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BEFORE THE SURFACE TRANSPORTATION BOARD

FINANCE DOCKET NO. 36500

CANADIAN PACIFIC RAILWAY LIMITED, *ET AL.* – CONTROL – KANSAS CITY SOUTHERN, *ET AL*.

APPLICANTS' MOTION TO COMPEL THE PRODUCTION OF DOCUMENTS REQUESTED IN DISCOVERY REQUESTS TO CSX TRANSPORTATION INC

EXPEDITED HANDLING REQUESTED

William A. Mullins
BAKER & MILLER PLLC
Suite 3000
2401 Pennsylvania Ave, N.W.
Washington, D.C. 20037
Email: wmullins@bakerandmiller.com
Telephone: (202) 663-7823

Adam J. Godderz
The Kansas City Southern Railway Company
P.O. Box 219335
Kansas City, MO 64121-9335
Email: agodderz@kcsouthern.com

Counsel for KCS

David L. Meyer
LAW OFFICE OF DAVID L. MEYER
1105 S Street NW
Washington, D.C. 20009
Email: David@MeyerLawDC.com
Telephone: (202) 294-1399

SULLIVAN & CROMWELL LLP
Adam S. Paris
1888 Century Park East, Suite 2100
Los Angeles, California 90067-1725
Email: parisa@sullcrom.com

Samantha F. Hynes
1700 New York Avenue, N.W., Suite 700
Washington, D.C. 20006-5215
Email: hyness@sullcrom.com
Telephone: (202) 956-7520

Jeffrey J. Ellis
Canadian Pacific
7550 Ogden Dale Road S.E.
Calgary, AB T2C 4X9 Canada
Email: Jeff_Ellis@cpr.ca
Telephone: (888) 333-6370

Counsel for CP

March 30, 2022

BEFORE THE SURFACE TRANSPORTATION BOARD

Finance Docket No. 36500

CANADIAN PACIFIC RAILWAY LIMITED, ET AL. –
–CONTROL– KANSAS CITY SOUTHERN, ET AL.

APPLICANTS' MOTION TO COMPEL
DISCOVERY FROM CSX TRANSPORTATION INC.

Applicants[1] submit the following motion to compel discovery from CSX Transportation Inc. ("CSXT") in response to their refusal to comply with Applicants' First Discovery Request.

I. Introduction

CSXT refuses to comply with Applicants' First Discovery Request to CSXT ("Request"), served on February 23, 2022—exactly five weeks ago. In that Request, Applicants asked for complete traffic tape data for the entire CSXT system for the years 2018, 2019, 2020 and 2021. Applicants have since reluctantly abandoned their Request for all years except for 2019, as a compromise and in a good faith attempt to expedite the process. On March 25, Applicants and CSXT participated in a conference call with Judge Thomas P. McCarthy, the administrative law judge responsible for overseeing the above-captioned proceeding, to resolve the conflict. Although Judge McCarthy did not rule on the issue, he stated he was inclined to conclude that Applicants' Request is relevant. Applicants and CSXT have met and conferred twice and to this day, CSXT still objects to producing its traffic tape data for 2019, which

[1] Applicants are Canadian Pacific Railway Limited, Canadian Pacific Railway Company, and their U.S. rail carrier subsidiaries Soo Line Railroad Company, Central Maine & Quebec Railway US Inc., Dakota, Minnesota & Eastern Railroad Corporation, and Delaware and Hudson Railway Company, Inc. (collectively, "CP") and Kansas City Southern, the Kansas City Southern Railway Company, Gateway Eastern Railway Company, and The Texas Mexican Railway Company (collectively, "KCS").

jeopardizes Applicants' ability to adequately review and respond to issues raised by CSXT and other parties in their Comments and Request for Conditions ("Comments").

II. Background

On February 23, Applicants served the following discovery request on CSXT:

> 1. Produce complete traffic tape data for the years 2018, 2019, 2020, and 2021, including all available data records for both loaded and empty movements and revenue and non-revenue movements for the entire CSXT system, and including standard fields of information typically provided to the STB when preparing the Carload Waybill Sample.

Ex. A (CSXT R&Os to Applicants' First Discovery Request, at 1).

The same day, Applicants also served essentially the same request on Norfolk Southern, BNSF Railway Company, Union Pacific and Canadian National Railway Company and asked to receive a response within five days of service, considering that their request was short and straightforward and referred to a concept (100% traffic tapes) known and well understood by all Class 1 railroads. On Sunday, February 27 at 5:25 pm EST, the day before the Response to Applicants' Request was due, CSXT requested at 10-day extension to provide their Responses and Objections ("R&Os") to that one Request. Applicants agreed to give CSXT a four-day extension to respond, which CSXT complied with. Ex. B ([EXTERNAL] STB Docket No. FD36500 - Request for Extension on Responses to Applicants' First Set).

CSXT's response, which it was hoping to get 15 days to provide, was four sentences long. CSXT fully objected to Applicants' Request because, it argued, the Request is unduly burdensome, overbroad, irrelevant and vague. Ex. A (CSXT R&Os to Applicants' First Discovery Request, at 1-2).

On March 8, Applicants provided CSXT with the particular fields from the traffic tape data that Applicants wished to see included in the production. Three days later, CSXT responded that it still objected to producing the requested data because "[it] is not relevant to the Application, which was filed on October 29, 2021, using 2019 traffic data as the base year for the application, or to CSXT's comments in response." *See* Ex. C ([EXTERNAL] Re: Applicants' First set of Discovery Requests to CSXT).

While some other Class 1 railroads had either reservations or questions about Applicants' request for 100% traffic tapes, none of them ever argued that they were not relevant. These railroads have all either produced the data requested already, or have agreed to do it and are working towards the delivery.

On March 14, Applicants explained to CSXT the reasons why the traffic tape data is relevant to their case and to their response to the issues raised in Comments and involving CSXT traffic flow. Receiving no response from CSXT, Applicants followed up on March 17. Later that day, CSXT told Applicants they were unwilling to produce any traffic data. *See* Ex. C ([EXTERNAL] Re: Applicants' First set of Discovery Requests to CSXT). The only objection remaining between the parties is relevance. On March 18, Applicants wrote to Judge Thomas P. McCarthy, to rule on whether Applicants are entitled to CSXT's traffic tape data that they had requested weeks prior. *See* Ex. D (FD 36500, Canadian Pacific Ry., et al. – Control – Kansas City Southern, et. al).

Judge McCarthy agreed to hear the parties' position and stated he was inclined to conclude that Applicants' Request is relevant but requested that they meet and confer about this issue, which they did on two separate occasions (March 28 and March 29). The first day, the

parties made a lot of progress, and CSXT ordered the traffic tapes to be ready for production regardless of whether the parties would reach an agreement or whether the tapes would be obtained following a ruling on a motion to compel. Ex. E ([EXTERNAL] Re: Meet and Confer between Applicants and CSXT re: traffic tape data). However, the next day, CSXT attempted to use access to their traffic tapes as leverage to obtain documents they request from KCS a lot sooner than they would normally be owed, to schedule the deposition of a KCS's witness on their schedule, and to request informal discussions with CP and KCS experts for four half-days before they would *decide* whether they provide the traffic tapes to Applicants or no. Applicants were of the view that CSX's proposal was unfair and they moved to compel.

A. The Applicable Relevance Standard Is Broad.

Pursuant to 49 C.F.R. § 1114.21, "[p]arties may obtain discovery . . . regarding any matter, not privileged, which is relevant to the subject matter involved in a proceeding . . . ." 49 C.F.R. § 1114.21(a)(1). Specifically, the Board has consistently recognized that "[t]he requirement of relevance means that the information *migh*t be able to affect the outcome of a proceeding." *Waterloo Rwy. Co–control–Can. Nat'l Rwy.*, 2003 WL 21009327, at *2 (S.T.B. May 6, 2003) (emphasis added); *see also Town of North Judson—Adverse Discontinuance of Serv.—In LaPorte, Porter, & Starke Counties, Ind*, 2015 WL 4620569, at *2 (S.T.B. Aug. 3, 2015)*; Ballard Term. Railroad Co.—Acquisition & Operation Exemption—Woodinville Subdivision.*, 2013 WL 4498193, at *2 (S.T.B. Aug. 22, 2013); *Reasonableness of BNSF Rwy. Co.*, 2012 WL 2378133, at *3 (S.T.B. Jun. 21, 2012)*; Oregon Int'l Port—Feeder Line Application—Coosbay Line*, 2008 WL 4153211, at *2 (STB Sept. 10, 2008); *CF Inds. Inc.* v. *Kaneb Pipe Line Partners*, 2004 WL 2669795, at *1 (STB Nov. 23, 2004).

Applicants are entitled to discover relevant information provided the discovery request is not unduly burdensome. 49 C.F.R. § 1114.21(a)(1), (c). CSXT's traffic tape data for 2019 is relevant because it allows Applicants to properly address issues that were raised in Comments and that involve CSXT's traffic flow. The requested data is easy to collect and customarily kept by railroads which participate in merger proceedings, making this dispute if not unique, certainly unusual. Although the current merger rules do not apply in the context of this proceeding, the Board surely sees it as beneficial for parties to a merger application to share their 100% traffic tapes since these current merger rules provide that:

> Applicants must indicate, as soon as practicable after the issuance of a protective order, that they will make their 100% traffic tapes available (subject to the terms of the protective order) to any interested party on written request. The applicants may require that, if the requesting party is itself a railroad, applicants will make their 100% traffic tapes available to that party only if it agrees, in its written request, to make its own 100% traffic tapes available to applicants (subject to the terms of the protective order) when it receives access to applicants' tapes." 49 C.F.R. § 1180.4(b)(4)(iii).

In March 2021, when Canadian Pacific filed a notice of intention to file a control application, it offered its 100% traffic tapes, and CN reciprocated. Applicants' 100% traffic tapes were included in their workpapers and sent to CSXT on November 5, 2021, almost six months ago.

B. Applicants' Request Is Relevant.

The traffic tape data that Applicants are seeking to obtain from CSXT is highly relevant to the outcome of this case because without it, Applicants must address the traffic-related issues raised by CSXT and others using the Board's waybill information, which is a sample and may not include all the moves relevant to their analysis.

In the context of its Comments, CSXT has repeatedly raised issues involving its traffic flow, thereby making its 100% traffic tapes *de facto* relevant to the outcome of this proceeding. It has done so, for example, by asserting that the CPKC Application ("Application") "threatens to reduce competition over rail gateways connecting the eastern and western United States." Ex. F (CSXT Comments and Request for Conditions, at 1). CSXT makes this assertion in part because it claims the Application will have the effect of "reducing the ability of CSXT and KCSR to interchange traffic in New Orleans on commercially reasonable terms, and . . . reducing competition between the eastern and western U.S. by downgrading and reducing traffic volume over the KCSR line between Kansas City and East St. Louis." *Id.* at 1-2. CSXT's traffic tape data will help Applicants construct a complete picture of traffic flows in those areas. This will help Applicants assess whether CSXT's concerns have any basis at all, and if so, whether conditions proposed by CSXT are necessary or even helpful. *E.g., id.* at 23. (CSXT asks "the Board impose a condition . . . that requires CPKC . . . to maintain commercially reasonable rates and provide service at or above current service levels commensurate with shipper demand to maintain CSXT's opportunity to compete effectively for traffic that can move most efficiently over the E[ast] S[aint] L[ouis]-Kansas City Line to and from points on CSXT east of E[ast] S[aint] L[ouis].").

Other parties have also raised competitive concerns regarding the Springfield Line. *See, e.g.*, Ex. G (CN's Comments on Application and Request for Conditions, at 64) ("In light of the competitive concerns and threat to the adequacy of post-merger transportation discussed above, the Board should require divestiture to CN's U.S. subsidiary, Illinois Central, of the Springfield Line."). Because CSXT's traffic tape data will help Applicants develop a

complete picture of the traffic flow, it will also assist Applicants in understanding and responding to the concerns and any proposed conditions of these and other parties.

Further, in addition to CSXT, other parties have also put CSXT traffic flows at issue. UP has asserted as part of its proposed condition that Applicants' commitment to keep the Laredo Gateway open on "commercially reasonable" terms applies when "UP interlines with CSXT . . . to move traffic to the East in competition with CPKC (or CPKC and NS or CSX)." Ex. H (Union Pacific ("UP") Comments and Request for Conditions, at 23-24). UP's Thomas Haley Verified Statement notes that "[t]he Chicago-Laredo lane is of particular significance in this case, and states that "[o]f Applicants' projected diversions of 33,218 automotive carloads, about 60% involve movements between Mexico and Chicago (including traffic to Chicago interchanges with CSX and NS)." Ex. H (UP Comments and Request for Conditions, Haley V.S. at 20). CSXT's traffic tape data will help Applicants respond to these assertions as well.

These examples are non-exhaustive, but clearly establish that CSXT does not need to make arguments based on traffic flow to make traffic data information that might affect the outcome of this proceeding. CSXT's 100% traffic tapes are clearly relevant and as such, Applicants are entitled to obtain them through discovery.

C. Expedited Handling is Warranted.

The exceptional circumstances of this particular Request warrant an expedited handling. First, Applicants have served their Discovery Request to CSXT five weeks ago and are still arguing over the relevance of traffic tapes, which are routinely shared by parties to a merger under normal circumstances. Second, the parties have already explained the issue to

Judge McCarthy and been given their fair chance to explain their positions, which are unlikely to have changed and which resulted in Judge McCarthy stating he was inclined to conclude that Applicants' Request is relevant and should be granted for 2019 traffic tape data. Third, CSXT requested the preparation of the traffic tapes in the morning of March 28, confirming that they would be ready within a few days, at most – therefore, the traffic tapes are now ready and can be produced immediately following an hearing and an Order on Friday, April 1, 2022. S*ee* Ex. E ([EXTERNAL] Re: Meet and Confer between Applicants and CSXT re: traffic tape data).

III. Conclusion

Applicants request a response to this motion from CSXT within 24 hours, in light of the fact that all of the issues have been fully aired before Your Honor. Applicants respectfully request a hearing on Friday, April 1 on the central issue of this Request: the relevance of CSXT's 100% traffic tapes to the issues raised in this proceeding. CSXT has already formally confirmed having prepared the tapes for production, and as such, they can be produced on Friday following the hearing if this motion is granted.

