through Houston. The main arteries through central Houston are the HBT West Belt, the HBT East Belt and the former SP Sunset route (Englewood-Chaney Junction-West Junction-Rosenberg). UP intends to invest capital so that it can concentrate more of its operations on the former SP east-west routes and the West Belt, freeing capacity on the East Belt for on-line switching, transfer movements, local industry deliveries and BNSF and Tex Mex through trains.

- **Construct Tower 87 connections** ($4.0 million)

As soon as it receives City of Houston approval, UP will construct connections in the northeast and northwest quadrants at Tower 87, where the HBT East Belt crosses the former SP route. The northwest quadrant connection was proposed in the UP/SP merger application, but was delayed by City concerns. Currently, no easily-used connection exists between Englewood and Settegast yards, which are situated nearly route through Settegast Yard. To further improve this route, Bridge 16, located just below Tower 86 on the East Belt, should be double tracked at a cost of some $12.7 million. This would eliminate a bottleneck on the East Belt. Finally, Tex Mex could construct a set out and pick up track at Basin Yard on the East Belt, just north of Tower 86.

- **Third main track - Double Track Junction to T&NO Junction** ($5.0 million)

This line already has two tracks, but BNSF switching at New South Yard frequently blocks one or more of them. This additional trackage would serve as a bypass around New South Yard. An alternative to this new construction would be for UP and BNSF to control the New South Yard area jointly from their dispatching facility at Spring, Texas. Today, BNSF's Yardmaster controls the area.

- **Upgrade Harrisburg Line, West Junction to Tower 30** ($5.5 million)

UP will upgrade and install CTC on the Harrisburg Line around the south side of Houston. These improvements will facilitate the use of the East and West Belt lines as through routes. For example, they will benefit some movements on the Brownsville Subdivision, coal trains to and from Houston Lighting & Power, traffic to Galveston and some movements to and from Strang Yard. The improved line will provide an alternate route to Englewood and Settegast for traffic entering Houston on the Glidden Subdivision in case of congestion on the former SP route through Chaney Junction.

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PUBLIC DOCUMENT COUNT: 4
CONFORMED PERIOD OF REPORT: 19980331
FILED AS OF DATE: 19980514
SROS: NYSE

FILER:

COMPANY DATA:
COMPANY CONFORMED NAME: UNION PACIFIC RAILROAD CO/D
CENTRAL INDEX KEY: 0000092259
STANDARD INDUSTRIAL CLASSIFICATION: RAILROADS, LINE-HAUL OPERAT
IRS NUMBER: 946001323
STATE OF INCORPORATION: DE
FISCAL YEAR END: 1231

FILING VALUES:
FORM TYPE: 10-Q
SEC ACT:
SEC FILE NUMBER: 001-06146
FILM NUMBER: 98619563

BUSINESS ADDRESS:
STREET 1: SOUTHERN PACIFIC BLDG
STREET 2: ONE MARKET PLZ ROOM 505
CITY: SAN FRANCISCO
STATE: CA
ZIP: 94105
BUSINESS PHONE: 4155411000

MAIL ADDRESS:
STREET 1: SOUTHERN PACIFIC BLDG
STREET 2: ONE MARKET PLZ RM 505
CITY: SAN FRANCISCO
STATE: CA
ZIP: 94105

FORMER COMPANY:
FORMER CONFORMED NAME: SOUTHERN PACIFIC TRANSPORTATION CO
DATE OF NAME CHANGE: 19920703
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FORM 10-Q

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549-1004

(Mark One)

[ X ] QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES

EXCHANGE ACT OF 1934

For the quarterly period ended March 31, 1998

OR

[ ] TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from__________________ to ____________________

Commission file number 1-6146

UNION PACIFIC RAILROAD COMPANY
(Exact name of Registrant as specified in its charter)

| | |
|---|---|
| DELAWARE | 94-6001323 |
| (State or other jurisdiction of incorporation or organization) | (I.R.S. Employer Identification No.) |

1416 DODGE STREET, OMAHA, NEBRASKA
(Address of principal executive offices)

68179
(Zip Code)

(402) 271-5000
(Registrant's telephone number, including area code)

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

YES X NO

As of April 30, 1998, the Registrant had outstanding 4,465 shares of Common Stock, $10 par value, and 388 shares of Class A Stock, $10 par value.

THE REGISTRANT MEETS THE CONDITIONS SET FORTH IN GENERAL INSTRUCTIONS H(1)(a) AND (b) OF FORM 10-Q AND IS THEREFORE FILING THIS FORM WITH THE REDUCED DISCLOSURE FORMAT.

<INDEX PAGE>

UNION PACIFIC RAILROAD COMPANY
INDEX

PART I. FINANCIAL INFORMATION

PART II. OTHER INFORMATION



<PAGE>1

PART I - FINANCIAL INFORMATION

ITEM 1. CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

UNION PACIFIC RAILROAD COMPANY AND CONSOLIDATED SUBSIDIARY COMPANIES

CONDENSED STATEMENT OF CONSOLIDATED INCOME AND RETAINED EARNINGS
For The Three Months Ended March 31, 1998 and 1997

(Millions of Dollars)
(Unaudited)

| | 1998 | 1997 |
|---|---|---|
| Operating Revenues . . . . . . . . . . | $2,284 | $2,563 |
| Operating Expenses: | | |
| Salaries, wages and employee benefits. . . . . . . . . . . . . . . | 884 | 855 |
| Equipment and other rents . . . . . . | 356 | 314 |
| Fuel and utilities (Note 3). . . . . | 208 | 281 |
| Depreciation and amortization . . . . | 246 | 240 |
| Materials and supplies. . . . . . . . | 132 | 148 |
| Purchased services. . . . . . . . . . | 141 | 159 |
| Other costs (Note 5). . . . . . . . . | 264 | 213 |
| Total . . . . . . . . . . . . . . . | 2,231 | 2,210 |
| Operating Income . . . . . . . . . . . | 53 | 353 |
| Other Income - Net . . . . . . . . . . | 18 | 36 |
| Interest Expense (Note 3). . . . . . . | (134) | (122) |
| Income (Loss) Before Income Taxes. . . | (63) | 267 |
| Income Tax Expense (Benefit) . . . . . | (31) | 97 |
| Net Income (Loss) . . . . . . . . . | $ (32) | $ 170 |
| Retained Earnings: | | |
| Beginning of period . . . . . . . . . | 4,110 | 3,939 |
| Net income (loss) (Note 6). . . . . . | (32) | 170 |
| Dividends to parent . . . . . . . . . | (110) | (109) |
| End of Period. . . . . . . . . . | $3,968 | $4,000 |

| | | |
|---|---|---|
| Ratio of Earnings to Fixed Charges (Note 4). . . . . . . . . . | .6 | 2.5 |

The accompanying accounting policies and notes to condensed financial statements are an integral part of these statements.

