

Surface Transportation Board Issues 2 Decisions on Disputes Arising from 1996 "Union Pacific-Southern Pacific" Railroad Merger

Surface Transportation Board (Board) Chairman Linda J. Morgan announced today that the Board has issued two decisions (Decision Nos. 95 and 96) addressing disputes concerning the trackage rights received by The Burlington Northern and Santa Fe Railway Company (BNSF) in connection with the 1996 "Union Pacific (UP)-Southern Pacific (SP)" railroad merger in the case entitled *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*, Finance Docket No. 32760.

BACKGROUND

As noted in Surface Transportation Board "News" release No. 01-70 issued December 20, 2001, the Board issued a decision on that date ending, as scheduled, the agency's formal oversight process for the UP-SP merger, and stated that the Board would remain available to consider and promptly resolve any disputes of general applicability relating to BNSF's access to shippers under the BNSF Agreement (containing a complete description of the rights granted to BNSF in connection with the merger), or any other issues relating to parties' compliance with conditions imposed on the merger by the Board, subject to any applicable arbitration requirement. Decision Nos. 95 and 96, as summarized below, demonstrate the Board's continuing availability to address such disputes.

DECISION NO. 95

In Decision No. 95, the Board addressed a dispute concerning the Board-imposed, "build-in/build-out" condition (involving lines built from an existing line to a facility or lines built from a facility to an existing line) to preserve the pre-merger status quo as to potential "build-in/build-out" lines. This condition intended that, if, prior to the merger, a shipper served exclusively either by UP or by SP could have "built out" to a nearby line of the other railroad (or, if the other railroad could have "built in" to the shipper), then BNSF should be given sufficient trackage rights to access any such future build-in/build-out line.

UP and BNSF have taken different positions relative to the circumstances under which BNSF should be required to construct or fund, on UP lines, new connections, facilities, or other improvements to provide service to a build-in/build-out line. BNSF contended that it should be responsible for such construction or funding only if (1) UP demonstrates that, absent such construction, BNSF's proposed service would unreasonably and materially interfere with UP's service to its customers, and (2) requiring BNSF to undertake such construction would not impair BNSF's ability to provide competitive service. UP contended that BNSF must bear the responsibility of avoiding or remedying all unreasonable interference during construction and, upon completion, all material interference between BNSF's build-in/build-out operations and existing rail service.

In Decision No. 95, the Board declined to adopt a generic standard for all build-in/build-out situations. The Board noted that the standards proposed by BNSF and UP appeared to provide undue leverage to the party proposing the standard, and would create disincentives on the part of one party or the other to actively seek creative dispatching, scheduling, or other operational solutions that would minimize the need for additional capital expenditures. The Board further noted that the BNSF standard could affect UP's ability to conduct its own operations on the trackage rights lines, and, in certain instances, could compel UP to subsidize BNSF's build-in/build-out operations, and that the UP standard could limit the underlying competition-preserving purpose of the build-in/build-out condition and, in certain instances, could prevent BNSF from replicating the competitive posture of the pre-merger SP.

The Board therefore directed BNSF and UP to resume negotiations relative to the various issues arising from implementation of the build-in/build-out condition. The Board further directed that BNSF and UP, in efforts to craft solutions to operational problems resulting from the application of the build-in/build-out condition, should seek to minimize the operating inconvenience to UP, consistent with ensuring that BNSF can provide competitive service. The Board added that any controversies that cannot be resolved by negotiation may be submitted for resolution either to the Board (on a case-by-case basis) or to arbitration (as provided in the BNSF Agreement).

DECISION NO. 96

In Decision No. 96, the Board addressed a dispute concerning the mechanism for adjusting fees applicable to the trackage rights that BNSF received in connection with the UP-SP merger.