Respectfully submitted,

Dated: March 30, 2022

/s/ William A. Mullins
William A. Mullins
Erin A. Glavich
BAKER & MILLER PLLC
2401 Pennsylvania Ave., N.W.
Suite 300
Washington, DC 20037
Telephone: (202) 663-7820
Facsimile: (202) 663-7849

Adam J. Godderz

/s/ David L. Meyer
David L. Meyer
Law Office of David L. Meyer
1105 S Street NW
Washington, D.C. 20009
Email: David@MeyerLawDC.com
Telephone: (202) 294-1399

Adam S. Paris
Sullivan & Cromwell LLP
1888 Century Park East
Los Angeles, CA 90067-1725
Email: parisa@sullcrom.com

THE KANSAS CITY SOUTHERN
RAILWAY COMPANY
P.O. Box 219335
Kansas City, MO 64121-9335
Telephone: (816) 983-1360
Facsimile: (816) 983-1227

Counsel for KCS

Telephone: (310) 712-6663

Samantha F. Hynes
Sullivan & Cromwell LLP
1700 New York Avenue, N.W., Suite 700
Washington, D.C. 20006-5215
Email: hyness@sullcrom.com
Telephone: (202) 956-7520

Jeffrey J. Ellis
Canadian Pacific
7550 Ogden Dale Road S.E.
Calgary, AB T2C 4X9 Canada
Email: Jeff_Ellis@cpr.ca
Telephone: (888) 333-6370

Counsel for CP

CERTIFICATE OF SERVICE

I hereby certify that I have caused the foregoing Motion to Compel Production from CSXT to be served electronically or by first-class mail, postage pre-paid, on all parties of record in these proceedings.

/s/ Marc-André Cyr

March 30, 2022

Exhibit A

BEFORE THE
SURFACE TRANSPORTATION BOARD

Docket No. FD 36500

CANADIAN PACIFIC RAILWAY LIMITED; CANADIAN PACIFIC RAILWAY COMPANY; SOO LINE RAILROAD COMPANY; CENTRAL MAINE & QUEBEC RAILWAY US INC.; DAKOTA, MINNESOTA & EASTERN RAILROAD CORPORATION; AND DELAWARE & HUDSON RAILWAY COMPANY, INC.
—CONTROL—
KANSAS CITY SOUTHERN; THE KANSAS CITY SOUTHERN RAILWAY COMPANY; GATEWAY EASTERN RAILWAY COMPANY; AND THE TEXAS MEXICAN RAILWAY COMPANY

CSX TRANSPORTATION INC.'S RESPONSES AND OBJECTIONS TO APPLICANTS' FIRST SET OF DISCOVERY REQUESTS

CSX Transportation Inc. ("CSXT") hereby responds to Applicants' First Set of Discovery Requests to Union Pacific Railroad Company as follows:

Request No. 1:

Produce complete traffic tape data for the years 2018, 2019, 2020, and 2021, including all available data records for both loaded and empty movements and revenue and non-revenue related movements for the entire CSXT system, including standard fields of information provided to the STB when preparing the Carload Waybill Sample.

Objection and Response to Request No. 1:

CSXT objects to Applicants' request as unduly burdensome and overbroad in that, and to the extent that, it seeks information that is not relevant to the consideration of the Application or to CSXT's comments. CSXT also objects to the request as vague in that it refers generally to "traffic tape data" and appears to require something more than would be submitted as part of the Carload Waybill Sample. Without prejudice to the foregoing objections, CSXT further objects to Instruction No. 4 to the extent that it is inconsistent with the treatment of Highly Confidential

material prescribed in the Protective Order. CSXT is willing to meet and confer with Applicants to attempt to understand the nature of the data they are seeking and the reasons for the request.

Respectfully submitted,

/s/ Paul A. Cunningham

Kent A. Gardiner
Ryan C. Tisch
Crowell & Moring LLP
1001 Pennsylvania Avenue NW
Washington, DC 20004-2595
(202) 624-2674
rtisch@crowell.com

Paul A. Cunningham
Harkins Cunningham, LLP
1750 K Street NW, Suite 300
Washington, DC 20006
(202) 415-4026
pac@harkinscunningham.com

Steven C. Armbrust
CSX Transportation, Inc.
500 Water Street
Jacksonville, FL 32202
(904) 359-3276

Louis E. Gitomer
Law Offices of Louis E. Gitomer, LLC
600 Baltimore Avenue, Suite 301
Towson, MD 21204
(410) 296-2250
Lou@lgraillaw.com

Attorneys for CSX Transportation, Inc.

Dated: March 4, 2022

cc: All Parties of Record
ALJ McCarthy

CERTIFICATE OF SERVICE

I hereby certify that I have caused the foregoing CSX Transportation's Responses and Objections to Applicants' First Set of Discovery Requests in Docket No. FD-36500, *Canadian Pacific Railway Limited; Canadian Pacific Railway Company; Soo Line Railroad Company; Central Maine & Quebec Railway US Inc.; Dakota, Minnesota & Eastern Railroad Corporation; and Delaware & Hudson Railway Company, Inc. – Control – Kansas City Southern, The Kansas City Southern Railway Company, Gateway Eastern Railway Company, and The Texas Mexican Railway Company*, to be served electronically or by first class mail, postage pre-paid, on all parties of record in this proceeding.

S/ Paul A. Cunningham

Paul A. Cunningham
Attorney for CSX Transportation, Inc.

March 4, 2022

Exhibit B

Golden, Nathan H.

From: Paris, Adam S.
Sent: Sunday, February 27, 2022 7:16 PM
To: nkling@harkinscunningham.com
Cc: Cyr, Marc-André O.; pac@harkinscunningham.com
Subject: RE: [EXTERNAL] STB Docket No. FD36500 - Request for Extension on Responses to Applicants' First Set

Neil – We are amenable to an extension through Friday, March 4, which should be more than sufficient to produce the traffic tapes.

From: nkling@harkinscunningham.com
Sent: Sunday, February 27, 2022 2:25 PM
To: Paris, Adam S.
Cc: Cyr, Marc-André O. ; pac@harkinscunningham.com
Subject: [EXTERNAL] STB Docket No. FD36500 - Request for Extension on Responses to Applicants' First Set

Adam:

In view of the opposition filings tomorrow, CSXT requests a 10 day extension of time, until March 9, 2022, to respond to Applicant's First Set of Discovery to CSX Transportation. Your anticipated courtesy is appreciated.

Best,

Neill

Neill C. Kling
Harkins Cunningham LLP
1055 Westlakes Drive, Suite 300 Berwyn, PA 19312
Direct: 215.851.6709 | Main: 215.851.6700 | Fax: 215.851.6710
nkling@harkinscunningham.com | www.harkinscunningham.com [harkinscunningham.com]

****This is an external message from:** nkling@harkinscunningham.com ******

Exhibit C

Cyr, Marc-André O.

From: Cyr, Marc-André O.
Sent: Thursday, March 17, 2022 8:10 PM
To: 'nkling@harkinscunningham.com'
Cc: 'david@meyerlawdc.com'; Hynes, Samantha F.; 'Lou@lgraillaw.com'; 'pac@harkinscunningham.com'; Paris, Adam S.; 'rtisch@crowell.com'; 'wmullins@bakerandmiller.com'
Subject: RE: [EXTERNAL] Re: Applicants' First set of Discovery Requests to CSXT

Mr. Kling:

We will reach out to Judge McCarthy to seek assistance in resolving the dispute over the traffic tapes.

Regards,

Marc-André Cyr
Sullivan & Cromwell LLP
T: (857) 209- 1986 | cyrm@sullcrom.com

From: nkling@harkinscunningham.com <nkling@harkinscunningham.com>
Sent: Thursday, March 17, 2022 2:33 PM
To: Cyr, Marc-André O. <cyrm@sullcrom.com>
Cc: 'david@meyerlawdc.com' <david@meyerlawdc.com>; Hynes, Samantha F. <hyness@sullcrom.com>; 'Lou@lgraillaw.com' <Lou@lgraillaw.com>; 'pac@harkinscunningham.com' <pac@harkinscunningham.com>; Paris, Adam S. <Parisa@sullcrom.com>; 'rtisch@crowell.com' <rtisch@crowell.com>; 'wmullins@bakerandmiller.com' <wmullins@bakerandmiller.com>
Subject: RE: [EXTERNAL] Re: Applicants' First set of Discovery Requests to CSXT

Mr. Cyr:

CSXT remains unwilling to produce the requested information.

Applicants have failed to articulate the relevance of their request. Your stated need for “traffic flow information” to support the Transaction is not explained. And it seems to be untimely. Any such information should have been provided by Applicants with the Application.

Are you suggesting that Applicants now believe the information in the Application is inaccurate and that their market impact analysis (including the potential traffic diversions from CSXT) and operating plan are both based on inaccurate or incomplete information?

As your request may pertain to CSXT’s recent comments, Applicants have access to any relevant information. Regarding New Orleans and East St. Louis, KCS has the traffic flow information pertaining to traffic interchanged between CSXT and KCS. Traffic handled by CSXT to and from Mexico is all handled at some point during the move by KCSM. As regards the Meridian Speedway, KCS, as an independent carrier or as a participant in the NS-KCS arrangements related to the MSLLC, has access to any information that might be available to CSXT.

Finally, regarding your reference to the new rules (by which we assume you mean 49 CFR 1180.4(b)(4)(iii) (2020)), Applicants vigorously sought to avoid the use of the new rules and obviously all of the principles that were the basis for them. Claiming the new rules as a basis for relevancy is contrary to that position.

Best regards,

Neill C. Kling
Harkins Cunningham LLP
1055 Westlakes Drive, Suite 300 Berwyn, PA 19312
Direct: 215.851.6709 | Main: 215.851.6700 | Fax: 215.851.6710
nkling@harkinscunningham.com | www.harkinscunningham.com [harkinscunningham.com]

From: "Cyr, Marc-André O." <cyrm@sullcrom.com>
To: "'nkling@harkinscunningham.com'" <nkling@harkinscunningham.com>
Cc: "'pac@harkinscunningham.com'" <pac@harkinscunningham.com>, "'rtisch@crowell.com'" <rtisch@crowell.com>, "'Lou@lgraillaw.com'" <Lou@lgraillaw.com>, "'wmullins@bakerandmiller.com'" <wmullins@bakerandmiller.com>, "'david@meyerlawdc.com'" <david@meyerlawdc.com>, "Paris, Adam S." <Parisa@sullcrom.com>, "Hynes, Samantha F." <hyness@sullcrom.com>
Date: 03/17/2022 10:33 AM
Subject: RE: [EXTERNAL] Re: Applicants' First set of Discovery Requests to CSXT

Mr. Kling,

I write to follow-up on CSXT's production of traffic tapes. Please let us know when you expect to produce this data.

Best,

Marc-André Cyr
Sullivan & Cromwell LLP
T: (857) 209- 1986 | cyrm@sullcrom.com

From: Cyr, Marc-André O.
Sent: Monday, March 14, 2022 11:08 AM
To: 'nkling@harkinscunningham.com' <nkling@harkinscunningham.com>
Cc: pac@harkinscunningham.com; rtisch@crowell.com; Lou@lgraillaw.com; wmullins@bakerandmiller.com; david@meyerlawdc.com; Paris, Adam S. <Parisa@sullcrom.com>; Hynes, Samantha F. <hyness@sullcrom.com>
Subject: RE: [EXTERNAL] Re: Applicants' First set of Discovery Requests to CSXT

Mr. Kling:

Applicants are trying to develop the most accurate traffic flow information—an exercise that is both relevant for the Application and for the Applicants' Response to Comments. This cannot be done using the STB waybill information only, because it is a sample that does not include all the moves and may not include the moves relevant to CSX's requests or the requests of others for which we need detailed traffic information.

Obtaining traffic tape data for 2018, 2019, 2020 and 2021 would provide a broader view into trends on specific lanes over this period as well as cover more interline routing options that have been used over this period, but CSX has simply no basis to refuse producing the data for 2019, which has been used for the base year. Under the new rules, the Board would have required carriers to exchange 100% traffic tapes, so it is clearly aware of the relevance of such data in the context of a merger.

We will proceed to the ALJ promptly absent some further reassurance of cooperation.

Best regards,

Marc-André Cyr
Sullivan & Cromwell LLP
T: (857) 209- 1986 | cyrm@sullcrom.com

From: nkling@harkinscunningham.com <nkling@harkinscunningham.com>
Sent: Friday, March 11, 2022 10:35 PM
To: Cyr, Marc-André O. <cyrm@sullcrom.com>
Cc: pac@harkinscunningham.com; rtisch@crowell.com; Lou@lgraillaw.com; wmullins@bakerandmiller.com; david@meyerlawdc.com; Paris, Adam S. <Parisa@sullcrom.com>; Hynes, Samantha F. <hyness@sullcrom.com>
Subject: [EXTERNAL] Re: Applicants' First set of Discovery Requests to CSXT

Dear Mr. Cyr:

This responds to your e-mail below. While we appreciate the detail that you provided concerning the request, CSXT's primary objection to providing all of its Traffic Tape Data is not ambiguity, but relevance. From CSXT's perspective, its traffic tape data is not relevant to the Application, which was filed on October 29, 2021, using 2019 traffic data as the base year for the application, or to CSXT's comments in response. Please inform us of what Applicants believe is the relevance of the CSXT Traffic Tape Data to the Application or the comments.

Best regards,

Neill C. Kling
Harkins Cunningham LLP
1055 Westlakes Drive, Suite 300 Berwyn, PA 19312
Direct: 215.851.6709 | Main: 215.851.6700 | Fax: 215.851.6710
nkling@harkinscunningham.com | www.harkinscunningham.com [harkinscunningham.com]

From: "Cyr, Marc-André O." <cyrm@sullcrom.com>
Date: March 8, 2022 at 18:53:18 EST
To: pac@harkinscunningham.com, rtisch@crowell.com, Lou@lgraillaw.com
Cc: wmullins@bakerandmiller.com, david@meyerlawdc.com, "Paris, Adam S." <Parisa@sullcrom.com>, "Hynes, Samantha F." <hyness@sullcrom.com>
Subject: Applicants' First set of Discovery Requests to CSXT

Counsel,

We served a request for production of your complete traffic tape data for years 2018, 2019, 2020 and 2021 on February 23. Although we do not view this request as ambiguous or vague, we are available to provide further clarity. Please provide waybill records for all revenue movements, empty and loaded, including the following information:

- Waybill Number
- Waybill Date
- Car Number and Initial (Container Number and Initial where applicable)
- AAR Car Type
- Car Ownership
- Shipper
- Consignee
- Freight Payer
- Number of Carloads/Units on Waybill
- Intermodal Service Code (As defined in STB's Carload Waybill Sample)
- Transit Code (As defined in STB's Carload Waybill Sample)
- Type of Move (As defined in STB's Carload Waybill Sample)
- 7-Digit STCC Commodity Code
- Lading Weight of Shipment
- Empty/Load Indicator
- Actual Miles
- Rebill Code
- Through Freight Revenues (where available)

- Through Fuel Surcharge Revenues (where available)
- Carriers' own division of through freight revenues
- Carriers' own division of through fuel surcharge revenues
- Payouts and revenue deductions from carriers' own division of revenues, including, but not limited to, payments to shortline and switching railroads
- Full route information for movement (including information sufficient to identify all railroads and junctions involved in the end-to-end movement)
    - Including, but not limited to, information sufficient to identify the ultimate origin and destination railroad SCACs and location FSACs , as well as the carriers' own on and off junctions points and receiving and forwarding railroads where applicable
- Pricing Authority
- Shipment termination timestamp (i.e., the date and time the shipment is released to the consignee)

Please produce this data this week.