<PAGE>2

UNION PACIFIC RAILROAD COMPANY AND CONSOLIDATED SUBSIDIARY COMPANIES

CONDENSED STATEMENT OF CONSOLIDATED FINANCIAL POSITION

(Millions of Dollars)
(Unaudited)

| ASSETS | March 31, 1998 | December 31, 1997 |
|---|---|---|
| Current Assets: | | |
| Cash and temporary investments . . . . . | $ 48 | $ 50 |
| Accounts receivable - net (Note 3) . . . | 390 | 456 |
| Materials and supplies . . . . . . . . . | 301 | 288 |
| Other current assets . . . . . . . . . . | 193 | 251 |
| Total Current Assets . . . . . . . . . | 932 | 1,045 |
| Investments: | | |
| Investments in and advances to affiliated companies . . . . . . . . . . | 652 | 595 |
| Other investments . . . . . . . . . . . | 29 | 29 |
| Total Investments . . . . . . . . . . . | 681 | 624 |
| Properties, at cost: | | |
| Road and other . . . . . . . . . . . . | 23,867 | 23,610 |
| Equipment . . . . . . . . . . . . . . . | 7,241 | 7,084 |
| Total Properties . . . . . . . . . . | 31,108 | 30,694 |
| Less accumulated depreciation and amortization . . . . . . . . . . . . | 5,365 | 5,208 |
| Properties - Net . . . . . . . . . . | 25,743 | 25,486 |
| Other Assets . . . . . . . . . . . . . . . | 123 | 92 |
| Total Assets . . . . . . . . . . . . | $27,479 | $27,247 |

The accompanying accounting policies and notes to condensed financial statements are an integral part of these statements.

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UNION PACIFIC RAILROAD COMPANY AND CONSOLIDATED SUBSIDIARY COMPANIES

CONDENSED STATEMENT OF CONSOLIDATED FINANCIAL POSITION

(Millions of Dollars)
(Unaudited)

| LIABILITIES AND STOCKHOLDER'S EQUITY | March 31, 1998 | December 31, 1997 |
|---|---|---|

| | | |
|---|---|---|
| Current Liabilities: | | |
| Accounts payable . . . . . . . . . . . . | $ 448 | $ 660 |
| Accrued wages and vacation . . . . . . | 377 | 382 |
| Taxes payable . . . . . . . . . . . . . . | 263 | 263 |
| Casualty and other reserves . . . . . . | 365 | 364 |
| Debt due within one year . . . . . . . | 129 | 229 |
| Other current liabilities (Note 2). . . | 800 | 869 |
| | ------- | ------- |
| Total Current Liabilities . . . . . . | 2,382 | 2,767 |
| | ------- | ------- |
| Debt Due After One Year . . . . . . . . | 2,415 | 2,361 |
| Deferred Income Taxes . . . . . . . . . | 6,670 | 6,698 |
| Retiree Benefit Obligations . . . . . . | 759 | 749 |
| Due to UPC Long-Term . . . . . . . . . . | 4,824 | 3,993 |
| Other Liabilities (Note 2 and 5) . . . . | 1,650 | 1,758 |
| Redeemable Preference Shares . . . . . . | 29 | 29 |
| Series A, $10,000 par value; 4,829 shares | | |
| Series B, $10,000 par value; 436 shares | | |
| Stockholder's Equity (Note 2): | | |
| Common stock - $10.00 par value; 9,200 shares authorized and 4,465 . . . . . | - | - |
| Class A stock - $10.00 par value; 800 shares authorized and 388 . . . . . . | - | - |
| Capital surplus . . . . . . . . . . . . | 4,782 | 4,782 |
| Retained earnings . . . . . . . . . . . | 3,968 | 4,110 |
| | ------- | ------- |
| Total Stockholder's Equity . . . . . | 8,750 | 8,892 |
| | ------- | ------- |
| Total Liabilities and Stockholder's Equity . . . . . . . . . . . . . . | $27,479 | $27,247 |
| | ======= | ======= |

The accompanying accounting policies and notes to condensed financial statements are an integral part of these statements.

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UNION PACIFIC RAILROAD COMPANY AND CONSOLIDATED SUBSIDIARY COMPANIES

CONDENSED STATEMENT OF CONSOLIDATED CASH FLOWS
For the Three Months Ended March 31, 1998 and 1997

(Millions of Dollars)
(Unaudited)

| | 1998 | 1997 |
|---|---|---|
| Cash from Operations: | | |
| Net Income (Loss) (Note 5). . . . . . . . | $ (32) | $ 170 |
| Non-Cash Charges to Income: | | |
| Depreciation and amortization . . . . . | 246 | 240 |
| Deferred income taxes . . . . . . . . . | (27) | 35 |
| Other - net . . . . . . . . . . . . . . | (54) | (48) |
| Changes in current assets and liabilities . . . . . . . . . . . . . . | (272) | (98) |
| | ----- | ----- |
| Cash Provided (Used) by Operations. . . . . . . . . . . | (139) | 299 |
| | ----- | ----- |

Investing Activities:

| | | |
|---|---|---|
| Capital investments . . . . . . . . . . . | (518) | (402) |
| Other - net . . . . . . . . . . . . . . . | (25) | (30) |
| Cash Used in Investing Activities . . . | (543) | (432) |

Equity and Financing Activities:

| | | |
|---|---|---|
| Debt repaid . . . . . . . . . . . . . . . | (132) | (89) |
| Financings . . . . . . . . . . . . . . . | 91 | 80 |
| Dividends paid to parent . . . . . . . . | (110) | (109) |
| Advances from affiliated companies - net. . . . . . . . . . . . | 831 | 237 |
| Cash Provided by Equity and Financing Activities . . . . . . . . | 680 | 119 |
| Net Change in Cash and Temporary Investments . . . . . . . . . . | $ (2) | $ (14) |

The accompanying accounting policies and notes to condensed financial statements are an integral part of these statements.



