

Surface Transportation Board Issues Decision Resolving Trackage-Rights Dispute Arising from "Union Pacific-Southern Pacific" Railroad Merger

Surface Transportation Board (Board) Chairman Linda J. Morgan announced today that the Board has issued a decision, Decision No. 98, resolving a dispute relative to the mechanism for adjusting fees applicable to the railroad trackage rights acquired by The Burlington Northern and Santa Fe Railway Company (BNSF) in connection with the 1996 "Union Pacific-Southern Pacific" (UP-SP) railroad merger.

Background. The initial rates applicable to the BNSF trackage rights (involving one railroad's rental of the use of its lines to another railroad) were established in Section 9(a) of the BNSF Agreement (the document containing a complete description of the rights granted to BNSF in connection with the merger). Section 12 of the BNSF Agreement provides for the "adjustment" of 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 resolved by Decision No. 98 concerns two component items 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 URCS costs. The first disputed item is the so-called "acquisition premium," the excess of the price paid to acquire the SP railroads over the pre-acquisition book value of those railroads. The second disputed item concerns the costs of certain capacity improvements undertaken by UP on the trackage rights lines that have been 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 BNSF and even though the BNSF Agreement generally requires that both UP and BNSF 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 Earlier Decision. As described in Surface Transportation Board "News" release No. 02-12 issued March 21, 2002, the Board, in Decision No. 96 issued on that date, addressed the dispute that it is resolving in Decision No. 98 being issued today. In Decision No. 96, the Board concluded that, although BNSF had 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 to demonstrate that the disputed items should be omitted from the URCS calculations required to create the Section 12 adjustment factor. The Board stated that it was 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 agreed-upon adjustments to the trackage rights fee.

Today's Decision. In Decision No. 98, the Board has resolved the dispute first addressed in Decision No. 96. In today's decision, the Board determined that BNSF has not shown that the effects of the disputed items should be omitted from the calculations used to determine annual adjustments to the trackage rights fees paid by BNSF to UP for the trackage rights received by BNSF in the UP-SP merger proceeding. The Board specifically determined that inclusion of the effects of the disputed items in the fee-adjustment process would not amount to a double-count, and that the evolution of the fee-adjustment mechanism now contained in Section 12 of the BNSF Agreement does not support the view of BNSF and the American Chemistry Council (formerly the Chemical Manufacturers Association) that the adjustment mechanism must necessarily incorporate only URCS costs for post-mergers years, or disregard the effects of the disputed items. To incorporate UP's projected post-merger efficiencies in the trackage rights fees, the Board pointed out, would necessarily

mean an adjustment mechanism that would use UP's pre-merger, not post-merger, costs as a base. The Board concluded that, absent any compelling evidence to the contrary, the URCS costs used in the Section 12 adjustments must be developed in accord with its Uniform System of Accounts and its standard costing procedures and that no document or evidence presented during the course of the UP-SP merger proceeding contains any indication that the parties ever contemplated that the URCS calculations required by Section 12 would not be performed in that manner.

The Board, in today's decision, further noted that there is no competitive justification for departing from the plain language of Section 12 in adjusting the trackage rights fees that have been in place. The Board explained that, as the Board has noted on several prior occasions, BNSF has continued to effectively replace the competition that otherwise would have been lost when SP was absorbed into UP. The Board specifically noted that BNSF's trackage rights fees under the Section 12 fee-adjustment process are almost 10 percent below the fees that BNSF would now be paying under the adjustment mechanism to which it initially agreed, and are also considerably below the trackage rights fees the Board would have set under its governing compensation methodology had the parties not agreed to lower charges.

In addition to resolving the dispute before it in this case, the Board also ordered UP and BNSF to provide certain information pertaining to the implementation of Section 12, including a revised Section 12 to reflect how it has been implemented. The Board provided that these filings are due 30 days from the date of issuance of Decision No. 98. The Board then went on to establish a new formal approval process for that provision, under which interested parties may submit comments to the Board on the railroads' filings within 20 days after the railroads have made their submission to the Board.

The Board issued Decision No. 98 today 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, Decision No. 98. Chairman Morgan commented in a separate expression.

A printed copy of the 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 decision also is available for viewing and downloading via the Board's website at <http://www.stb.dot.gov>.

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