Sincerely,

Marc-André Cyr
Sullivan & Cromwell LLP | 125 Broad Street |
New York, NY 10004-2498
T: (212) 558-3123 | F: (212) 558-3588 | C: (857) 209-1986
cyrm@sullcrom.com| http://www.sullcrom.com

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****This is an external message from:** nkling@harkinscunningham.com ******

Exhibit D

Golden, Nathan H.

From: Cyr, Marc-André O.
Sent: Friday, March 18, 2022 11:02 AM
To: 'tmccarthy@fmshrc.gov'; 'zbyers@fmshrc.gov'; 'ctolbert@fmshrc.gov'
Cc: 'nkling@harkinscunningham.com'; 'david@meyerlawdc.com'; Hynes, Samantha F.; 'Lou@lgraillaw.com'; 'pac@harkinscunningham.com'; Paris, Adam S.; 'rtisch@crowell.com'; 'wmullins@bakerandmiller.com'; 'eglavich@bakerandmiller.com'; Golden, Nathan H.; Sarnoff, Zachary A.; Heflin, Jason O.
Subject: FD 36500, Canadian Pacific Ry., et al. – Control – Kansas City Southern, et. al
Attachments: CSXT Responses and Objections 20220304.pdf; Applicants' First set of Discovery Requests to CSXT.pdf; Applicants' First Set of Discovery Requests to CSXT.pdf

Your Honor:

On behalf of Applicants, we are asking you to assist Applicants to resolve a disagreement between them and CSXT concerning Applicants' First Set of Discovery Requests.

On February 23, Applicants served on CSXT the following discovery request:

> 1. Produce complete traffic tape data for the years 2018, 2019, 2020, and 2021, including all available data records for both loaded and empty movements and revenue and non-revenue movements for the entire CSXT system, and including standard fields of information typically provided to the STB when preparing the Carload Waybill Sample.

The same day, Applicants also served essentially the same request on NS, BNSF, UP and CN. More than three weeks later, CSXT is the only railroad objecting to the production of <u>any</u> of its traffic tape data, because "[f]rom CSXT's perspective, its traffic tape data is not relevant to the Application, which was filed on October 29, 2021, using 2019 traffic data as the base year for the application, or to CSXT's comments in response." *See* Email from Neill C. Kling (on behalf of CSXT) to Marc-André Cyr, Adam Paris, William Mullins, David Meyer *et al.* (on behalf of Applicants) sent March 11, 2022 at 10:35 pm. Unlike this quote may seem to suggest, CSXT is *not* willing to share its traffic tape data for the year 2019, which served as the base year for the Application (or for any other year).

Applicants and CSXT's exchanges over the relevance of traffic tapes are no longer showing signs of progress towards a resolution and, for that reason, we are asking Your Honor to supervise a conference call over this narrow issue as soon as possible.

Attached to this email are Applicants' First Set of Discovery Requests, CSXT's Responses and Objections to Applicants' First Set of Discovery Requests and the entirety of the correspondence between them on this issue.

Please feel free to reach out to me with any questions.

Best regards,

Marc-André Cyr
Sullivan & Cromwell LLP | 125 Broad Street |
New York, NY 10004-2498
T: (212) 558-3123 | F: (212) 558-3588 | C: (857) 209-1986

cyrm@sullcrom.com| http://www.sullcrom.com

Exhibit E

Golden, Nathan H.

From: pac@harkinscunningham.com
Sent: Monday, March 28, 2022 9:02 AM
To: Cyr, Marc-André O.
Cc: rtisch@crowell.com; Lou@lgraillaw.com; wmullins@bakerandmiller.com; david@meyerlawdc.com; Paris, Adam S.; Hynes, Samantha F.; eglavich@bakerandmiller.com; Golden, Nathan H.
Subject: [EXTERNAL] Re: Meet and Confer between Applicants and CSXT re: traffic tape data

Hi, Marc.

This morning we commissioned NERA to begin preparing the CSXT data for such production as we ultimately agree.

Best wishes,

pac

Paul A. Cunningham
Harkins Cunningham LLP
1750 K Street, NW
Washington, DC 20006

Mobile: 202-415-4026
Fax: 202-973-7610
pac@harkinscunningham.com

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> On Mar 28, 2022, at 11:41, Cyr, Marc-André O. <cyrm@sullcrom.com> wrote:
>
> Paul and team,
>
> Thank you for the productive conversation this morning.
>
> I just wanted to confirm that we agree to pursue the meet and confer process tomorrow based on your commitment to discuss the matter with your client today and ensure that the traffic tapes are ready for production in the next few days, regardless of whether our negotiations are successful tomorrow (although we certainly hope so).
>
> Best,
>
> Marc-André Cyr
> Sullivan & Cromwell LLP
> T: (857) 209- 1986 | cyrm@sullcrom.com

-----Original Appointment-----
From: Cyr, Marc-André O.
Sent: Friday, March 25, 2022 2:43 PM
To: Cyr, Marc-André O.; 'pac@harkinscunningham.com'; 'rtisch@crowell.com'; 'Lou@lgraillaw.com'; 'wmullins@bakerandmiller.com'; 'david@meyerlawdc.com'; Paris, Adam S.; Hynes, Samantha F.; 'eglavich@bakerandmiller.com'; Golden, Nathan H.
Subject: Meet and Confer between Applicants and CSXT re: traffic tape data
When: Monday, March 28, 2022 9:00 AM-9:30 AM (UTC-05:00) Eastern Time (US & Canada).
Where: https://sullcrom.zoom.us/j/6079209799

Marc-André O. Cyr is inviting you to a scheduled Zoom meeting.

Join Zoom Meeting
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+1 346 248 7799 US (Houston)
833 548 0282 US Toll-free
877 853 5247 US Toll-free
888 788 0099 US Toll-free
833 548 0276 US Toll-free
+44 203 481 5240 United Kingdom
+44 203 901 7895 United Kingdom
+44 208 080 6591 United Kingdom
+44 208 080 6592 United Kingdom
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+44 131 460 1196 United Kingdom
+44 203 481 5237 United Kingdom
0 800 260 5801 United Kingdom Toll-free
0 800 358 2817 United Kingdom Toll-free
0 800 456 1369 United Kingdom Toll-free
0 800 031 5717 United Kingdom Toll-free
+61 3 7018 2005 Australia
+61 7 3185 3730 Australia
+61 8 6119 3900 Australia
+61 8 7150 1149 Australia
+61 2 8015 6011 Australia
1800 945 157 Australia Toll-free
1800 317 562 Australia Toll-free
1800 893 423 Australia Toll-free
+32 2 788 0173 Belgium

+32 1579 5132 Belgium
+32 2 290 9360 Belgium
+32 2 585 5574 Belgium
+32 2 588 4188 Belgium
+32 2 788 0172 Belgium
0 800 800 99 Belgium Toll-free
0 800 293 46 Belgium Toll-free
0 800 294 51 Belgium Toll-free
+86 10 8783 3177 China
+86 10 5387 6330 China
400 669 9381 China Toll-free
400 182 3168 China Toll-free
400 616 8835 China Toll-free
+33 1 7037 9729 France
+33 1 7095 0103 France
+33 1 7095 0350 France
+33 1 8699 5831 France
+33 1 7037 2246 France
0 805 543 065 France Toll-free
0 800 940 415 France Toll-free
0 800 944 049 France Toll-free
+49 69 7104 9922 Germany
+49 69 3807 9883 Germany
+49 69 3807 9884 Germany
+49 69 5050 0951 Germany
+49 69 5050 0952 Germany
+49 695 050 2596 Germany
0 800 000 6954 Germany Toll-free
0 800 1800 150 Germany Toll-free
0 800 588 9791 Germany Toll-free
0 800 000 1590 Germany Toll-free
+852 5803 3731 Hong Kong SAR
+852 5808 6088 Hong Kong SAR
+852 3008 3297 Hong Kong SAR
+852 5803 3730 Hong Kong SAR
800 931 645 Hong Kong SAR Toll-free
800 906 780 Hong Kong SAR Toll-free
800 931 189 Hong Kong SAR Toll-free
+81 524 564 439 Japan
+81 3 4578 1488 Japan
+81 363 628 317 Japan
0 120 836 177 Japan Toll-free
00 663 381 4092 Japan Toll-free
0 800 100 5040 Japan Toll-free
0 120 829 768 Japan Toll-free
+853 6262 1604 Macau SAR
0 800 910 Macau SAR Toll-free
0 800 191 Macau SAR Toll-free
Meeting ID: 607 920 9799
Find your local number: https://sullcrom.zoom.us/u/acAE1NGVNS

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6079209799@zoomcrc.com

Join by H.323
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162.255.36.11 (US East)
221.122.88.195 (China)
115.114.131.7 (India Mumbai)
115.114.115.7 (India Hyderabad)
213.19.144.110 (Amsterdam Netherlands)
213.244.140.110 (Germany)
103.122.166.55 (Australia Sydney)
103.122.167.55 (Australia Melbourne)
209.9.211.110 (Hong Kong SAR)
149.137.40.110 (Singapore)
64.211.144.160 (Brazil)
69.174.57.160 (Canada Toronto)
65.39.152.160 (Canada Vancouver)
207.226.132.110 (Japan Tokyo)
149.137.24.110 (Japan Osaka)
Meeting ID: 607 920 9799

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**This is an external message from: pac@harkinscunningham.com **

Exhibit F

BEFORE THE
SURFACE TRANSPORTATION BOARD

DOCKET NO. FD 36500

CANADIAN PACIFIC RAILWAY LIMITED; CANADIAN PACIFIC RAILWAY COMPANY; SOO LINE RAILROAD COMPANY; CENTRAL MAINE & QUEBEC RAILWAY US INC.; DAKOTA, MINNESOTA & EASTERN RAILROAD CORPORATION;AND DELAWARE & HUDSON RAILWAY COMPANY, INC. – CONTROL – KANSAS CITY SOUTHERN, THE KANSAS CITY SOUTHERN RAILWAY COMPANY, GATEWAYEASTERN RAILWAY COMPANY, AND THE TEXAS MEXICAN RAILWAY COMPANY

CSX TRANSPORTATION, INC.'S COMMENTS AND REQUEST FOR CONDITIONS

Kent A. Gardiner
Ryan C. Tisch
Crowell & Moring LLP
1001 Pennsylvania Avenue, NW
Washington, DC 20004-2595
(202) 624-2674
rtisch@crowell.com

Paul A. Cunningham
Harkins Cunningham, LLP
1750 K Street, N.W., Suite 300
Washington, D.C. 20006
(202) 415-4026
pac@harkinscunningham.com

Steven C. Armbrust
CSX Transportation, Inc.
500 Water Street
Jacksonville, FL 32202
(904) 359-1229

Louis E. Gitomer
Law Offices of Louis E. Gitomer, LLC
600 Baltimore Avenue, Suite 301
Towson, MD 21204
(410) 296-2250
Lou@lgraillaw.com

Attorneys for CSX Transportation, Inc.

Dated: February 28, 2022

BEFORE THE
SURFACE TRANSPORTATION BOARD

STB Finance Docket No. 36500

CANADIAN PACIFIC RAILWAY LIMITED; CANADIAN PACIFIC RAILWAY COMPANY; SOO LINE RAILROAD COMPANY; CENTRAL MAINE & QUEBEC RAILWAY US INC.; DAKOTA, MINNESOTA & EASTERN RAILROAD CORPORATION; AND DELAWARE & HUDSON RAILWAY COMPANY, INC. – CONTROL – KANSAS CITY SOUTHERN; THE KANSAS CITY SOUTHERN RAILWAY COMPANY; GATEWAY EASTERN RAILWAY COMPANY; AND THE TEXAS MEXICAN RAILWAY COMPANY[1]

CSX TRANSPORTATION, INC.'S COMMENTS AND REQUEST FOR CONDITIONS

Under the schedule set forth by the Surface Transportation Board (the "Board") in Decision No. 11 in this proceeding ("Proceeding") served on November 23, 2021, CSX Transportation, Inc. ("CSXT"), submits these comments and requests for conditions on the proposed control of Kansas City Southern ("KCS") and its rail carrier subsidiaries, including, among others, the Kansas City Southern Railway Company ("KCSR") and Kansas City Southern Mexico ("KCSM") by Canadian Pacific Railway Limited ("CP"), a Canadian company (the "Proposed Transaction").[2]

CSXT objects to the Proposed Transaction to the extent it threatens to reduce competition over rail gateways connecting the eastern and western United States and thereby harm shippers by: (a) maintaining (and possibly expanding) the division of traffic over the Meridian Speedway,

[1] References to decisions in this Proceeding use this abbreviated form: Canadian Pacific Railway Limited, et al.-Control- Kansas City Southern, et al., Docket No. 36500, Decision No. , served .
[2] CP and KCS, and together with their United States subsidiaries, are referred to herein as the "Applicants." KCSM is not an Applicant.

(b) reducing the ability of CSXT and KCSR to interchange traffic in New Orleans on commercially reasonable terms, and (c) reducing competition between the eastern and western U. S. by downgrading and reducing traffic volume over the KCSR line between Kansas City and East St. Louis.