UNION PACIFIC RAILROAD COMPANY AND CONSOLIDATED SUBSIDIARY COMPANIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

1. RESPONSIBILITIES FOR FINANCIAL STATEMENTS: The condensed consolidated inancial statements of Union Pacific Railroad Company (the Company or the Railroad) are unaudited and reflect all adjustments (consisting only of normal and recurring adjustments) that are, in the opinion of management, necessary for a fair presentation of the financial position and operating results for the interim periods. The condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto contained in the Company's Annual Report on Form 10-K for the year ended December 31, 1997. The results of operations for the three months ended March 31, 1998 are not necessarily indicative of the results for the year ending December 31, 1998. Certain 1997 amounts have been reclassified to conform to the 1998 financial statement presentation.

2. ACQUISITION OF SOUTHERN PACIFIC RAIL CORPORATION (SOUTHERN PACIFIC OR SP): Union Pacific Corporation (UPC or the Corporation) consummated the acquisition of Southern Pacific in September 1996. The acquisition of Southern Pacific has been accounted for using the purchase method. On February 1, 1998, Union Pacific Railroad Company, a Utah Corporation (UPRR-Utah), was merged with and into Southern Pacific Transportation Company, a Delaware Corporation (SPT), the principal SP rail affiliate (the SPT Merger), with SPT continuing as the surviving corporation and changing its name to "Union Pacific Railroad Company" (UPRR), immediately following the SPT Merger. Immediately prior to the SPT Merger, SPT was a wholly-owned, indirect subsidiary of UPC, and UPRR-Utah was a subsidiary of UPC, with all of the issued and outstanding shares of voting stock of UPRR-Utah being owned, directly or indirectly, by UPC. UPRR-Utah and SPT operated as a unified system before and after the SPT Merger.

   The SPT Merger has been accounted for in a manner similar to a pooling-of-interest combination of entities under common control since both entities involved in the merger were indirect wholly-owned subsidiaries of UPC at the date of the SPT Merger and with the surviving entity continuing as such.

In connection with the continuing integration of UPRR-Utah and Southern Pacific's rail operations (collectively, the Railroad), the Company is continuing to eliminate duplicate positions, (primarily positions other than train crews), relocate positions, merge or dispose of redundant facilities, dispose of certain rail lines and cancel uneconomical and duplicative SP contracts. The Company has also repaid certain of Southern Pacific's debt obligations. The Company recognized a $958 million liability in the Southern Pacific purchase price allocation for

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costs associated with SP's portion of these activities.

Through March 31, 1998, approximately $323 million in merger-related costs were paid by the Company and charged against these reserves, principally composed of approximately $160 million and $70 million, respectively, for severance and relocation payments made to approximately 3,700 Southern Pacific employees and approximately $63 million for labor protection payments. The Company expects the remaining merger payments will be made over the course of the next five years as the rail operations of UPRR-Utah and the SP are integrated and labor negotiations are completed and implemented.

In addition, the Company expects to incur approximately $206 million in acquisition-related costs through 1999 for severing or relocating UPRR-Utah employees, disposing of certain UPRR-Utah facilities, training and equipment upgrading. These costs will be charged to expense as incurred over the next two years. Results for the three months ended March 31, 1998 include $18 million (after tax) in acquisition-related operating costs.

3. FINANCIAL INSTRUMENTS:

Risk Management: The Company uses derivative financial instruments in limited instances for other than trading purposes to manage risk as it relates to fuel prices and interest rates. Where the Company has fixed interest rates or fuel prices through the use of swaps, futures or forward contracts, the Company has mitigated the downside risk of adverse price and rate movements; however, it has also limited future gains from favorable movements.

The Company addresses market risk related to these instruments by selecting instruments whose value fluctuations highly correlate with the underlying item being hedged. Credit risk related to derivative financial instruments, which is minimal, is managed by requiring minimum credit standards for counterparties and monthly settlements. The total credit risk associated with the Company's counterparties was $36 million at March 31, 1998. The Company has not been required to provide, nor has it received, any collateral relating to its hedging activity.

The fair market value of the Company's derivative financial instrument positions at March 31, 1998 were determined based upon current fair market values as quoted by recognized dealers, or developed based on the present value of expected future cash flows discounted at the applicable zero coupon U.S. treasury rate and swap spread.

Fuel: Over the past three years, fuel costs approximated 10% of the Company's total operating expenses. As a result of the significance of the fuel costs and the historical volatility of fuel prices, the Company periodically uses swaps, futures and forward contracts to mitigate the impact of fuel price volatility. The intent of this program is to protect the Company's operating margins and overall

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profitability from adverse fuel price changes. At March 31, 1998, the Company had hedged 49% of its estimated remaining 1998 fuel consumption at $0.51 per gallon on a Gulf Coast basis and had outstanding swap agreements covering its fuel purchases of $267 million, with gross and net liability positions of $28 million. Fuel hedging increased the Company's first quarter 1998 and 1997 fuel costs by $14.5 million and $.1 million, respectively.

Interest Rates: The Company controls its overall risk relating to fluctuations in interest rates by managing the proportion of fixed and floating rate debt instruments within its debt portfolio over a given period. Derivatives are used in limited circumstances as one of the tools to obtain the targeted mix. The mix of fixed and floating rate debt is largely managed through the issuance of targeted amounts of such debt as debt maturities occur or as incremental borrowings are required. The Company also obtains additional flexibility in managing interest cost and the interest rate mix within its debt portfolio by issuing callable fixed rate debt securities.