The initial rates applicable to the BNSF trackage rights were established in Section 9(a) of the BNSF Agreement. Section 12 of the BNSF Agreement provides for the "adjustment" of the Section 9(a) rates as follows:

"All trackage rights charges under this Agreement shall be subject to adjustment upward or downward July 1 of each year by the difference in the two preceding years in UP/SP's system average URCS costs for the categories of maintenance and operating costs covered by the trackage rights fee. 'URCS costs' shall mean costs developed using the Uniform Rail Costing System."

The dispute addressed by the Board in Decision No. 96 concerns two items that are components of the "maintenance and operating costs covered by the trackage rights fee" when using standard accounting procedures--that is, procedures consistent with the Uniform System of Accounts--in developing Uniform Rail Costing System (URCS) costs but that BNSF argues were not to be included in the calculation here. The first disputed item is the so-called "acquisition premium"--the excess of the price paid to acquire the SP rail railroads over the pre-acquisition book value of such carriers. The second disputed item concerns the costs of certain capacity improvements undertaken by UP on trackage rights lines allocated--under Sections 9(c)(i) and 9(c)(iii) of the BNSF Agreement--entirely to UP, even though such lines are used both by UP and by BNSF and even though the BNSF Agreement generally requires that both railroads share costs based upon their respective usage of the line in question. The capacity improvements governed by Section 9(c)(i) are those necessary to achieve the benefits of the UP-SP merger as outlined in the UP-SP merger application. The capacity improvements governed by Section 9(c)(iii) are those undertaken within the first 18 months following the UP-SP merger.

The Board stated, however, that, if the URCS calculations underlying the Section 12 adjustment factor are performed as required, the disputed items will be included in that factor. The Board further noted that there was no indication anywhere in the public record compiled in the UP-SP merger proceeding that any party ever contemplated that URCS calculations required to create the Section 12 adjustment factor would not be performed as required. The Board observed that BNSF's assertion that it had contemplated that the URCS adjustment mechanism would reflect "actual costs" did not advance BNSF's case, because URCS costs, when calculated in the required manner, reflect actual costs. The Board added that, although BNSF may have contemplated that the Section 12 adjustment factor would exclude costs related to the acquisition premium and to Section 9(c)(i) and (iii) capacity improvements, it has not yet provided evidence of any agreement in UP-SP to exclude such items. Rather, the Board pointed out that BNSF had agreed to a formulation that references, without any mention of any such exclusion, "UP/SP's system average URCS costs for the categories of maintenance and operating costs covered by the trackage rights fee."

The Board also noted that BNSF has been successful in establishing a competitive presence over the trackage rights lines during a period in which the disputed items have been incorporated in its trackage rights fees, and that, while BNSF argues that it will be unable to maintain that success if the disputed items continue to be incorporated in the trackage rights fees, the disputed items are a very small fraction of the total costs of BNSF's movements involving the trackage rights lines.

The Board concluded that, although BNSF has not shown that the disputed items should be excluded (in the years in which they would otherwise be included) from the URCS calculations required to create the Section 12 adjustment factor,

BNSF should be given a further opportunity--in accordance with a procedural schedule set out in Decision No. 96--to demonstrate that the disputed items should be omitted from the URCS calculations required to create the Section 12 adjustment factor. The Board indicated that it is giving BNSF this additional opportunity because it is important that the trackage rights fee adjustment mechanism work as intended, so that any increases or decreases in UP's costs are properly reflected in the agreed-upon adjustments to the trackage rights fee.

The Board issued Decision No. 95 in Finance Docket No. 32760 on March 4, 2002. Decision No. 96 was issued today. Vice Chairman Burkes commented by separate expression in Decision No. 96. A printed copy of each decision is available for a fee by contacting **D~ 2 D~ Legal Copy Service, Suite 405, 1925 K Street, N.W., Washington, DC 20006, telephone (202) 293-7776**, or via da2dalegal@earthlink.net. The decisions also are available for viewing and downloading via the Board's website at <http://www.stb.dot.gov>.

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