CSXT seeks conditions to mitigate those threats. CSXT also seeks a remedy to mitigate CPKC's increased incentive to raise rates on its traffic in Mexico, lower its rates in the United States and thereby divert traffic from other US carriers at cross-border U.S-Mexico gateways. These problems, while significant, are not insurmountable. They can be cured by the conditions proposed by CSXT, which meet the criteria of 49 CFR 1180.1(d) (2000), the regulations that the Board elected to apply to this Proceeding.[3]

A. COMMENTS

If approved, the Proposed Transaction would be the first Major Transaction and largest change of control in the North American railroad network since 1999. In this Proceeding, the Board must base its evaluation of the Proposed Transaction on certain factors identified by Congress[4] to determine whether the Proposed Transaction is consistent with the public interest.[5]

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[3] FD 35400 Decision No. 4

[4] "In a proceeding under this section which involves the merger or control of at least two Class I railroads, as defined by the Board, the Board shall consider at least—
(1) the effect of the proposed transaction on the adequacy of transportation to the public;
(2) the effect on the public interest of including, or failing to include, other rail carriers in the area involved in the proposed transaction;
(3) the total fixed charges that result from the proposed transaction;
(4) the interest of rail carrier employees affected by the proposed transaction; and
(5) whether the proposed transaction would have an adverse effect on competition among rail carriers in the affected region or in the national rail system." 49 USC 11324 (b).
All but the second factor need to be considered in this Proceeding.

[5] "The Board shall approve and authorize a transaction under this section when it finds the transaction is consistent with the public interest." 49 USC 11324 (c).

The Board must further assess such a transaction through the lens of its "general policy statement for merger or control of at least two Class I railroads."[6]

On November 23, 2021, the Board accepted the Application filed October 29, 2021, for review.[7] The Board states that Applicants present a *prima facie* case by disclosing facts that, if construed in their most favorable light, support a finding that the Proposed Transaction is consistent with the public interest.[8] Applicants claim that, because the Proposed Transaction is end-to-end, it promises more efficient transportation over Applicants' routes, and presents no threat either to competition or to the efficient provision of railroad services. Applicants contend that the public benefits of the Proposed Transaction stem primarily from certain operational and service improvements, the value of which in a normal year after closing would be $194.6 million[9] and the private benefits resulting from the diversion of traffic from other railroads in a normal year would be $805.8 million.[10] Applicants assert, without specific support, that these diversions, despite traveling over longer and otherwise disadvantaged routes, are achievable because of the removal of only one interchange between CP and KCS,[11] plus limited price reductions, and unquantified operating improvements based on generalities and no supporting analyses.

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[6] As noted above, in FD 36500, Decision No. 4 the Board found the Proposed Transaction to be subject to the regulations set forth at 49 C.F.R. subpart A, in effect before July 11, 2001. However, the general policy statement in 49 CFR 1180.1 should not be ignored as the competitive implications of the Proposed Transaction remain far reaching.
[7] *Canadian Pacific Railway Limited, et al.-Control- Kansas City Southern, et al.*, Docket No. 36500, Decision No. 11, served November 23, 2021
[8] Id at. 10.
[9] Volume 1, page 74.
[10] Id.
[11] Id. at 96.

CSXT requests that, if the Board approves the Proposed Transaction, approval be conditioned to assure the Proposed Transaction lives up to Applicants' claims and does not hinder competition or the efficiency of the North American railroad network. These conditions are required because Applicants' support for their *prima facie* case is inadequate.[12] As explained in the Verified Statement of Professor Julie Carey and Dr. Al Bremser ("Carey V.S.", Exhibit A hereto), that lack of support poses threats to competition and efficiency that the Board should remediate (*See* Carey V.S. at 2-5).

Generally, Applicants' equivocal commitment to maintaining open gateways is inadequate to protect against CPKC's incentives and capability to close commercially both cross-border and domestic U.S. gateways.

The most important domestic gateway issues ignored by Applicants are the ongoing agreements between KCS and Norfolk Southern Railway Company ("NSR") that restrain competition over the Meridian Speedway for certain traffic to and from the eastern United States. The Meridian Speedway is the subject of an explicit market allocation scheme which divides the control of certain geographic areas and products between KCSR and NSR and reduces effective competition with NSR for traffic to and from points in the East best served over the Meridian Gateway.

The Application demonstrates that Applicants intend not to extend their gateway commitment to the Meridian Gateway, but instead to enshrine the existing market allocation arrangements, which never received competition review. The Applicants fail to address the

---

[12] The very purpose of the case-in-chief concept is to permit the Board and all interested parties "to have, upon the filing of an application, *all of the applicants' supporting evidence*." *Railroad Consolidation Procedures*, 363 I.C.C. 767, 770 (1980) (emphasis supplied).

competitive impacts of continuing this patent market division.

And, in this Proceeding, NSR is asking to expand this exclusive arrangement both in terms of type of traffic and geography covered by the arrangements.

CSXT's requested conditions address some of the Application's inadequacies that reveal threats to competition and the efficiency of the North American Railroad Network.[13] These conditions are related to the Proposed Transaction and designed to ensure shippers are not

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[13] (1) As explained further in the Carey V.S., Applicants' failures to support their *prima facie* case include Applicant'sincludeApplicant's economic witness who provides an inadequate competition analysis, particularly regarding potential harm relating to traffic to and from points in Mexico under KCSM's substantial control, (Carey V.S. at 6), and thus elides the Proposed Transaction's potential threat to competition and efficient routing of traffic to and from Mexico through Laredo. (2) Prof. Carey's market share analysis shows the Board should be concerned that the combination of the existing KCSM/KCS network with CP network, and Applicants' combined ability to influence prices and competition on traffic movements involving Mexico, provide the Applicants increased incentive and ability to reduce competition and harm shippers. (Carey V.S. at 4). (3) Most of Applicants' asserted transaction-related public benefits are not public benefits, but private benefits that will accrue solely to CPKC. (Carey V.S. at 4 and 31) and are not the product of efficiency gains that create lower costs and service improvements *See* FD No. 32760, Decision No. 44, August 6, 1996, at 363. (4) The few public benefits raise doubt about Applicant's claims the Transaction has the potential to increase competition. (Carey V.S. at 11-12). (5) Applicants' probable benefits are from traffic diversions to routes where CPKC has longer and disadvantaged routes, or to routes where the diversions could be realized without the Proposed Transaction, raising doubt about the potential for increased competition. (Carey V.S. at 4, 8, 11). (6) Applicants' supported public benefits are much lower than the total claimed (Carey V.S. at Figure 5) and much smaller as a proportion of transaction costs than demonstrated in prior large transactions. (Carey V.S. at Figure 9). (7) Applicants have not shown that the large incremental debt to finance the Proposed Transaction can be supported by the plausible potential additional revenues or costs savings from the Proposed Transaction. Absent that showing, the Application suggests a) the Proposed Application does not adequately support the stated rationale and financial case for the Transaction; b) the Transaction will lead to a greater burden on the Applicants' existing shippers ; and c) Applicants will have a greater incentive to seek revenues only via practices harming competition. (Carey V.S. at 43). (8) Applicants' proposed "open gateway" commitments are not sufficiently definitive, nor do they address many of Applicant's key gateways. (Carey V.S. at 24). (9) The Meridian Speedway is the subject of an explicit market allocation scheme which reduces effective competition with NS for traffic to and from points East best served over the Meridian Gateway.

burdened by excess costs or reduced competition. They would not impose unreasonable operating conditions or other restraints on CPKC and would not frustrate the ability of CPKC to provide its plausibly anticipated public benefits. *See* 49 CFR 1180.1(d)(1) (i-iv) (2000).

First, CSXT requests conditions that will assure that the Board does not, by approving the Application, enshrine the existing but never sanctioned restrictions on competition for the movement of traffic over the line between Meridian MS, and Shreveport, LA, owned by a joint venture controlled by KCS and the Alabama Great Southern Railroad Company ("AGS"), a subsidiary of NSR.[14]

Second, CSXT requests that the Board deny any NSR Responsive Application seeking to expand its rights under the Meridian Speedway Agreements.[15]

Third, CSXT requests the Board impose conditions to assure the continued competitiveness of the New Orleans Gateway.

Fourth, CSXT requests the Board impose conditions to obviate any risk the Proposed Transaction might harm efficient competition for East-West traffic through the gateway at East St. Louis, IL.

Fifth, CSXT requests the Board impose conditions to protect competition for traffic to and from Mexico from anticompetitive activity and preclude inefficient traffic diversions.

CSXT's requested conditions would reduce the potential for harm to shippers stemming from issues Applicants have either ignored or have addressed inadequately to support their *prima facie* case that the Proposed Transaction is consistent with the public interest, under the

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[14] Docket FD 34822, Exhibit A to the "Transaction Agreement" (Filed January 17, 2006).
[15] All agreements included as attachments to the *Verified Notice of Exemption* in FD 34822 filed January 17, 2006, are herein referred to as the "Meridian Speedway Agreements."

prevailing statutory and regulatory standards contained in 49 U.S.C. 11324(b) and 49 CFR 1180.1 (2020). *See also* Railroad Consolidation Procedures, 363 I.C.C. 767, 770 (1980).[16]

B. REQUESTS FOR CONDITIONS AND RELATED ORDERS

1. Conditions to remedy the Arrangements Among KCSR, MSLLC, and NSR that foreclose effective competition over the Meridian Speedway, and the requests for trackage rights sought by NSR in its expected Responsive Application.

KCSR and NSR cooperate to transport traffic over the line between Meridian, MS, and Dallas, TX, known as the Meridian Speedway (the "Speedway"). KCSR has granted NSR exclusive rights to handle certain traffic on the Speedway. [17, 18] These exclusivity provisions constitute pre-existing and prospective market division arrangements between NSR and KCSR that could receive continued and prospective antitrust immunity if the Proposed Transaction were approved by the Board without conditions

---

[16] "Under our new regulations, we shall instead issue, in appropriate circumstances and on our own motion, a show-cause order directed to the applicants and any other proponents of the transaction. If those parties cannot show cause why the application should not be summarily denied for failure to state a prima facie case (on either of the two bases discussed above), we would be remiss in allowing the proceeding to continue. Accordingly, we would deny the application."
The "two bases" are: "Applicants can fail to meet their burden of proof either by (1) disclosing facts that, even if construed in their most favorable light, are insufficient to support a finding that the proposal is consistent with the public interest, or by (2) disclosing facts that affirmatively demonstrate that the proposal is not in the public interest." Id. at 769.

[17] *See* "NSR shall have the exclusive right to transport NS Traffic over the Subject Trackage." Exhibit C to *Transaction Agreement*: NSR-MSLLC Joint Use Agreement, pg. 11. *See also* "For NS Traffic only, MSLLC may not perform haulage services for any carrier other than NSR or grant trackage rights or operating rights to KCSR or any Foreign Railroad on the Subject Trackage for NS Traffic [except NSR], absent the express written consent of NSR." Exhibit C to *Transaction Agreement*: NSR-MSLLC Joint Use Agreement, pg. 8.

[18] NSR may seek to expand that exclusivity to cover a broader geographic territory and lines of business as part of the Proposed Transaction. *See* FD 36500, Description of Anticipated Responsive Application by Norfolk Southern Railway Company (filed January 12, 2022, 5).

CSXT requests that any approval of the Proposed Transaction requires KCS and KCSR to nullify these exclusivity provisions and free KCSR to operate again over the MSLLC line as it could before any restrictive agreements with NSR, able to interchange overhead intermodal traffic moving over the Speedway between points west of Dallas and points east of Meridian, and, as KCSR deems commercially desirable, afford haulage or trackage rights to carriers other than NSR. CSXT also requests that any approval order impose the conditions described below to assure effective competition over the Speedway for all traffic that would benefit from this route.[19]

a. The Meridian Speedway Agreements

The Meridian Speedway runs between Meridian, MS, and Dallas, TX, through KCS' "hub" at Shreveport, LA. Before 2006, KCSR was the sole owner and operator of the rail line between Meridian, MS, and Dallas, TX.[20] In 2005, KCS, KCSR, NSR, and AGS entered an agreement to create a joint venture, Meridian Speedway LLC ("MSLLC"), to control the portion of the Speedway between Meridian, MS and Shreveport, LA.[21] KCS owns 70% of MSLLC and NSR owns 30%. MSLLS Agreements specify that only NSR use the Speedway to transport "NS

---

[19] The Board should also deny any expansion of the NSR's exclusive rights to additional traffic and a broader geographic territory described in NSR's January 12, 2022, that may be proposed by NSR pursuant to its Description of Anticipated Responsive Application (the "NSR's Speedway Proposal"). FD 36500, Description of Anticipated Responsive Application by Norfolk Southern Railway Company (filed January 12, 2022) at 5. Alternatively, should the Board approve NSR's proposal to increase its exclusive Speedway arrangements with KCSR, CSXT requests conditions to remove any risk those arrangements would preclude competition for any traffic over the Speedway by granting CSXT similar relief.

[20] Except for the portion of the line between milepost 95.26± and milepost 95.7± at Jackson, MS owned by the Illinois Central Railroad Company, a subsidiary of the Canadian National Railway Company.

[21] *See* definition of the Meridian/Shreveport line in the *Transaction Agreement*, (December 1, 2005), 1.

Traffic," defined as *all overhead intermodal traffic on the Speedway not originating or terminating on KCSR* ("NSR Exclusivity Traffic").[22] The same agreements establish that serving such traffic other than through NSR's exclusive rights was a "Major Decision" requiring NSR's consent.[23] These provisions have no termination date.

The agreements therefore grant NSR exclusivity, in perpetuity, for the transport over the Speedway of all non-KCS-location intermodal overhead traffic moving east of Meridian and west of Dallas, even though KCSR owns much of the Speedway, has a majority interest in the MSLLC joint venture, operates the portion of the Speedway owned by MSLLC, handled that traffic before entering limiting agreements with NSR, and continues to be capable of handling such traffic today. The Notice of Exemption regarding the Meridian Speedway Agreements suggest that this exclusivity is justified because NSR was willing to provide $300 million of capital investment in the Speedway, but "it did not want to do so unless it could be assured that other carriers would not use the capacity NS's investment would help to create."[24]

b. Lack of Review of the Meridian Speedway Agreements

On January 17, 2006, three Notices of Exemption were filed with the Board -- concurrently but not consolidated for handling.

First, KCS, KCSR, and MSLLC filed a Notice of Exemption for three transactions within

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[22] FD 34822, Kansas City Southern, the Kansas City Southern Railway Company, and Meridian Speedway, LLC –Exemption for Transactions Within a Corporate Family filed January 17, 2006, Exhibit D, 4.

[23] FD 34822, Kansas City Southern, the Kansas City Southern Railway Company, and Meridian Speedway, LLC –Exemption for Transactions Within a Corporate Family filed January 17, 2006, Exhibit A, 9-11 (defining "Major Decision"), 13 (defining "NS Traffic"), 29 (requiring NS consent for Major Decisions). *See also id.*, Exhibit B, 6; *id.* Exhibit C, 5-14; *id.* Exhibit D, 4-8.