At March 31, 1998, the Company had outstanding interest rate swaps on $109 million of notional principal amount of debt (4% of the total debt portfolio, excluding obligations to the Corporation) with gross and net liability positions of $8 million. These contracts mature over the next one to eight years. Interest rate hedging activity increased interest expense in both the first quarter of 1998 and 1997 by less than $1 million.

Sale of Receivables: The Company has sold, on a revolving basis, an undivided percentage ownership interest in a designated pool of accounts receivable. At December 31, 1997 and March 31, 1998, accounts receivable are presented net of the $650 million of receivables sold.

4. RATIO OF EARNINGS TO FIXED CHARGES: The ratio of earnings to fixed charges has been computed on a total enterprise basis. Earnings represent income from continuing operations less equity in undistributed earnings of unconsolidated affiliates, plus income taxes and fixed charges. Fixed charges represent interest, amortization of debt discount and expense, and the estimated interest portion of rental charges. For the three months ended March 31, 1998, fixed charges exceeded earnings by approximately $73 million.

5. COMMITMENTS AND CONTINGENCIES: There are various claims and lawsuits pending against the Company. Certain customers have submitted claims or stated their intention to submit claims to the Company for damages related to shipments delayed in transit as a result of congestion problems and certain customers have filed lawsuits seeking to recover damages for such delays. The nature of the damages sought by claimants includes, but is not limited to, contractual liquidated damages, freight loss or damage, alternative transportation charges, additional production costs, lost business and lost profits. In addition, some customers have asserted that they have the right to cancel contracts as a result of alleged material breaches of such contracts by the

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Railroad. The Company expects additional claims by shippers. The Company will continue to evaluate the adequacy of its reserves for claims and expects to add to such reserves as appropriate.

The Railroad is also party to certain regulatory proceedings before the Surface Transportation Board of the U.S. Department of Transportation (STB). One proceeding pertains to rail service problems in the western United States. As an outgrowth of this proceeding, the STB has issued an emergency service order imposing certain temporary measures on the Railroad designed, among other things, to reduce congestion on the Railroad's lines in the Houston, Texas area. A second proceeding, initiated under the STB's continuing oversight jurisdiction with respect to the Corporation's acquisition of Southern Pacific and consolidation of Southern Pacific with UPRR-Utah (and separate from the STB's regularly-scheduled annual proceeding to review the implementation of the merger and the effectiveness of the conditions that the STB imposed on it), is for the purpose of considering the justification for and advisability of any proposals for new remedial conditions to the merger as they pertain to service in the Houston, Texas/Gulf Coast area, including, proposals by Kansas City Southern Railway Company (KCS), Texas Mexican Railway Company (Tex Mex) and the Greater Houston Partnership (GHP) for the forced transfer by the Railroad to Tex Mex of certain lines and facilities in and around Houston, the establishment of a "neutral" switching operation in the greater Houston area and the permanent adoption of provisions in the STB's emergency service order that expanded Tex Mex's right to handle traffic to and from Houston. In addition, the STB has initiated various inquiries and formal rule-making proceedings regarding certain elements of rail regulation following two days of hearings by the STB at the request of two members of Congress and in response to shippers' expressions of concern regarding railroad service quality, railroad rates and allegedly inadequate regulatory remedies. If the Railroad is unsuccessful in eliminating the remaining congestion and service problems affecting its system, the STB could issue a new emergency service order with the expiration of the current one and order the Railroad to take additional actions including, among other things, further diversions of traffic or the transfer of certain rail lines or other facilities to other railroads. In addition, there can be no assurance that the proposals advanced by parties in the remedial conditions proceeding or the proceedings initiated in response to the rail regulation hearings will not be approved in some form. Should the STB or Congress take aggressive action in the rail regulation proceedings (e.g., by making purportedly competition-enhancing changes in rate and route regulation and "access" provisions), the adverse effect on the Railroad and other rail carriers could be material.

The Company is also subject to Federal, state and local environmental laws and regulations, and is currently participating in the investigation and remediation of numerous sites. Where the remediation costs can be reasonably determined, and where such remediation is probable, the Company has recorded a liability. In addition, the Company periodically enters into financial and other commitments and

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has retained certain contingent liabilities upon the disposition of formerly-owned operations.

In addition, UPC and certain of its officers and directors are currently defendants in two purported class action securities lawsuits, and certain current and former directors of the Corporation are currently defendants in a purported derivative action filed on behalf of the Corporation. The class action suits allege, among other things, that management failed to properly disclose the Railroad's service and safety problems and thereby issued materially false and misleading statements concerning the merger with SP and the safe, efficient operation of its rail network. The derivative action alleges, among other things, that the named current and former directors breached their fiduciary duties to the Corporation by approving the mergers of SP and Chicago and Northwestern Transportation Company into the Corporation without ensuring that the Corporation or the Railroad had adequate systems in place to effectively integrate those acquisitions into the operations of the Corporation and the Railroad. Because both the size of the class and the damages are uncertain, UPC and the Railroad are unable at this time to determine the potential liability, if any, which might arise from these lawsuits. Management believes that these claims are without merit and intends to defend them vigorously.

It is not possible at this time for the Company to fully determine the effect of all unasserted claims on its consolidated financial condition, results of operations or liquidity; however, to the extent possible, where unasserted claims can be estimated and where such claims are considered probable, the Company has recorded a liability. The Company does not expect that any known lawsuits, claims, environmental costs, commitments or guarantees will have a material adverse effect on its consolidated financial condition.

6. ACCOUNTING PRONOUNCEMENTS: In June 1997, the Financial Accounting Standards Board (FASB) issued Statement No. 130, "Reporting Comprehensive Income" (FAS 130), that is effective for all periods in 1998, including interim periods. The Company has adopted the provisions of FAS 130 effective January 1, 1998. The components of comprehensive income include, among other things, changes in the market value of futures contracts which qualify for hedge accounting and a net loss recognized as an additional pension liability but not yet recognized as net periodic pension cost. There is no impact from adopting FAS 130 for the three months ended March 31, 1998.

   Also in June 1997, the FASB issued Statement No. 131, "Disclosures about Segments of an Enterprise and Related Information," that is effective in 1998. The Company currently complies with most provisions of this Statement, and any incremental disclosure required by that Statement is expected to be minimal.

