

**SURFACE TRANSPORTATION BOARD ORDERS EFFICIENCY-PRODUCING CHANGES IN HOUSTON AS PART OF "UP/SP" OVERSIGHT PROCEEDING, BUT DOES NOT GRANT REQUESTS FOR OPEN ACCESS**

Surface Transportation Board (Board) Chairman Linda J. Morgan and Vice Chairman Gus A. Owen announced today that, in decisions issued in the "UP/SP Merger Oversight" proceedings, including the "Houston/Gulf Coast Oversight" proceeding, the Board ordered efficiency-producing changes in Houston, but did not grant requests for "open access."

As part of its decision approving the merger between the Union Pacific (UP) and the Southern Pacific (SP) railroad systems in 1996, the Board provided for five years of oversight to ensure that conditions that the Board had imposed were effective in mitigating potential competitive harm. Thus, once a year, the Board issues a decision addressing that matter. Additionally, in connection with the recent rail service crisis in the western United States, the Board initiated a separate proceeding to consider requests by various parties for conditions that would modify the way in which rail service is provided in the Houston/Gulf Coast area. The Board issued decisions today in both proceedings.

**Houston/Gulf Coast Oversight.** Although the Houston/Gulf Coast Oversight proceeding was brought against a backdrop of the service emergency that crippled railroads in the West for months--with effects that the Board recognized were serious, and that must be avoided in the future--the Board found that in many respects the case represented a continuation of the original merger proceeding. In the merger, UP paid a substantial purchase price for the entire SP system, which had a poor infrastructure but an attractive shipper base, particularly in the Houston area. In the merger proceeding, several parties had sought to open up access by having UP ordered to allow other railroads to serve shippers that were on its lines. The Board in the merger proceeding adopted several conditions to preserve competition, but it did not open up access as those parties sought. Many of those same parties returned to the Board in the Houston/Gulf Coast Oversight proceeding, seeking much of what they had sought unsuccessfully in the merger proceeding.

Relief Granted. In its decision in the Houston/Gulf Coast Oversight proceeding, the Board adopted a so-called "clear route" condition to enhance efficiency and facilitate the smooth movement of railcars through the Houston Terminal. Under the "clear route" condition, the neutral and highly efficient joint UP/Burlington Northern Santa Fe Railway Company (BNSF) dispatching center at Spring, TX, will have the authority through its Joint Director to route traffic through Houston over any available route, even a route over which the owner of the train does not have operating authority. Thus, as a result of the Board's decision, a BNSF train may be permitted to operate over track of UP; a UP train may be permitted to operate over track of BNSF; and a Texas Mexican Railway Company (Tex Mex) train may be permitted to operate over track of either UP or BNSF.

The Board also granted a request by Capital Metro Transit Authority (CMTA) to alter the trackage rights and interchange arrangement provided for in the merger proceeding between BNSF and CMTA's operator, Longhorn Railroad (Longhorn). BNSF supported the request, which UP opposed. CMTA stated that, without the change, Longhorn would likely go out of business, thereby depriving shippers of needed rail service.

Other Actions. Additionally, the Board directed UP to consult with the Port of Houston and the Houston Partnership as to how it is carrying out its infrastructure plan for the Houston/Gulf Coast region, and to report on the matter annually. As to several other situations that were raised, such as the membership of the Port Terminal Railroad Association, the Board found that private sector resolutions were moving forward, and that Board involvement was thus not appropriate at this time. Similarly, the Board declined to rule one way or the other as to concerns over operational changes that UP might make in the future, noting that UP has committed to give advance notice of its operational changes and to make all necessary accommodations to preserve competitive operations over its lines.

However, the Board decided not to adopt the so-called "Consensus Plan" sponsored by a group of shippers, two affiliated railroads, and the Railroad Commission of Texas. The Board noted that it understood and shared Houston's interest in averting a future service crisis, but it stated that it would not undo the merger in the way that had been proposed, noting that once the merger was implemented, it had helped to solve the emergency. The Board concluded that the Consensus Plan, which would effectively undo the merger in the Houston area, conflicts with its governing statute and with fundamental policies underlying it.

Discussion of Open Access. The Board noted that the Consensus Plan is premised on the idea that shippers should, wherever possible, be served by more than one railroad, even if, in order to produce such a system, railroads that own the majority of an area's rail infrastructure would be required to share their property with others that do not. Here, it pointed out, the conditions that the Consensus Plan parties seek would add two new competitors--BNSF and Tex Mex--for numerous Houston-area shippers that were served by only one carrier before the merger, and that therefore had not lost competitive rail service as a result of the merger. Finding that the Consensus Plan is not necessary to remedy any merger-related harm, the Board concluded that it effectively constitutes open access and that, if it were adopted, there would be no basis on which the Board could refuse to provide for open access throughout the rail system. The Board stated:

Whether an open access regulatory scheme for the railroad industry is good for carriers, shippers, and the Nation, absent demonstrated merger-related harm open access . . . is not provided for in the statute that the Board currently administers, and thus, in our view, is a matter more appropriately debated in Congress.