[24] *Verified Notice of Exemption* in FD 34822 filed January 17, 2006, at 5.

a corporate family[25]: (i) KCS transferred the line between Meridian, MS and Shreveport, LA to MSLLC, (ii) KCS continued in control of MSLLC upon MSLLC becoming a rail carrier, and (iii) MSLLC granted KCSR operating rights over MSLLC to operate as MSLLC's contract operator to fulfill MSLLC's contractual and common carrier obligations. Neither KCS nor KCSR, the parties that filed the Notice of Exemption, sought review or STB sanction of the competitive impacts of the exempted transactions, and the Board neither conducted such a review nor sanctioned those impacts.

Second, NSR filed a notice of exemption for springing trackage rights over the MSLLC between Meridian, MS, milepost 0.0± and 95.26±, and between Jackson, MS, milepost 95.7±, and Shreveport, LA, milepost V-169.85±. NSR could exercise those rights only after a major service standard failure or a permitted asset transfer.[26] Absent those occurrences, KCSR, as the operator of MSLLC, would provide haulage for NSR over the MSLLC as provided in the Meridian Speedway Agreements.[27]

Third, KCSR filed a notice of exemption for trackage rights to operate in local and overhead service on the MCLLC.[28]

NSR owns 30% of MSLLC. KCS owns 70% of MSLLC and uses its trackage rights over

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[25] FD 34822, Kansas City Southern, the Kansas City Southern Railway Company, and Meridian Speedway, LLC- Exemption for Transactions within a Corporate Family, filed January 17, 2006.
[26] Exhibit C to *Transaction Agreement*: NSR-MSLLC Joint Use Agreement, (December 1, 2005), 6.
[27] FD 34821, Norfolk Southern Railway Company-Trackage Rights Exemption-Between Meridian, MS and Shreveport, LA filed January 17, 2006. [Break down haulage further]
[28] FD 34823, The Kansas City Southern Railway Company-Trackage Rights Exemption-Meridian Speedway, LLC, filed January 17, 2006.

MSLLC to carry traffic for its own account and, on behalf of MSLLC,[29] and to provide haulage for NSR. NSR is the sole service provider of transcontinental intermodal traffic over the Speedway.[30]

In this Proceeding, the 2006 arrangements governing the Speedway were mentioned only cursorily by witnesses for the Applicants, two of which claimed no direct knowledge of the Meridian Speedway Agreements and none of whom mentioned the market division between KCSR and NSR. If the Board approves the Proposed Transaction without the conditions sought by CSXT, those exclusivity agreements would continue in place and there is a risk they would be exempted from the antitrust laws.[31]

The Board therefore has not analyzed the competitive effects of NSR's perpetual exclusivity, nor approved it. NSR's rights to exclusively move NS Traffic over the Speedway

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[29] "As the contract operator for MSLLC, KCSR will perform the haulage services contemplated by MSLLC's agreement with NSR, while simultaneously operating over the Line for its own account pursuant to local and overhead trackage rights granted by MSLLC to KCSR." FD 34822, Verified Notice of Exemption (January 17, 2006), 6. *See also*, "MSLLC shall deliver eastbound NSR Haulage Cars to NSR at Meridian and… westbound NSR Haulage Cars to KCSR and UP… at Shreveport." Exhibit C to *Transaction Agreement:* NSR-MSLLC Joint Use Agreement, 10. *See also* "MSLLC will hire KCSR to perform as the designated operator ("Designated Operator") for all railroad operations on behalf of MSLLC, including MSLLC railway operations required pursuant to the KCSR Joint Use Agreement and the NSR Joint Use Agreement." ibid., 1. *See also* "Nothing herein shall be interpreted as prohibiting the Designated Operator from transporting NSR Haulage Cars in a continuous movement operating over both the haulage routes covered by: (i) this Agreement and (ii) the Western Haulage Agreement." ibid., 10. *See Also*, "NSR's operations over the Subject Trackage shall at all times be subject to the direction and control of the Designated Operator." ibid., 8.

[30] "NSR will be the sole provider, via haulage and trackage rights over the Line, of service for transcontinental intermodal container traffic moving on the Line that does not originate or terminate on KCS's current system and that both (a) originates or terminates in the United States at or east of Meridian and enters or exits the Line at Meridian, and (b) originates or terminates in the United States west of Fort Worth, Texas, and enters or exits the Line at Shreveport." *See* FD 34822, Verified Notice of Exemption (January 17, 2006), 6.

[31] *See* 49 USC 11321(a).

were noticed under the "transaction within a corporate family" procedure, which exempts that transaction from regulation. However, this exemption applies only where the transaction meets the specific criteria such that, *inter alia*, it does not result in "a change in the competitive balance with carriers outside the corporate family."[32] Such an exemption does not excuse any adverse competitive impacts of the MSLLC arrangements, and it does not prevent the Board from correcting that situation. "If the notice of exemption contains false or misleading information which is brought to the Board's attention, the Board shall summarily revoke the exemption for the carrier and require divestiture." 49 CFR 1180.4(g)(1)(iv). As described below and by Prof. Carey (*see* Carey V.S. 44-52), the restrictions on the type of traffic that KCS can handle over the Speedway and on its ability to interchange with other carriers for service upstream and downstream do have anticompetitive effects in the form of horizontal market division exacerbated by vertical integration. These anticompetitive effects were not revealed or even discussed in any of the notices of exemption, a clear violation of the requirement that Board prior review "is unnecessary to protect shippers from market abuse." 49 CFR 1180.2(d). The Board has the authority to review and change the Meridian Speedway Agreements that are not consonant with ICCTA and revoke the exemption to the extent the Applicants or NSR contend that the exemption exempts the Meridian Speedway Agreements from competition review under ICCTA.[33]

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[32] "Transactions within a corporate family that do not result in adverse changes in service levels, significant operational changes, or *a change in the competitive balance with carriers outside* [emphasis added] the corporate family." 49 CFR 1180.2(d)(3).

[33] 49 USC 10505d; *see also* 49 USC 10502d: "The Board may revoke an exemption, to the extent it specifies, when it finds that application in whole or in part of a provision of this part to

Relatedly, Applicants or NSR may argue that even to the extent the NSR exclusivity resulted in anticompetitive economic effects as discussed below, those effects are not specific to the Proposed Transaction. However, any such anticompetitive effects would cast into doubt the validity of the use of the intracorporate transaction procedure to exempt review of the Meridian Speedway Agreements, as this procedure is not available for transactions resulting in a "change in the competitive balance with carriers outside the corporate family."[34] To the extent Applicants or NSR argue instead that the 2006 request for exemption did not, in fact, include a request to exempt the NSR exclusivity agreement, then those arrangements can clearly be abrogated and, in either case, would be subject to antitrust review. And any NSR request for *expansion* of NSR's exclusive rights to cover new markets as part of the Proposed Transaction would indisputably be transaction-specific.

c. Anticompetitive Concerns Regarding the Meridian Speedway Agreements

The Meridian Speedway Agreements {and other exhibits submitted with the MSLLC Notice of Exemption} [35] {and subsequent amendments to those agreements} had two principal

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the person, class, or transportation is necessary to carry out the transportation policy of section 10101 of this title. The Board shall, within 90 days after receipt of a request for revocation under this subsection, determine whether to begin an appropriate proceeding."

[34] *Compare* STB Finance Docket No. 34822, *Verified Notice of Exemption Pursuant to 49 C.F.R. § 1180.2(d)(3)* at 6-7 (January 17, 2006) ("Pursuant to 49 C.F.R. §1180.d(d)(3), KCS, KCSR, and MSLLC invoke the Board's class exemption … for transactions within a corporate family."), *with* 49 C.F.R. § 1180.2(d)(3) (2000) ("Transactions within a corporate family that do not result in adverse changes in service levels, significant operational changes, *or a change in the competitive balance with carriers outside the corporate family*." (Emphasis supplied)).

[35] FD 34822, Kansas City Southern, the Kansas City Southern Railway Company, and Meridian Speedway, LLC –Exemption for Transactions Within a Corporate Family filed January 17, 2006.

competitive effects, neither of which has previously been subject to review by the Board or Antitrust Agencies.[36]

The first effect was to horizontally divide the markets that NSR and KCSR could serve over the Speedway. Prior to any restrictive agreement with NSR, KCSR was free to offer interline service in conjunction with other carriers for intermodal traffic to and from points east of the Speedway in competition with NSR. In exchange for capital investment on the Speedway, KCSR agreed not to compete with NSR, and instead exclusively to provide haulage, through MSLLC, for NSR's service of NSR Exclusivity Traffic.

Had it occurred in any other industry, the Antitrust Agencies would have scrutinized this perpetual restriction on competition in exchange for a defined investment. In view of the restrictions on KCS's ability to provide competing service,[37] the unique nature of the Speedway assets controlled by the joint venture,[38] both parties' veto rights over major competitive

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[36] The U.S. Department of Justice and the Federal Trade Commission

[37] *See*, *e.g.*, U.S. Dep't of Justice & Fed. Trade Comm'n, Antitrust Guidelines for Collaborations Among Competitors 19 ("The Agencies consider whether, to what extent, and in what manner the relevant agreement permits participants to continue to compete against each other and their collaboration, either through separate, independent business operations or through membership in other collaborations …. In general, competitive concern likely is reduced to the extent that participants actually have continued to compete, either through separate, independent business operations or through membership in other collaborations, or are permitted to do so.")

[38] *See*, *e.g.*, *id.* at 19-20 ("If such resources must be contributed to the collaboration and are specialized in that they cannot readily be replaced, the participants may have lost all or some of their ability to compete against each other and their collaboration, even if they retain the contractual right to do so. In general, the greater the contribution of specialized assets to the collaboration that is required, the less the participants may be relied upon to provide independent competition." (footnote omitted)).

decisions,[39] and the indefinite duration of the exclusivity and collaboration,[40] the agencies would likely conclude that the agreements resulted in a perpetual, significant restriction on competition between KCSR and NSR. The agencies would therefore consider primarily whether this restriction is justified by NSR's $300 million investment into the Speedway.[41]

To be cognizable, efficiencies resulting from a transaction must be verifiable, not anticompetitive, and not achievable through less restrictive means.[42] While NSR is likely to argue that its investment in the Speedway generated real efficiencies, and that the investment would not have taken place without some agreement granting NSR exclusive rights to carry some kinds of traffic across the Speedway, it would also have to acknowledge the arrangement's potentially anticompetitive effects – principally, the closing of the Speedway to traffic destined for other Eastern carriers (discussed more fully below). Antitrust Agencies reviewing this type of collaboration would conduct an extensive analysis to "consider whether cognizable efficiencies likely would be sufficient to offset the potential of the agreement to harm consumers in the relevant market."[43]

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[39] *See, e.g., id.* at 20-21 ("[T]he Agencies consider the extent to which the collaboration's governance structure enables the collaboration to act as an independent decision maker. For example, the Agencies ask whether participants are allowed to appoint members of a board of directors for the collaboration, if incorporated, or otherwise to exercise significant control over the operations of the collaboration.").
[40] *See, e.g., id.* at 21 ("The Agencies consider the duration of the collaboration in assessing whether participants retain the ability and incentive to compete against each other. In general, the shorter the duration, the more likely participants are to compete against each other and their collaboration.").
[41] *See generally id.* at 23-25.
[42] *E.g., id.* at 23.
[43] *Id.* at 25.

The Agreements' horizontal restriction unto itself may or may not have passed review for anticompetitive impacts if it had been reviewed. However, whether the horizontal effects of the KCS-NSR market division (which, among other things, ceded a competitive advantage that KCS had for some traffic that NSR might otherwise carry or receive over other gateways) would have passed review by the Board as a pooling[44] or division of traffic arrangement, or a change of control, or review under the antitrust laws is less significant here than the fact the arrangements creating NSR's exclusivity of asset control and market division scheme has never been subjected to a competition review. And, absent evidence not in the record of the Board's 2006 intracorporate transaction exemption proceeding or the record in this Proceeding, it is unclear what conclusion such a review would have reached. In this case, the perpetual nature of NSR's exclusivity (or market division) enhances the magnitude of potential anticompetitive effects. A reviewing regulator would likely have demanded substantial evidence of the pro-competitive attributes of the collaboration to determine if they outweighed such anticompetitive effects, had such evidence been presented.

The second and interrelated competitive effect of the NSR-KCS agreements stems from the vertical integration of the Meridian Speedway into NSR's extensive rail network. The arrangement granted NSR exclusive control of upstream (or downstream) service over the Meridian Speedway for NSR Exclusivity Traffic. Prior to the Meridian Speedway Agreements, carriers competing against NSR to serve traffic between Meridian and points east could have

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[44] "A rail carrier providing transportation subject to the jurisdiction of the Board under this part may not agree or combine with another of those rail carriers **to pool or divide traffic** or services or any part of their earnings without the approval of the Board under this section or section 11123 of this title." 49 U.S.C. 11322(a). Moreover, "The Board may impose conditions **governing the pooling or division…**" 49 U.S.C. 11322(B).

received or delivered traffic in interchange with KCS or through haulage or trackage agreements The MSLLC Agreements forbade this form of competition: No carrier other than NSR may, in conjunction with KCS, compete with NSR for movements of intermodal traffic that include overhead movements over the Speedway other than to and from KCSR locations.

NSR's acquisition of exclusive control of overhead intermodal traffic on the Meridian Speedway appears to have resulted in significant foreclosure of competition for service to and from the east end of the Speedway. As Prof. Carey shows, NSR has achieved a nearly {{ }} market share for overhead intermodal traffic moving over the Meridian Speedway gateway to serve specific lanes connecting west coast and east coast markets not directly served by a single railroad (Carey V.S. at 50, Figures 13 and 14). This result is strongly indicative of anticompetitive effects, and that NSR's exclusive control of the Meridian Speedway has resulted in market power for this traffic.