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   In February 1998, the FASB issued Statement No. 132, "Employers' Disclosures about Pensions and Other Postretirement Benefits," that is effective in 1998 (FAS 132). FAS 132 revises and standardizes disclosures required by FAS 87, 88, and 106. Restatement of the retirement plans footnote will be required for all earlier periods presented in comparative financial statements at December 31, 1998.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

UNION PACIFIC RAILROAD COMPANY AND CONSOLIDATED SUBSIDIARY COMPANIES

MANAGEMENT'S NARRATIVE ANALYSIS OF THE RESULTS OF OPERATIONS

Three Months Ended March 31, 1998 Compared to March 31, 1997

## Mergers

On February 1, 1998, Union Pacific Railroad Company, a Utah Corporation (UPRR-Utah), was merged with and into Southern Pacific Transportation Company, a Delaware Corporation (SPT), the principal SP rail affiliate (the SPT Merger), with SPT continuing as the surviving corporation and changing its name to "Union Pacific Railroad Company" (UPRR), immediately following the SPT Merger. Immediately prior to the SPT Merger, SPT was a wholly-owned, indirect subsidiary of UPC, and UPRR-Utah was a subsidiary of UPC, with all of the issued and outstanding shares of voting stock of UPRR-Utah being owned, directly or indirectly, by UPC. UPRR-Utah and SPT operated as a unified system before and after the SPT Merger.

The SPT Merger has been accounted for in a manner similar to a pooling-of-interest combination of entities under common control since both entities involved in the merger were indirect wholly-owned subsidiaries of UPC at the date of the SPT Merger and with the surviving entity continuing as such.

## Congestion and Service Issues

As previously reported in the Company's 1997 Annual Report on Form 10-K, congestion in and around Houston and the coastal areas of Texas and Louisiana (the Gulf Coast region) began to have a material adverse effect on the Company's operations and earnings in the third quarter of 1997. System congestion started in the Gulf Coast region and spread throughout the system as the Railroad shifted resources to help mitigate the problem in the Gulf Coast region. The congestion was brought on by, among other things, crew shortages and restricted track access caused by necessary track maintenance on former Southern Pacific lines, increased demand, washouts due to severe weather, derailments and congestion at Texas/Mexico gateways. Traffic slowed further as rail yards in the Gulf Coast region

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filled, slowing access into and out of the yards and forcing trains to be held on sidings. Slower average train velocity led to a greater need for locomotives in the region. As traffic in the region backed up and the Railroad redeployed locomotives to the Gulf Coast region to help alleviate local congestion, congestion problems spread to other parts of the Railroad's system during the third and fourth quarters of 1997.

To restore service to acceptable levels, the Railroad implemented a Service Recovery Plan (the Plan) in October, 1997. The Plan focuses on reducing the number of cars on the system and restoring system velocity, which, in turn, results in more reliable service to customers. Implementation of the Plan has resulted in improvement in the overall operation of the Railroad and is addressing congestion problems in the Gulf Coast region and the surrounding southeast portion of the Railroad's system (although intermittent periods of congestion continue to arise in other regions, primarily in the Midwest). In late March and early April 1998, congestion in the Gulf Coast region was aggravated by several severe storms and congestion caused by operational problems on Mexican railroad lines south of Laredo, Texas. However, operational initiatives subsequently implemented by the Railroad, including the Railroad's embargo of most southbound traffic destined for the Laredo gateway, have substantially reduced congestion on the Railroad's lines in the Gulf Coast region.

In connection with its integration with Southern Pacific, the Company has implemented (i) TCS in the southeast portion of UPRR's system, which includes the Gulf Coast region, where the cut over to TCS occurred on December 1, 1997, (ii) directional running from Dexter Junction, Missouri, on the north, across Arkansas, western Louisiana and eastern Texas to the Houston and San Antonio areas on the south, beginning on February 1, 1998 and (iii) the hub-and-spoke labor agreements in Texas and Arkansas. Although the Company believes that the full implementation of these changes is essential to achieving significant long-term benefits, their implementation also contributed to the persistence of congestion in the affected Gulf Coast region during late 1997 and early 1998.

On March 28, 1998, the Railroad embargoed most southbound traffic destined for the Laredo, Texas gateway to address worsening congestion at that gateway and clear the backlog of cars waiting to cross into Mexico. The embargo applied to grain, chemicals, industrial products and coal, but not finished automobiles, auto parts or intermodal traffic or any northbound traffic through Laredo. The Railroad rerouted some of the embargoed traffic through other Railroad gateways to Mexico, none of which were subject to the embargo. The Railroad believed that this embargo was necessary because congestion problems principally within Mexico and agricultural inspection delays at the border that affected the Laredo gateway had worsened during the weeks preceding the imposition of the embargo and were affecting other areas within the southeast region of its system, resulting in a substantial backlog of cars waiting to move south to Laredo. Imposition of the embargo quickly resulted in a significant reduction in the backlog of cars. Accordingly, on April 14, 1998, the

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Railroad amended the embargo to introduce permitting to control traffic volumes. The permitting system allowed customers to move traffic that had been embargoed while allowing the Railroad to meter southbound traffic to prevent any surge of business that could again block the Laredo crossing. On April 16, 1998, the Railroad further amended the embargo to eliminate permit requirements for domestic shipments terminating at Laredo, and on April 22, 1998, the Railroad canceled the embargo.

Financial Impact of Congestion - The Railroad has estimated that the cost of the congestion-related problems for the three months ended March 31, 1998 was approximately $260 million, after tax, which reflected the combined effects of lost business, higher costs associated with system congestion, costs associated with implementation of the Plan, alternate transportation and customer claims. Although progress has been made in improving service, the Railroad expects these problems to continue to have an adverse impact on 1998 results. In addition, as a result of recent operating losses incurred by the Railroad and in order to fund its capital programs, the Corporation has incurred substantial incremental debt since December 31, 1997, and obtained additional financing on April 1, 1998 from a private placement of $1.5 billion of 6-1/4% preferred securities of Union Pacific Capital Trust, a statutory business trust sponsored by the Corporation, which securities are convertible into common stock of the Corporation at an initial conversion price of $68.90. The timing of the Corporation's return to profitability will be determined by how rapidly it is able to eliminate congestion, and return to normal operations throughout its system.