Other Statutory Tenets. The Board also reviewed the existing railroad statutes in other respects. It noted that well-established transportation law recognizes that some shippers are served by a single railroad, and that such "captive shippers" may pay higher rates under "demand-based differential pricing" legal principles that govern the railroad industry, to reflect the economies of the railroad industry and the fact that some rail traffic is more captive and some more competitive. Because the railroad industry is not an open access industry, and because some shippers may pay more than others under the law that the Board administers, merger proceedings are not used as vehicles to equalize the competitive positions of shippers generally. The Board noted that it does impose competitive conditions to ensure that a merger does not put shippers into a worse position than they were in before, and it imposed several such conditions in this case. But, it stated, a well-established principle of rail merger law is that the conditions that the Board imposes in a merger proceeding are designed to ameliorate specific merger-related harm, and not to simply add more competitors.

The Board noted that another principle of transportation merger law is that the conditions adopted not be disproportionate. Here, the Board decided to ameliorate potential competitive harm through extensive trackage rights to BNSF. The Consensus Plan parties had argued that the BNSF trackage rights have not been adequate to achieve the Board's objectives. Rather than attempting to improve upon the less intrusive remedy that the Board had adopted, however, the Consensus Plan would move immediately to the most extreme remedy possible. Even if there were additional harm that the initial conditions did not fully ameliorate, the Board found that the Consensus Plan remedies--which do not seek to improve the existing remedies, but rather to set up far more drastic and intrusive ones--would be disproportionate.

In this regard, the Board noted that, during the proceeding, the parties argued at some length about when a government-imposed merger condition constitutes a "taking" of property. The Board found that the answer depends on the facts of the case. It pointed out that narrowly tailored merger conditions imposed to address merger-related harm are not considered a taking, but overreaching, disproportionate conditions could become confiscatory. And it recognized that once a merger has been consummated, and the carrier can no longer choose to walk away from it, the imposition of disproportionate new conditions becomes increasingly inconsistent with notions of commercial certainty and fairness.

Infrastructure Issues. Finally, the Board addressed the argument made during the proceeding by the Consensus Plan parties that adding more competitors in Houston would be appropriate because carriers and the shippers they serve will, as a rule, invest in their businesses and in infrastructure only where there is competition. For example, in this case, Dow Chemical and Formosa Plastics indicated that, if they obtain additional rail service, they would consider paying for infrastructure improvements, and Tex Mex indicated that it would consider investing in Houston infrastructure, but only if

the restriction limiting the service it can provide for Houston shippers is removed. In response to these arguments, UP pointed out that reducing its revenues by adding competitors for its more lucrative business (without providing it the opportunity to compete for other carriers' more captive traffic) would undercut its ability to invest in infrastructure. Thus, UP argued, even if Dow, Formosa, and Tex Mex did make investments, which they would expect to recover in rate reductions (or in Tex Mex's case additional traffic), the net effect would be that UP would reduce its investment and that investment overall would be lower.

The Board addressed these arguments with the following observations:

UP has promised to invest \$1.4 billion in Houston area infrastructure if the Consensus Plan is not adopted. There is no way to determine on this record whether the Consensus Plan would ultimately produce, for the Houston infrastructure, more, less, or the same level of investment. Indeed, more broadly, we cannot determine here, and do not need to determine here, how the railroad system would evolve if open access were adopted in Houston and, ultimately, the rest of the Nation: it could have unknown but significant effects on infrastructure, employment, and traffic patterns. Perhaps the plastics and chemicals shippers in Houston, with their high-volume, lucrative traffic, would indeed be net beneficiaries of an open access system, while small, lower-volume shippers in rural areas could lose their rail service entirely. Perhaps short-line railroads would step in to provide service to some shippers on lines that might be abandoned by the larger railroads. And perhaps the Federal government or state agencies would provide funds to augment infrastructure funding and to ensure that any such abandonments would not occur.

Right now, however, we have a commitment from UP to make sizable and sorely needed investments in the Houston area infrastructure, which were not capable of being made by the financially weakened SP before UP took it over. Whatever the merits of the "more-competitors-enhance-infrastructure-investment" argument, they are more appropriately made in an open access debate before Congress involving the entire rail system than in this case.

**General Oversight.** A variety of parties also sought additional conditions in the general oversight proceeding. The Board found, however, that most of those requests were tied to the service crisis that has now ended, and that neither they nor any of the other requests that were made were associated with merger-related harm. Accordingly, the Board did not grant new conditions in the general oversight proceeding, although it indicated that it would continue to monitor the merger implementation.

The Board's decisions were issued in Union Pacific Corp.--Control and Merger--Southern Pacific Rail Corp. [Houston/Gulf Coast Oversight], [Finance Docket No. 32760 \(Sub-No. 26\), Decision No. 10 \(STB served Dec. 21, 1998\)](#), and Union Pacific Corp.--Control and Merger--Southern Pacific Rail Corp., [Finance Docket No. 32760 \(Sub-No. 21\), Decision No. 13 \(STB served Dec. 21, 1998\)](#).

The Board's decisions are available on the Board's web site at [www.stb.dot.gov](http://www.stb.dot.gov).

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