That such foreclosure resulted from Meridian Speedway exclusivity would be unsurprising. The Antitrust Agencies consider whether such vertical integration would cause input foreclosure by assessing the integrated firm's ability and incentive to "profitably use its supply of an input (the related product) to weaken the competitive constraint it faces from rivals in the downstream market (the relevant market)."[45] The chief mechanisms by which vertically integrating firms may do so is to "raise rivals' costs by increasing the price or lowering the quality of the [upstream] product" or to "refuse to supply rivals with the [upstream] products altogether."[46]

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[45] U.S. Dep't of Justice & Fed. Trade Comm'n, Vertical Merger Guidelines 4 n.4 (2020).
[46] *Id.* at 4

Antitrust Agencies consider vertically-integrating parties' ability to foreclose downstream competition by determining whether the merged firm could likely cause rivals to lose significant sales in the downstream market or otherwise compete less aggressively for customers' business.[47] The Guidelines explain this element is not satisfied if rivals can readily switch purchases to alternatives, including self-supply, without a meaningful effect on the price, quality, or availability of products or services in the downstream market.[48] As explained by Prof. Carey, (Carey V.S. at 49) the Meridian Speedway has a direct route and shorter mileage for certain NSR Exclusivity Traffic moving between the southwest and southeastern U.S.,[49] whereas interchanges over routes other than the Meridian Speedway may require longer routes or travel over operationally disadvantaged gateways such as New Orleans[50] and Memphis.[51] Alternative gateways likely are not similarly-efficient routes for some NSR Exclusivity Traffic and they therefore could not constrain NSR's apparent market power for this service.

The Antitrust Agencies consider the integrating parties' incentive to foreclose rivals based on whether the party benefits significantly in the downstream market when rivals lose sales or alter their behavior in response to the foreclosure.[52] Regarding NSR's exclusive control

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[47] *See*, *e.g.*, Vertical Merger Guidelines 4.
[48] *Id.*
[49] For NS Exclusive rights on Meridian Speedway see "Norfolk Southern Railway Company-Meridian Speedway-Joint Use Agreement", May 2006,8.1.11-KCSR-HC-00013373 to KCSR-HC-00013408, at KCSR-HC-00013377-82
[50] *See* DiDeo V.S.
[51] Industry trade press has discussed congestion at Memphis. *See* Memphis shippers ask STB to intervene on intermodal congestion, Journal of Commerce online, April 21, 2021. Available at https://www.joc.com/rail-intermodal/intermodal-shipping/memphis-shippers-ask-stb-intervene-intermodal-congestion_20210420.html ; What's Really Going On in Memphis? Railway Age, June 9, 2021. Available at https://www.railwayage.com/news/whats-really-going-on-in-memphis/
[52] *See*, *e.g.*, Vertical Merger Guidelines 5.

of NSR Exclusivity Traffic movements over the Meridian Speedway, NSR's actual market conduct demonstrates its incentives were precisely to foreclose competition. KCSR and MSLLC were prohibited from interchanging NSR Exclusivity Traffic with any carrier other than NSR and, today, no such interchanges occur at Meridian.

d. Proposed Expansion of NSR's Exclusivity

NSR's Description of Responsive Application proposes to expand NSR Traffic to include all intermodal, "premium boxcar," and automotive traffic that originates or terminates west of Shreveport, and east of Meridian, including some (so far only vaguely defined) Mexico traffic.[53] Thus, NSR's exclusive rights would extend to new locations and new shippers and to entirely new lines of business.

NSR's request to expand the scope of its Meridian Speedway rights to include new geographic areas and lines of business would expand the same integration that occurred in 2006, resulting in apparent foreclosure, regarding those locations and lines of business. Because there are no alternative, similarly-efficient gateways available for the new locations and lines of business that are not available for existing NSR Exclusivity Traffic, the foregoing context raises real concern that an expansion of NSR's exclusivity would result in additional, prospective foreclosure. More detailed analysis of the likelihood of such foreclosure will be appropriate based upon the details of NSR's Responsive Application.

e. Conditions Requested

If the Board approves the Proposed Transaction, CSXT requests that the Board condition

[53] Description of Anticipated Responsive Application by Norfolk Southern Railway Company, filed January 12, 2022 (NS-6) at 5-6.

its approval on orders that:

1. Abrogate any Meridian Speedway Agreements precluding competition between NSR and CPKC (or any other carrier) from competing through arrangements with CPKC or MSLLC for the movement of what has been defined as NS Exclusivity Traffic to, from, or over MSLLC.

This condition will re-establish the competitive *status quo* before 2006 by removing the limitations on the traffic KCSR can handle alone, or with other carriers – by interchange, haulage, or trackage rights over the Speedway.

2. Deny any NSR Responsive Application or requested condition that would permit NSR to expand its exclusive rights over the Speedway.

This condition will assure that NSR cannot extend its exclusive rights over the Speedway to new geographic areas or new types of traffic. While NSR may be entitled under the MSLLC Agreements and related agreements to additional operating rights over the Speedway (which is a matter for the courts to decide under those agreements), no continuance or expansion should be permitted of the adverse vertical effects on competition posed by NSR's exclusive rights to move large volumes of traffic over the Speedway to and from the East.

3. Require Applicants and MSLLC to establish an efficient interchange between CPKC and CSXT at Meridian, MS and to keep that initial gateway open on commercially reasonable terms.

CSXT can currently receive and deliver traffic interchanged with KCS at Meridian with a G&W subsidiary – MNBR – or directly through haulage over MNBR.

While KCS has other carriers with which it can interchange traffic to and from the East over the Speedway, CSXT is the only Class I carrier that can offer competition with NSR throughout the East for traffic that can move efficiently over the Speedway. CPKC should have to maintain an efficient interchange with CSXT at Meridian.

Such an interchange condition together with a requirement to keep that gateway open will assure competition over the Speedway to and from points in the East and prevent CPKC from diverting traffic that can most efficiently move over the Speedway to other, less efficient routes., (see Carey V.S. at 54 regarding CPKC's incentives to divert traffic inefficiency).

2. Assuring efficient East-West interchange at New Orleans, LA ("NOLA").

NOLA is a principal East-West gateway, especially for traffic between the Southeast U.S. and the Southwest U.S. and Mexico.

Since 2006, as explained by Mr. DiDeo in his Verified Statement regarding New Orleans ("DiDeo NOLA V.S." at 2, Exhibit B hereto) the CSXT interchange with KCSR at NOLA has been constrained by KCSR's abandonment of certain trackage which resulted in a less efficient interchange with CSXT. Since that abandonment, KCSR, in recognition of the added cost imposed on the CSXT- KCSR interchange, absorbed until 2020 the cost of an alternative interchange route over New Orleans Public Belt {"NOPB"}. Since 2020 KCSR has absorbed most of the NOPB charges. However, KCSR has an option to terminate the Interchange Agreement on 30 days' notice, effectively increasing CSXT's cost on interchange traffic by a factor of ten, leading to potential disruption for shippers that would contravene the conditions predicate to KCSR's eligibility for an exemption under the applicable regulations.[54] That would have the effect of providing CPKC additional leverage to divert the interchange to a location more favorable to CPKC.

CPKC's ability to increase CSXT's costs and plans to divert traffic to less efficient routes

[54] 49 CFR 1180.2(d)(5).

(*see* Carey V.S. at 7) means that CSXT can no longer rely on KCSR's economic interest in the NOLA interchange as an incentive to continue to bear the additional cost imposed on the CSXT-KCSR interchange by KCSR's abandonment or to abide by the routing agreed to with CSXT to reduce the impact of KCSR's refusal to bear the cost of NOPB's services.

CSXT requests a condition requiring CPKC to continue to absorb those costs as provided in the agreement attached to the DiDeo NOLA V.S. and to continue interchange with CSXT, by modifying the agreement to be terminable only on mutual consent by the parties.

3. Assuring effective competition is preserved over the KCS route between Kansas City, MO and the KCS-CSX interchange at E. St. Louis, MO. for traffic moving to, from, or through Kansas City to and from points in the Eastern U.S. served by CSXT through E. St. Louis.

Applicants propose to downgrade their use of their line between Springfield, IL, and Kansas City, MO. In response, Canadian National Railway ("CN") has noticed its intent to file a responsive application seeking divesture of that line.[55]

CSXT can now interchange traffic to and from Kansas City via interchange with KCSR at East Saint Louis, IL ("ESL"), mostly over the via the Springfield line. This route competes with the NSR route between Kansas City and ESL. The KCSR-ESL Line between Kansas City and its interchange with CSXT in East St. Louis is a significant competitive route for traffic moving between the east and Kansas City. Today competition exists between the single-line route between Kansas City and points in the east over the NSR and the joint-line CSXT-KCSR route over East St. Louis. The downgrading of the KCSR-ESL Line and diversion of traffic to Chicago, as proposed by Applicants, threatens to reduce the level of competition NSR faces for

[55] CN's Description of Anticipated Responsive Application, FD 36500 (CN-10) served January 12, 2022.

traffic to and from Kansas City. As explained in the DiDeo Verified Statement regarding East St. Louis ("DiDeo ESL V.S." at 1, Exhibit C hereto), the downgrading and diversion will cause slower trains and lower volumes that will degrade service and reduce competition with NSR.

CSXT takes no position regarding a divesture of the Springfield-Kansas City line. CSXT expects, however, that the portion of that line between ESL and Kansas City will no longer be preferred – by either CPKC or CN – for traffic now moving via Kansas City between shippers on KCSR and CP and shippers on CSXT east of ESL (DiDeo ESL V.S. at 1). Neither CPKC nor CN has a direct route that competes with NSR (which has a route between ESL and Kansas City) directly east of ESL.

To offset this expected downgrade of the KCS route between ESL and Kansas City and to avoid any reduction in competition, CSXT requests that the Board impose a condition on the Proposed Transaction that requires CPKC (or CN if it acquires the line) to maintain commercially reasonable rates and provide service at or above current service levels commensurate with shipper demand to maintain CSXT's opportunity to compete effectively for traffic that can move most efficiently over the ESL-Kansas City Line to and from points on CSXT east of ESL.

4. Requiring efficient routing and permanent protection for shippers regarding the U.S. effects of CPKC's Mexican operations.

Any threat to the efficiency of the U.S. rail system is a threat to the public interest and the railroad industry's ability to increase the value of their capacity to serve the U.S. economy and increase its ability to divert traffic off the highways to railroads.

Especially regarding Mexico traffic over the Laredo gateway (80% of which is served by truck), railroads cannot hope to increase their market share – reducing costs to shippers, highway

congestion, and carbon emissions – unless that traffic can flow over the most efficient rail routes.[56]

One benefit claimed by Applicants for the Proposed Transaction is the more efficient and competitive movement of traffic to and from shippers in Mexico served by CPKC and shippers in the U.S. and Canada. Applicants have not shown how they will fulfill this promise. Instead, Applicants have obscured the details of railroad competition to and from Mexican points served by KCSM. (Carey V.S. at 36). The protections Applicants propose to assure the Proposed Transaction will enhance rather than reduce competition for cross-border movements are vague (Carey V.S. at 24).

A bi-directional assessment of cross-border traffic to and from KCSM stations shows (i) the need for concern that KCSR's dominance of this traffic north of the U.S. Mexico Gateway provides CPKC with the potential incentive and ability to reduce competition and harm shippers, and (ii) the need to impose conditions that assure CPKC cannot abuse KCSM's market power in Mexico. (Carey V.S. at 3, 5, 14, 15, 23, 41).

As explained by Professor Carey (Carey V.S. at 18-19) {{ [redacted] }}. Applicants project traffic diversions that are inexplicable without CPKC exerting market power or providing unrevealed operation or service advantages in the United States.[57]

As regards movements within the U.S. and subject to the Board's jurisdiction, the Board

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[56] *See* Carey V.S. at 33-34.

[57] The potential for uneconomic diversions by CPKC heightens CSXT's concerns regarding the risk that NSR' Responsive Application would continue and expand an inefficient, anti-competitive market allocation that could hurt competition for traffic moving to and from Mexico.

can directly regulate CPKC's adherence to any commitments or conditions imposed in this Proceeding. However, because the Board cannot regulate KCSM, the Board should not approve the Proposed Transaction without conditions to protect shippers from the risk that CPKC will abuse its market power in Mexico to hurt competition or the efficient movement of traffic to, from, or through Mexico and the U.S.

To aid the provision of such protection, the Board should require CPKC to provide shippers with sufficient information about CPKC's pricing and service plans for movements to and from points in Mexico served directly or indirectly by KCSM to, from, or through the U.S.

5. Finally, the Board should require that KCSM and all other CPKC controlled carriers will not economically close any gateway to or from points served by a CPKC controlled carrier.

Respectfully submitted,

/s/ Paul A. Cunningham

Kent A. Gardiner
Ryan C. Tisch
Crowell & Moring LLP
1001 Pennsylvania Avenue NW
Washington, DC 20004-2595
(202) 624-2674
rtisch@crowell.com

Paul A. Cunningham
Harkins Cunningham, LLP
1750 K Street NW, Suite 300
Washington, DC 20006
(202) 415-4026
pac@harkinscunningham.com

Steven C. Armbrust
CSX Transportation, Inc.
500 Water Street
Jacksonville, FL 32202
(904) 359-3276

Louis E. Gitomer
Law Offices of Louis E. Gitomer, LLC
600 Baltimore Avenue, Suite 301
Towson, MD 21204
(410) 296-2250
Lou@lgraillaw.com

Attorneys for CSX Transportation, Inc.

Dated: February 28, 2022

cc: All Parties of Record
ALJ McCarthy

CERTIFICATE OF SERVICE

I hereby certify that I have caused the foregoing CSX Transportation's Comments and Request for Conditions in Docket No. FD-36500, *Canadian Pacific Railway Limited; Canadian Pacific Railway Company; Soo Line Railroad Company; Central Maine & Quebec Railway US Inc.; Dakota, Minnesota & Eastern Railroad Corporation; and Delaware & Hudson Railway Company, Inc. – Control – Kansas City Southern, The Kansas City Southern Railway Company, Gateway Eastern Railway Company, and The Texas Mexican Railway Company*, to be served electronically or by first class mail, postage pre-paid, on all parties of record in this proceeding.

S/ Paul A. Cunningham

Paul A. Cunningham
Attorney for CSX Transportation, Inc.