## Results of Operations

The Company reported a loss of $32 million in the first quarter of 1998, compared to $170 million of reported net income in 1997. This decline in earnings is the result of the continuing effects of congestion on the Company's operations, which was estimated to cost the Company approximately $260 million after-tax in the first quarter of 1998. Both periods included the impact of one-time SP merger-related costs for severance, relocation and training of employees ($18 million reduction in net income in 1998 and $9 million reduction in net income in 1997).

The operating ratio for the first quarter of 1998 was 97.7, which included approximately 15 points estimated to be attributable to congestion costs (both lost business and incremental operating costs). This compares to an operating ratio of 86.2 for the same period in 1997. Operating revenues fell $279 million (11%) to $2.28 billion in 1998. This decrease reflects continuing congestion, the impact of the Asian crisis on export grain and intermodal markets and weak grain demand as farmers delay shipments due to the current grain price environment. Average commodity revenue per car (ARC) fell 1% to $1,149 per car, while total carloadings fell 9% (approximately 189,000 cars). Commodity revenue in 1998 fell 10% over the same period in 1997 as shown in the table below:

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Commodity Revenue
Three Months Ended 3/31/98

| (Revenue in 000's) | Cars | ARC | Commodity Revenue | Versus 1997 Change | Versus 1997 % |
|---|---|---|---|---|---|
| Automotive | 159,400 | $1,446 | $ 230,464 | $ (6,973) | (3) |
| Agricultural | 203,177 | 1,554 | 315,786 | (87,410) | (22) |
| Intermodal | 590,115 | 606 | 357,506 | (56,924) | (14) |
| Chemicals | 222,798 | 1,749 | 389,773 | (43,719) | (10) |
| Energy | 442,094 | 1,124 | 496,988 | (15,207) | (3) |
| Industrial | 320,602 | 1,359 | 435,709 | (40,502) | (9) |
| Total Commodity | 1,938,186 | $1,149 | $2,226,226 | $(250,735) | (10) |

Automotive: Commodity revenue fell $7 million or 3% to $230 million, despite a 1% increase in carloadings, reflecting new business opportunities and steady economic conditions in the Automotive industry. Strong demand and the new Ford business led the 3% increase in finished autos carloadings, while parts volumes fell 2% resulting from congestion-related diversions of traffic and inventory control by major manufacturers. Average commodity revenue per car declined 4%, resulting from generally shorter-haul Ford business and less long-haul Mexico business.

Agricultural Products: Commodity revenue fell 22% to $316 million. Carloadings declined 18% to 203,000 cars, primarily the result of a 25% decrease in corn volumes due to soft export demand (strong foreign production and the effect on exchange rates due to the Asian crisis), as well as, continued congestion. Most agricultural products suffered from congestion problems and related equipment shortages; meals and oils were the only bright spot, as U.S. producers benefitted from strong export markets, primarily to Mexico. Average commodity revenue per car declined 5%, largely the result of weak exports, which significantly reduced the average length of haul.

Intermodal: Commodity revenue declined 14% to $358 million, while carloadings fell 12% to 590,000 loads--the result of continued congestion and related diversions of traffic, as well as equipment imbalances caused by strong imports and weak exports. Average commodity revenue per car fell 1%, as unfavorable mix was largely offset by new longer-haul business.

Chemicals: Carloadings declined 6% to 223,000 cars and commodity revenue decreased $44 million (10%) to $390 million. The decline in volume resulted principally from system congestion (partially the result of congestion of traffic crossing at the Mexican border), which more than

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offset strong market demand. Average commodity revenue per car declined 4% due to generally shorter hauls (storage-in-transit moves for plastic and strong growth in short-haul potash moves) and unfavorable product mix.

Energy (Primarily Coal): Commodity revenue fell 3% to $497 million in 1998, driven by a 3% decrease in carloadings. Continued congestion problems, diversions of business to competing roads and a late February blizzard led the decline, despite strong demand. Average commodity revenue per car was flat quarter over quarter. Powder River Basin (PRB) train cycles fell slightly from first quarter 1997, 24.8 in 1998 vs. 25.1 in 1997; however, longer trains (117.6 cars/train in 1998 vs. 114.1 in 1997) boosted loads by approximately 3,200 units helping to improve PRB business versus 1997. All other mine locations posted declines, largely due to congestion and related train cycle time issues.

Industrial Products: Carloadings decreased 10%, while commodity revenue declined 9% to $436 million. Volume declines resulted primarily from continued congestion (in the Southern tier and the Pacific Northwest), as well as, the Company's sale of its Duck Creek North line in 1997. Average commodity revenue per car improved 1%, the result of the absence of shorter-haul Duck Creek North business and favorable mix changes.

Operating expenses were $2,231 million, $21 million (1%) higher than the first quarter 1997 operating costs of $2,210 million. Higher operating costs reflected approximately $77 million of congestion-related costs ($148 million of congestion-related costs offset by $71 million of volume savings from lower business levels). The impact of congestion was partially offset by lower fuel costs, merger benefits and volume-related cost savings, as carloads were off 9% and gross-ton miles were down 10%.

Labor expense was $29 million (3%) higher than 1997, as net congestion-related costs and wage inflation were partially offset by merger consolidation benefits. Quarter-over-quarter, the work force levels were virtually flat, as merger-related staff reductions and attrition were offset by new hiring for train and engine crews.

Depreciation expense grew $6 million or 3% to $246 million due to the Company's extensive capital program in 1997 and 1998. The Company spent over $2 billion on capital projects in 1997 and anticipates spending $2.2 billion in 1998 of which $400 million will be merger-related.

Materials and Supplies expenditures were down $16 million (11%) from first quarter 1997. More rebuild projects (which are capitalized) and less maintenance projects in 1998 plus the absence of large program maintenance projects on freight cars in 1998 accounted for the quarter-over-quarter decline.

Fuel and Utilities expenses were down $73 million or 26% from 1997, reflecting lower fuel prices and congestion-related volume declines. A reduction in gross-ton miles quarter-over-quarter (down 10%) generated volume-related fuel savings of $24 million versus 1997. Prices were down 11.7 cents per gallon to 63.6 cents, saving $33 million. The fuel

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consumption rate of 1.416 gallons per thousand gross-ton miles improved 3% from last year's 1.457 (largely slower locomotive speeds), lowering the Company's fuel costs by another $7 million.

Rent Expense was up 13% ($42 million) versus 1997, as system congestion (which hindered car cycle times) combined with unfavorable rates (strong market demand for equipment) to drive up equipment rent costs.

Other Costs (including purchased services) increased $33 million(9%) from 1997, reflecting higher costs for customer claims and service recovery initiatives (focused on combating system congestion). Congestion -related cost increases were partially offset by merger consolidation benefits (trackage rights reimbursements and contract pricing savings) and cost savings from company-wide cost control efforts.

Operating income declined $300 million to $53 million in 1998, reflecting the effect of continued congestion and inflation. Interest expense increased $12 million to $134 million, principally resulting from higher debt levels. Other income, net declined $18 million due to the absence of the Duck Creek North branch line sale in 1997. Income taxes decreased $128 million to a benefit of $31 million, primarily reflecting lower income before income taxes.

## Other Matters

Accounting Pronouncements: In June 1997, the Financial Accounting Standards Board (FASB) issued Statement No. 130, "Reporting Comprehensive Income" (FAS 130), that is effective for all periods in 1998, including interim periods. The Company has adopted the provisions of FAS 130 effective January 1, 1998. The components of comprehensive income include, among other things, changes in the market value of futures contracts which qualify for hedge accounting and a net loss recognized as an additional pension liability but not yet recognized as net periodic pension cost. There is no impact from adopting FAS 130 for the three months ended March 31, 1998.

Also in June 1997, the FASB issued Statement No. 131, "Disclosures about Segments of an Enterprise and Related Information," that is effective in 1998. The Company currently complies with most provisions of this Statement, and any incremental disclosure required by that Statement is expected to be minimal.

In February 1998, the FASB issued Statement No. 132, "Employers' Disclosures about Pensions and Other Postretirement Benefits," that is effective in 1998 (FAS 132). FAS 132 revises and standardizes disclosures required by FAS 87, 88, and 106. Restatement of the retirement plans footnote will be required for all earlier periods presented in comparative financial statements at December 31, 1998.

Commitments and Contingencies - There are various claims and lawsuits pending against the Company. Certain customers have submitted claims or

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stated their intention to submit claims to the Company for damages related to shipments delayed in transit as a result of congestion problems and certain customers have filed lawsuits seeking to recover damages for such delays. The nature of the damages sought by claimants includes, but is not limited to, contractual liquidated damages, freight loss or damage, alternative transportation charges, additional production costs, lost business and lost profits. In addition, some customers have asserted that they have the right to cancel contracts as a result of alleged material breaches of such contracts by the Railroad. The Company expects additional claims by shippers. The Company will continue to evaluate the adequacy of its reserves for claims and expects to add to such reserves as appropriate.

The Railroad is also party to certain regulatory proceedings before the Surface Transportation Board of the U.S. Department of Transportation (STB). One proceeding pertains to rail service problems in the western United States. As an outgrowth of this proceeding, the STB has issued an emergency service order imposing certain temporary measures on the Railroad designed, among other things, to reduce congestion on the Railroad's lines in the Houston, Texas area. A second proceeding, initiated under the STB's continuing oversight jurisdiction with respect to the Corporation's acquisition of Southern Pacific and consolidation of Southern Pacific with UPRR-Utah (and separate from the STB's regularly-scheduled annual proceeding to review the implementation of the merger and the effectiveness of the conditions that the STB imposed on it), is for the purpose of considering the justification for and advisability of any proposals for new remedial conditions to the merger as they pertain to service in the Houston, Texas/Gulf Coast area, including, proposals by Kansas City Southern Railway Company (KCS), Texas Mexican Railway Company (Tex Mex) and the Greater Houston Partnership (GHP) for the forced transfer by the Railroad to Tex Mex of certain lines and facilities in and around Houston, the establishment of a "neutral" switching operation in the greater Houston area and the permanent adoption of provisions in the STB's emergency service order that expanded Tex Mex's right to handle traffic to and from Houston. In addition, the STB has initiated various inquiries and formal rule-making proceedings regarding certain elements of rail regulation following two days of hearings by the STB at the request of two members of Congress and in response to shippers' expressions of concern regarding railroad service quality, railroad rates and allegedly inadequate regulatory remedies. If the Railroad is unsuccessful in eliminating the remaining congestion and service problems affecting its system, the STB could issue a new emergency service order with the expiration of the current one and order the Railroad to take additional actions including, among other things, further diversions of traffic or the transfer of certain rail lines or other facilities to other railroads. In addition, there can be no assurance that the proposals advanced by parties in the remedial conditions proceeding or the proceedings initiated in response to the rail regulation hearings will not be approved in some form. Should the STB or Congress take aggressive action in the rail regulation proceedings (e.g., by making purportedly competition-enhancing changes in rate and route regulation and "access" provisions), the adverse effect on the Railroad and other rail carriers could be material.

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The Company is also subject to Federal, state and local environmental laws and regulations, and is currently participating in the investigation and remediation of numerous sites. Where the remediation costs can be reasonably determined, and where such remediation is probable, the Company has recorded a liability. In addition, the Company periodically enters into financial and other commitments and has retained certain contingent liabilities upon the disposition of formerly-owned operations.

In addition, UPC and certain of its officers and directors are currently defendants in two purported class action securities lawsuits, and certain current and former directors of the Corporation are currently defendants in a purported derivative action filed on behalf of the Corporation. The class action suits allege, among other things, that management failed to properly disclose the Railroad's service and safety problems and thereby issued materially false and misleading statements concerning the merger with SP and the safe, efficient operation of its rail network. The derivative action alleges, among other things, that the named current and former directors breached their fiduciary duties to the Corporation by approving the mergers of SP and Chicago and Northwestern Transportation Company into the Corporation without ensuring that the Corporation or the Railroad had adequate systems in place to effectively integrate those acquisitions into the operations of the Corporation and the Railroad. Because both the size of the class and the damages are uncertain, UPC and the Railroad are unable at this time to determine the potential liability, if any, which might arise from these lawsuits. Management believes that these claims are without merit and intends to defend them vigorously.