February 28, 2022

Exhibit A

PUBLIC VERSION

BEFORE THE
SURFACE TRANSPORTATION BOARD

DOCKET NO. FD 36500

CANADIAN PACIFIC RAILWAY LIMITED; CANADIAN PACIFIC RAILWAY COMPANY; SOO LINE RAILROAD COMPANY; CENTRAL MAINE & QUEBEC RAILWAY US INC.; DAKOTA, MINNESOTA & EASTERN RAILROAD CORPORATION; AND DELAWARE & HUDSON RAILWAY COMPANY, INC. – CONTROL – KANSAS CITY SOUTHERN, THE KANSAS CITY SOUTHERN RAILWAY COMPANY, GATEWAY EASTERN RAILWAY COMPANY, AND THE TEXAS MEXICAN RAILWAY COMPANY

CSX TRANSPORTATION, INC.'S COMMENTS AND REQUEST FOR CONDITIONS

VERIFIED STATEMENT OF PROFESSOR JULIE M. CAREY
AND DR. ALBERT W. BREMSER
NATIONAL ECONOMIC RESEARCH ASSOCIATES, INC.
(NERA)

TABLE OF CONTENTS

I. INTRODUCTION AND SUMMARY CONCLUSIONS 1

II. APPLICANTS' COMPETITION ANALYSIS IS INCOMPLETE AND RAISES UNIQUE ISSUES REGARDING MEXICO THAT WARRANT FUTURE CONDITIONS 5

A. Efficiency Considerations for a Competitiveness Assessment 6

B. The Remainder of Applicants' Vertical Effects Analysis is Incomplete and Insufficient 14

C. Recommended Conditions 23

III. APPLICANTS' LIMITED AND AMBIGUOUS COMMITMENTS TO KEEP "AFFECTED" GATEWAYS COMMERCIALLY OPEN 24

IV. THE PROPOSED TRANSACTION OFFERS FEW PUBLIC BENEFITS: APPLICANTS' CLAIMED PUBLIC BENEFITS ARE OVERSTATED AND MOST ARE ONLY PRIVATE BENEFITS 25

A. Applicants' Claimed Public Benefits are Primarily Potential Private Benefits to the Combined CP and KCS railroads 25

B. The Application Overstates Incremental Profits from Traffic Diversions 31

C. Analysis of Proposed Transaction Benefits and the Purchase Price Indicates that CPKCS has Less Benefits per Dollar Paid as Compared to Other Transactions 37

D. The High Incremental Debt Incurred for the Proposed Transaction Is Unlikely To Be Offset By Incremental Transaction Benefits Claimed 40

V. COMPETITIVE ISSUES WITH MERIDIAN SPEEDWAY 43

A. NSR's Request for Expanded Market Division and Asset Control on the Meridian Speedway and Conditions Necessary to Ameliorate Competitive Concerns 43

B. Competitive Concerns Arising from the Market Allocation Scheme on the KCS/NSR Meridian Speedway's 44

C. Expansion of NSR' Exclusive Share of Traffic that can move over the Speedway Will Further Reduce Competition in the Eastern Railroad Markets 52

D. Recommended Conditions to Ameliorate Competitive Concerns Regarding the Meridian Speedway and Affecting Eastern Rail Markets 54

I. INTRODUCTION AND SUMMARY CONCLUSIONS

My name is Julie M. Carey. I am an economist and Managing Director with National Economic Research Associates, Inc. ("NERA"). I routinely provide expert evidence before regulatory agencies, including the Surface Transportation Board ("STB" or the "Board"), as well as in commercial disputes before arbitrators and courts. I have approximately 25 years of experience addressing economic issues in the energy and transportation sectors. I have worked on numerous rate reasonableness disputes before the STB by providing economic evidence regarding stand-alone costs and future expectations of volume, revenue, and rates. I also have experience conducting economic analysis within disputes regarding haulage or trackage agreements. My work is routinely focused on economic analysis at the intersection of competition and regulation across energy and transportation industries. I have conducted competition analyses many dozens of times for the purposes of the regulatory approval of mergers and acquisitions, claims of discrimination, manipulation or anticompetitive behavior and for a variety of other purposes including within investigations and commercial disputes. Through my consultancy work, I have substantial experience providing consulting and testifying expert opinions involving competition, negotiated and market-based rates, economic damages, valuation analyses, and other economic analyses within regulatory and commercial disputes associated with transportation and other regulated and unregulated industries. In addition to my economic consultancy practice, I am an Adjunct Professor at Georgetown University, where I teach energy economics and policy in the graduate economics and political economics program, which includes instruction on the economics and regulation of railroad transportation. My Curriculum Vitae is attached as Exhibit 1. I am a addressing the competitive aspects in this verified statement ("V.S").

My name is Albert W. Bremser. I am a financial economist and an Associated Director with National Economic Research Associates, Inc. ("NERA"). I have a Ph.D. in Finance and I am a Chartered Financial Analyst (CFA) charterholder. I apply economic, finance, accounting and quantitative principles to regulatory and non-regulatory matters, which includes railroads. I provide expert evidence before regulatory agencies such as the Federal Energy Regulatory Commission ("FERC"). My Curriculum Vitae is attached as Exhibit 2. My areas of responsibility in this verified statement involve the financial analyses discussed in Section IV.A, IV.C, and IV.D, as supplemented by Professor Carey.

We were retained by Harkins Cunningham LLP on behalf of CSX Transportation ("CSXT") in this matter to review the Application that is the subject of this proceeding and provide an

economic opinion. In the Application to the Surface Transportation Board ("STB"), Applicant Canadian Pacific Railway Limited ("CP") proposes to acquire control of Applicant Kansas City Southern (KCS) and its subsidiaries, including The Kansas City Southern Railway Company ("KCSR") and Kansas City Southern Mexico ("KCSM") (the "Proposed Transaction"). The proposed combined company would be called CPKC or CPKCS. Applicants state the Proposed Transaction will combine two end-to-end railroads and lead to more efficient transportation services with no threat to competition.[1]

The Applicants' competition assessment is presented by Dr. Majure, who purports to weigh the potential for reduced competition against the potential benefits of the Proposed Transaction. When evaluating the vertical effects of the Proposed Transaction, Dr. Majure's assessment assumes that converting interline moves to single line service will result in enhanced efficiencies (citing unreliable claims by others) , and that CPKC's mere promise to keep the "affected" gateways open is sufficient to prevent competitive harm.[2] Applicants' Proposed Transaction Benefits, however, are inadequately supported and highly uncertain. The majority of Applicants' claimed efficiencies are not efficiencies but revenue diversions and potential private benefits that would accrue solely to Applicants. Applicants identify few potential expense or cost savings attributable to the Proposed Transaction that could be passed on to customers.

Dr. Majure provides an incomplete and inadequate competition analysis in support of the Applicants' claim that the Proposed Transaction poses no threat to competition and his conclusion that the Proposed Transaction will likely enhance competition.[3] The analysis is particularly deficient regarding potential harm relating to traffic to and from points in Mexico under KCSM's substantial market power. A more granular and complete vertical effects analysis requires a review of traffic moving south to Laredo (instead of just north of Laredo as assumed by Dr. Majure) and of specific customer locations for all traffic moving to and from KCSM points (instead of broad regions).

Conducting this expanded market share analysis demonstrates the potential of the combination of the two networks to adversely affect competition because it shows {{ [redacted] }} Economic analysis demonstrates that the multitude of locations not

[1] Railroad Control Application, Canadian Pacific Railway Limited; Canadian Pacific Railway Company; Soo Line Railroad Company; Central Maine & Quebec Railway US Inc; Dakota, Minnesota & Eastern Railroad Corporation; and Delaware & Hudson Railway Company, Inc. – Control – Kansas City Southern; The Kansas City Southern Railway Company; Gateway Eastern Railway Company; and The Texas Mexican Railway Company, Docket No. FD 36500, filed October 29, 2021 (Application). KCSM is not an Applicant and Applicants contend KCSM is not subject to the Board's jurisdiction. Hereafter, "CPKC Application".

[2] Verified Statement of Dr. Majure, CPKC Application, October 2021 V.S., ¶ 15-19. Hereafter, "Majure V.S.".

[3] Id. ¶ 24.

available to KCS/KCSM prior to the Proposed Transaction provide CPKC with the potential ability to adversely affect competition for traffic movements to and from Mexico after the Transaction. They will provide the Applicants an increased incentive and ability to reduce competition and harm shippers by economically eliminating or foreclosing rival railroads from the U.S. segments of these moves with a profitable pricing strategy (an analysis that Dr. Majure could have conducted but did not).

Substantial current and future cross-border rail traffic with Mexico is expected through the Laredo Gateway and it is important for the overall efficiency of the North American railroad network to ensure that traffic movements involving Mexico can move over the most economically efficient routes, consistent with the public interest. Properly analyzed, the Proposed Transaction could potentially impair competition related to Mexico which is best addressed through conditions set by the STB to ensure that shippers to and from Mexico and the U.S. are assured the opportunity for competition on commercially reasonable terms (and service) with CPKC from carriers north of the Laredo gateway. Requiring commercially reasonable terms should extend to all gateways used for traffic movements to and from Mexico as there are many shipper locations impacted. In doing so, the STB should also allow shippers to challenge rates and service for all segments of cross-border movements and secure remedies that, absent conditions would not be available because of limits on STB jurisdiction.

Most of Applicants' asserted transaction-related public benefits – roughly $888 million annually in a normal year and $1 billion in 2025[4] – are not public benefits, but are primarily private benefits that will accrue solely to CPKC through the diversion of revenue from other railroads (81%). Further, these benefits are predominantly associated with traffic diversions to routes where CPKC has longer and disadvantaged routes and to routes where these diversions could be secured without the Transaction.

The Applicants' supported benefits are much lower than their total claimed benefits and much smaller as a proportion of transaction costs than those demonstrated in prior large railroad transactions. This should lead the Board to review whether the Applicants' incremental debt[5]

[4] Public Version of Application, App. Vol. 1, p. 19. "As described in the Summary of Benefits Exhibit attached as Appendix B to this Volume, quantified public benefits would be more than $880 million annually in 2019 dollars."

[5] Applicants identified incremental debt of $8.5 billion. This figure appears to exclude a small amount of annual incremental dividends ($82 million), that if added, would be consistent with the STB's statutory definition of fixed charges (Section 1180.6(a)(2)(iii). *See* Application, App. Vol. 1, p. 22. and Exhibit 18, pp. 7 -10; App Vol. 1. pp. 150-153.

incurred for this Proposed Transaction can be supported by the potential additional revenues or costs savings from the Proposed Transaction.

Finally, the Applicants' public benefits analyses are not tailored specifically to the U.S, and do not quantify the cost savings or private benefits limited to the U.S., thereby limiting the Board's capacity to ascertain the Proposed Transaction is consistent with the public interest of the United States.

In addition to these aspects of the Application, I also discuss the potential for further competitive harm to customers in the Eastern U.S. that results from the KCS and Norfolk Southern Railway Company ("NSR") Meridian Speedway Agreements and could be aggravated as a result of the transactions described in NSR's Description of Anticipated Responsive Application.[6] These anticompetitive concerns arise from the Meridian Speedway's use of an explicit market allocation scheme that divides the control of certain geographic areas and products between KCS and NSR and has vertical effects that reduce competition. This type of market division is prohibited by antitrust agencies and was exempted from regulatory review by the STB with no competition analyses.

The Meridian Speedway agreements enabled NSR to vertically integrate (economically) across the Meridian Segment into its Eastern rail system (by eliminating KCS's segment), providing NSR with exclusive access from Shreveport to Meridian for transcontinental intermodal traffic for specific origin and destination location pairs in the Southwest and Southeast U.S that are advantaged on the Meridian Speedway route. The southeastern U.S. locations were not previously served by KCS. Both NSR's existing exclusive rights and its proposed expansion of those rights raise anticompetitive concerns and distort competition between NSR, KCSR, and CSXT for NS Traffic for which the most efficient route is over the Speedway. This type of market division, which serves only to reduce competition in vertically affected markets, is prohibited by antitrust agencies and this market division was never reviewed by the STB with respect to its effect on competition.

The Board should not approve the Proposed Transaction without conditions to mitigate the risks it presents for competition. Most important, NSR's exclusive right to move "NS Traffic" (hereafter referred to as "NSR Exclusivity Traffic") over the Meridian Speedway should be abolished and CPKC be freed to work with its connecting carriers to develop commercially reasonable terms to interchange or otherwise move traffic that is carried over the Meridian Speedway. To the extent the Board approves NSR's request to expand its market division to additional products and a broader

[6] *See* STB Finance Docket No. 36500, Description of Anticipated Responsive Application by Norfolk Southern Railway Company, January 12, 2022.

geographic scope, additional conditions to protect competition should be imposed.[7] Without conditions, any such expansion would further diminish competition in Eastern railroad markets for traffic movements across the Meridian Speedway.

II. APPLICANTS' COMPETITION ANALYSIS IS INCOMPLETE AND RAISES UNIQUE ISSUES REGARDING MEXICO THAT WARRANT FUTURE CONDITIONS

Regarding the potential harm to competition, Applicants' witness, Dr. Majure, provides an incomplete and inadequate competition analysis, particularly regarding potential harm relating to traffic to and from points on KCSM in Mexico.[8] A complete vertical effects analysis of traffic involving Mexico under KCSM's substantial market power should include: (1) analysis of traffic moving south to Laredo (instead of just north of Laredo as assumed by Dr. Majure), based on (2) analysis of specific customer locations (rather than just the broad geographic areas—Mexican states, BEAs in the U.S., and Economic Regions in Canada) assessed by Dr. Majure.[9] These more granular analyses show {{ [redacted] }} than Dr. Majure's analysis and confirm the need for further assessment of anticompetitive effects from the Proposed Transaction, including evaluating potentially profitable pricing strategies to foreclose rivals.

Based on my analysis below, with KCSM's substantial market power of railroad movements entering and exiting the U.S. for its customers, and KCS's dominance of movements to and from KCSM at Laredo, the expanded CPKC network locations, the combined CPKC could potentially impair competition through vertical effects absent conditions by the STB to ensure that the important Laredo gateway (and all gateways used for traffic movements to and from Mexico) remain open on commercially reasonable price and service terms for rivals such that competition is not distorted, including allowing future challenges to rates and service.

[7] I understand that CPKC plans to address NSR's proposed expansion in their forthcoming filing. I will supplement my opinion and address the NSR proposal.

[8] My assessment of the potential competitive effects is limited to the vertical effects and not the potential horizontal effects due to time limitations.

[9] Broad geographic areas are not appropriate in Dr. Majure's vertical effects analysis because they do not accurately portray station level access, which is necessary to serve most shippers, like automotive plants. This is distinct from analysis of intermodal flows in other part of this opinion.

A. Efficiency Considerations for a Competitiveness Assessment

Dr. Majure's assessment of the potential vertical effects from the Proposed Transaction relies in part on claims by others that converting interline moves to single-line service will increase economic efficiency. Dr. Majure uses the statements of CP Witness Brooks to support the Applicants' contention that shifting from interline service to single-line service will enhance efficiency and for the sufficiency of Applicants' promise to keep the gateways open.[10] Dr. Majure did not independently study any anticipated changes to traffic flows and assumed traffic will be diverted as projected by other witnesses. Dr. Majure relies on the proposition that CPKC can compete with other railroads (and therefore effectuate Applicants' Transaction related Benefits) through the demonstration of "diverted traffic," presented by other Witnesses."[11] From those assumed future efficiencies, Dr. Majure infers that the proposed vertical transaction provides the opportunity for procompetitive benefits.[12] He does not, however, investigate those asserted opportunities.[13] And the assertions he relies on are not reliable.