It is not possible at this time for the Company to fully determine the effect of all unasserted claims on its consolidated financial condition, results of operations or liquidity; however, to the extent possible, where unasserted claims can be estimated and where such claims are considered probable, the Company has recorded a liability. The Company does not expect that any known lawsuits, claims, environmental costs, commitments or guarantees will have a material adverse effect on its consolidated financial condition.

## Cautionary Information

Certain information included in this report contains, and other materials filed or to be filed by the Company with the Securities and Exchange Commission (as well as information included in oral statements or other written statements made or to be made by the Company) contain or will contain, forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. Such forward-looking information may include, without limitation, statements that the Company does not expect that lawsuits, environmental costs, commitments, contingent liabilities, labor negotiations, claims or other matters will have a material adverse effect on its consolidated financial condition, results of operations or liquidity and other similar expressions concerning matters that are not historical facts, and projections or predictions as to the Company's



financial or operational results. Such forward-looking information is or will be based on information available at that time, and is or will be subject to risks and uncertainties that could cause actual results to differ materially from those expressed in the statements. Important factors that could cause such differences include, but are not limited to whether the Company is fully successful in overcoming its congestion-related problems and implementing the Plan and other operational and financial initiatives, industry competition and regulatory developments, natural events such as floods and earthquakes, the effects of adverse general economic conditions, fuel prices, labor strikes, the impact of year 2000 systems problems and the ultimate outcome of shipper claims related to congestion, environmental investigations or proceedings and other types of claims and litigation.

## PART II. OTHER INFORMATION

### Item 1. LEGAL PROCEEDINGS

SOUTHERN PACIFIC ACQUISITION: As previously reported in the Company's 1997 Annual Report on Form 10-K, various appeals have been filed with respect to the STB's August 12, 1996 decision (the Decision) approving the acquisition of control of Southern Pacific by UPC. All of the appeals have been consolidated in the U.S. Court of Appeals for the District of Columbia Circuit. Oral argument in the case is scheduled for September 11, 1998. Various appellants have withdrawn their appeals, leaving only Burlington Northern and Santa Fe Railway Company (BNSF), the Western Coal Traffic League (WCTL), Enterprise Products Company and the City of Reno, Nevada with appeals pending. On April 10, 1998 WCTL filed a motion to vacate and remand the Decision in light of a proceeding the STB commenced on March 31, 1998, under its continuing oversight jurisdiction over the merger, to consider whether any additional conditions are justified and should be imposed to deal with service problems in the Houston/Gulf Coast area. The STB, the Corporation, the Company and BNSF have opposed this motion. The Corporation and the Company believe that it is unlikely that the disposition of the remaining appeals will have a material adverse impact on its consolidated financial condition or its results of operations.

RAIL SERVICE PROCEEDINGS AND RELATED MATTERS: As previously reported in the Company's 1997 Annual Report on Form 10-K, UPRR is currently subject to an emergency service order issued by the STB on October 31, 1997, as an outgrowth of a proceeding initiated by the STB on October 2, 1997 to investigate rail service problems in the western United States. The original service order, which, among other things, imposed several temporary measures designed to reduce congestion on UPRR's lines in the Houston area, was modified and extended by a supplemental order dated December 4, 1997. On February 25, 1998, the STB, citing the gravity of UPRR's congestion problems and characterizing them as "not yet close to being resolved," further modified the emergency service order and extended it until August 2, 1998, the maximum period allowable under the law for the original order.

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On March 31, 1998, the STB initiated a proceeding under its continuing oversight jurisdiction with respect to the merger of the Corporation and Southern Pacific to consider proposals for new remedial conditions to the merger as they pertain to service in the Houston, Texas/Gulf Coast area. This proceeding, which is separate from the STB's regularly scheduled annual proceeding to review the implementation of the merger and the effectiveness of the conditions that the STB imposed on it, was initiated in response to submissions by Texas Mexican Railway Company (Tex Mex) and Kansas City Southern Railway Company (KCS) and by the Greater Houston Partnership ("GHP"), proposing that the Railroad be directed to transfer certain lines and facilities in the Gulf Coast region to other rail carriers, that a "neutral" switching operation be established in the greater Houston area and that provisions in the STB's emergency service order that expanded Tex Mex's right to handle traffic to and from Houston be adopted permanently. The STB's decision announcing the proceeding established a procedural schedule for the submission of evidence, replies and rebuttal.

If continued implementation of the Plan and other operational and financial initiatives undertaken by the Company ultimately proves unsuccessful in alleviating the remaining congestion and related service problems experienced by the Railroad, the STB could issue a new emergency service order upon the expiration of the current one and order the Railroad to take additional actions including, among other things, further diversions of traffic or the transfer of certain of the Railroad's rail lines or other facilities to other railroads. In addition, there can be no assurance that the proposals advanced by Tex Mex, KCS, GHP or other parties in the remedial conditions proceeding will not be approved in some form.

RAIL ACCESS AND COMPETITION: Acting pursuant to requests from two members of Congress and responding to shippers' concerns about railroad service quality, railroad rates and allegedly inadequate regulatory remedies, the STB on April 17, 1998, following two days of hearings, issued a decision opening inquiries into certain elements of rail regulation. The STB noted that no parties to the hearings had shown how aggressive remedies designed to produce lower rates and enhance competition would permit the industry to cover system costs and support reinvestment. Nevertheless, it (i) directed a panel of disinterested economic experts to recommend appropriate standards to measure railroad revenue adequacy, which is used to determine whether rates are lawful (this portion of the decision was subsequently modified to permit, as an alternative, discussions of this issue between railroad and shipper representatives); (ii) initiated a rule-making proceeding to consider revisions to "competitive access"