Applicants' claimed Total Transaction Benefits (supporting their contention of procompetitive benefits) include substantial incremental profits from traffic diversions[14] away from competitor railroads, trucks, or other growth initiative traffic. However, Applicants' claimed Total Benefits are inadequately supported and uncertain. The majority of their claimed Total Benefits would produce only potential private benefits that would accrue solely to the Applicants. These private benefits are 81% of the Total Benefits claimed by Applicants. Potential public benefits from anticipated Transaction-related cost savings (discussed in Section IV below) are only 19% of claimed Total Benefits.

Applicants' incremental profits from traffic diversions that are estimated by others are referenced by Dr. Majure to support his claim that merger efficiencies will enhance competition due

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[10] "All of these difficulties suggest that the reason interline service is inferior to single-line service is that separate railroads are limited in what they can do to align their incentives with respect to joint operations – limitations that fit into the model of vertical mergers enhancing efficiency by enabling more efficient coordination." Majure V.S., ¶ 17.

[11] "…[A]s a result, the combined CP/KCS product would be expected to divert some traffic from other railroads" and you rely on other witnesses for any possible assumed and traffic diversion to CP/KC (relying on Mutén, Wahba Naantz and FTI (Brown Zembrowski)" Majure V.S. ¶18 and footnote 8. {{ [redacted] }}

Majure V.S. ¶ 10.

[13] Dr. Majure has presented no specific analysis to quantify potential benefits from vertical integration. In deposition, {{ [redacted] }}

Applicants' traffic diversions are sponsored by three witnesses, including rail diversion (Brown/Zebrowski), truck to rail diversions (Mutén) and growth initiative volumes (Wabba and Naantz).

to the "single-line service."[15] However, the Applicants' traffic diversions include many that they expect to be diverted to Applicants' longer and otherwise disadvantaged routes as well as many that can be realized by CP and KCS independently without the Proposed Transaction.[16] They contend no rate reduction is required in most instances to effect those diversions.[17]

Figure 1 below shows CPKC's Laredo to Chicago route that is longer and more circuitous than UP's (CPKC is approximately 24% longer than UP).[18] This is just one prominent example of CPKC's inefficient routing as compared to other railroad carriers (as discussed in Section IV.B below. Nearly {{ }} of the Applicants' claimed traffic diversions involve railroad movements between Mexico and the upper Midwest U.S., including to and from Chicago.[19] Notably, in his comments on the proposed CN-KCS merger, {{ }}, a process which is inconsistent with the assumptions employed by the witnesses he relies on in this instance.[20] None of these asserted traffic diversions involving Mexico are based on rate reductions.

[15] Majure V.S. ¶ 15-19. { }

See Section IV. B and Carey HC-WP "Rail and Truck Diversions.pdf" and HC-WP "Growth Initiative.pdf" for CPKC routes that compete with other railroads.

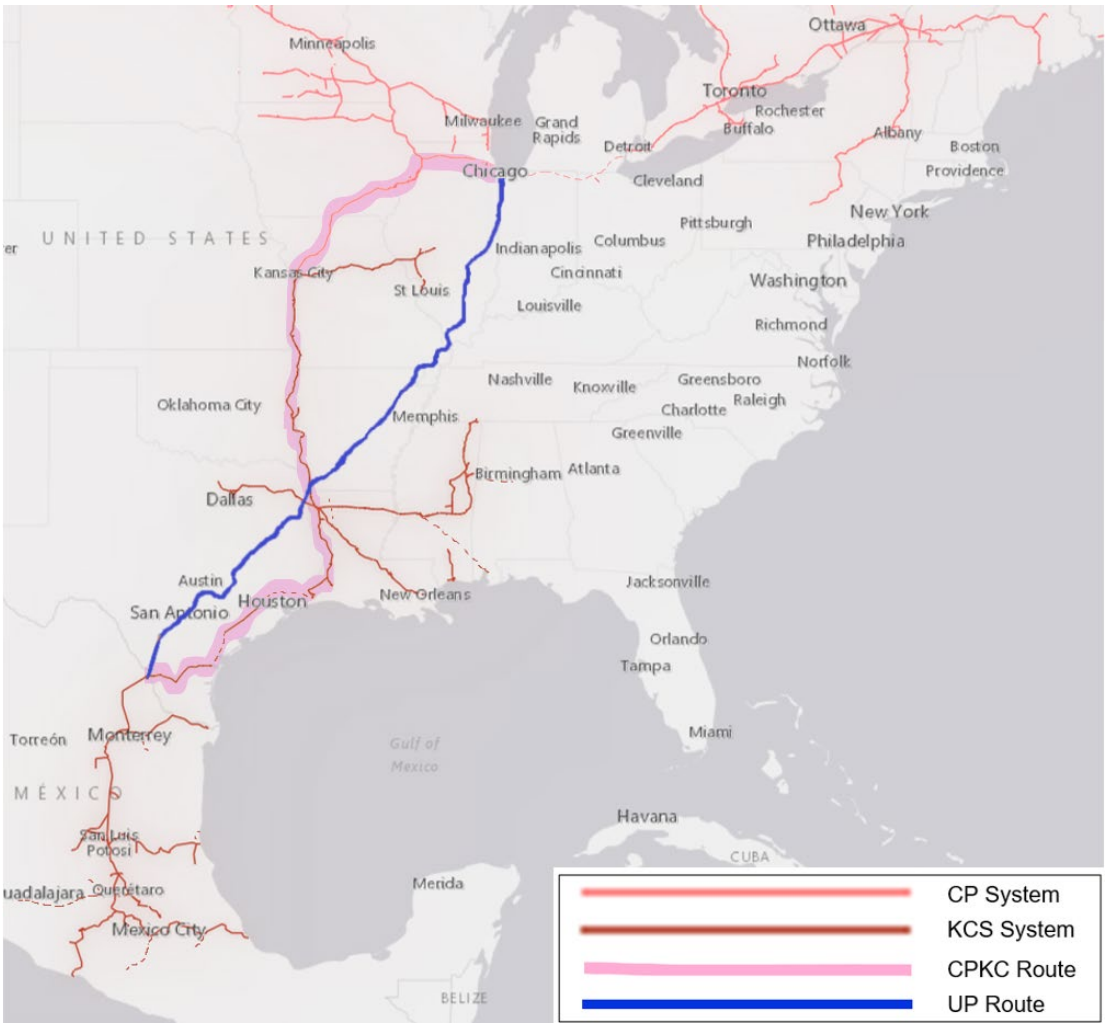
[17] The primary single route that Applicants contend that rail rates will be reduced is {{ }}.

[18] 24% = (1724/1390)-1

[19] {{ }} out of 509,490 units. When considering all diversions to all destinations and origins, over {{ }} of diversion units involve routes which include Mexico. *See* Carey HC-WP "Mexico Diversion Claims.xlsm."

[20] *See* Majure CN V.S. ¶ 88. {{ .}} *See* Brown and Zebrowski HC-WP "8-Diversion Identification.xlsx"

Figure 1: CPKCS' Rail Route from Laredo to Chicago versus UP



The principal economic efficiencies associated with vertical transactions in the railroad industry are cost reductions, including reductions in operational costs from efficiencies and reduced overhead.[21] These reduced costs can be passed along to shippers in the form of reduced rates. This is especially true of transactions that convert interline traffic to single line traffic. Prior STB mergers, and analysis of these mergers, identify reduced rates as a principal indicator of economic efficiency

[21] *See* Scherer, F.M., and Ross, David, "Industrial Market Structure and Economic Performance", Third Edition, pp. 524-527. *See* Utton, M.A., "Market Dominance and Antitrust Policy", Edward Elgar Publishing Limited, 1995, pp 216-219. *See also* Carlton, Dennis W. and Perloff, Jeffrey M., "Modern Industrial Organization", Fourth Edition, 2005, at pp. 415-416.

justifying vertically integrating transactions.[22] These more dated transactions occurred a time with challenges with excess rail capacity and ample opportunities to reduce costs and to benefit shippers.

Cost reductions can be achieved through the conversion of interline service to single-line service, (also called vertical integration), by removing the margin (above variable cost)[23] that each carrier requires to service the traffic, and replacing it with only a single margin required by the single railroad operating single line service.[24] Additionally, there are greater opportunities to reduce the margin through cost reductions from removal of redundancies in each railroad's operations, such as general and administrative functions, procurement, and other duplicative overhead costs. The more these types of costs can be reduced, the stronger the overall Transaction benefits. Taken together, the cost reductions and improved operating efficiencies will benefit the customers with improved service and likely lead to rate reductions in the future. Therefore, Applicants' position that no rate reduction is needed to entice shippers to use its single line service to and from Mexico (and most other claimed traffic diversions) requires close inspection. Dr. Majure does not directly address expected cost and rate reductions as a recognized economic efficiency benefit in this case. However, he did so when he discussed whether a {{ [redacted] }} likely raises concerns of reduced competition and contrasted that with a {{ [redacted] }}.[25] Keen focus on the Applicants' projected cost reduction is needed to determine if the Proposed Transaction is likely to result in procompetitive benefits from the creation of single line service (as Dr. Majure concludes).[26]

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[22] An analysis of 1985-2005 U.S. freight rail data demonstrates that average prices of shipments decrease by approximately 15% following railroad mergers, the majority of which is owed to re-optimized routing and network changes. *See* Chen, Yanyou, "Efficiency Gain from Mergers: Evidence from the U.S. Railroad Network", September 4, 2021. *See also* Berndt Et Al., "Cost Effects of Mergers and Deregulation in the U.S. Rail Industry", The Journal of Productivity Analysis, 4, 127-144 (1993). The STB has stated that "[t]he primarily end-to-end (vertical) integration of the rail operations conducted by BN and Santa Fe will enable the consolidation carrier to reduce the costs it incurs and to improve the services it provides. Shippers should benefit from lower rates and improved service, including new single-line service." *See* Burlington Northern Inc. et al. – Control and Merger – Santa Fe Pacific Corporation et al., Finance Docket No. 32549 (Decision No. 38 decided Aug. 16, 1995), 10 I.C.C.2d.

[23] The margin (above variable cost) and contribution margin are terms used in the railroad industry to refer to the revenue in excess of variable cost or mark-up over variable cost. Margin or contribution margin are used to evaluate the additional monies available to the railroad above the incremental cost to serve the traffic that can contribute the overhead functions of the railroad and the broader network investment activities.

[24] The multiple lumps are also referred to as double marginalization. *See* U.S. Department of Justice & The Federal Trade Commission, "Vertical Merger Guidelines", June 30, 2020, at Section 4a. Antitrust agencies consider the net effect on competition of the vertically merged unilateral incentives (e.g. foreclosure and elimination of double marginalization).

[25] { [redacted] }} *See* Expert Statement of W. Robert Majure, Finance Docket No. 36514, Canadian National Railway Company, Et Al. – Control – Kansas City Southern, Et Al., June 28, 2021 ("Majure CN V.S.") ¶ 86 and 38.

[26] *See* Scherer, F.M., and Ross, David, "Industrial Market Structure and Economic Performance", Third Edition, pp. 524-527. *See* Utton, M.A., "Market Dominance and Antitrust Policy", Edward Elgar Publishing Limited, 1995, pp 216-219. *See also* Carlton, Dennis W. and Perloff, Jeffrey M., "Modern Industrial Organization", Fourth Edition, 2005, at pp. 415-416.

To further assess the potential economic efficiencies from the Transaction and the extent of potential pro-competitive benefits, I investigated the Applicants' anticipated cost savings from the Proposed Transaction. The small cost savings benefits forecast by Applicants suggests a limited impact on future customers.[27] Notably, the limited anticipated cost savings from the Proposed Transaction are not comparable to those expected from prior railroad consolidations. Applicants in those prior transactions forecast substantial Transaction related cost saving, which provided the STB with a more reliable expectation of future benefits and rate reductions.[28] The Proposed Transaction offers fewer opportunities for cost saving than prior Major Transactions. And those opportunities would be handicapped because CPKC's routes are longer and otherwise disadvantaged as compared to competing routes. Consequently, CPKC has fewer opportunities to produce the public efficiency benefits that justify vertical transactions. As I discuss above, Applicants' failure to project significant cost savings or rate decreases is an important consideration in a vertical effects assessment.

Regarding potential opportunities for economic efficiency gains associated with CPKC's conversion of interline service to single line service, the Applicants make general claims but provide limited evidence or analysis. First, the CP business witness supporting the efficiencies from the single line offering (Mr. Brooks),[29] which consist of {{ }} traffic diversions involving Mexico,[30] confirms no "hard analysis" was conducted with respect to CPKC competitiveness compared to UP or BNSF and he has no sales experience with Mexico to draw upon in such estimates.[31] Indeed, in the normal course of business prior to the announcement of the Proposed Transaction, CP's acknowledged {{"

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[27] It is unclear why Applicants' Transaction benefits include limited cost savings, but this could potentially arise because of the lesser contribution margin that KCS has observed in recent years and exists in the Pre-Transaction state which would limit the opportunity to reduce overhead. *See* Surface Transportation Board's 2018 Determination of Railroad Revenue Adequacy, Docket No. EP 552 (Sub-No.23) (STB served September 5, 2019).

[28] *See* Section IV.B for a discussion. Applicants' cost savings benefit on a percentage basis are lower than other transactions due to the very large private benefits.

[29] Mr. Brooks describes lessons learned from prior interline agreements to contrast with "full potential of single-line service". *See* Brooks V.S ¶ 28-36 at 36.

[30] {{ }} out of 509,490 units. When considering all diversions to all destinations and origins, over {{ }} of diversion units involve routes which include Mexico. *See* Carey HC-WP "HC-Mexico Diversion Claims.xlsm."

[31] {{

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Applicants provide no analysis of route distance, cycle times, or other specific service quality elements unique to CPKC single line movements compared to its competitor railroads (with shorter routes and other advantages).[33] UP's route from Laredo to Chicago is about 24% shorter than CPKC. Challenges with curvatures and hills on CP's system between Davenport, Iowa, and Kansas exist as well as steeper grades near the Des Moines River Valley that impact CPKC transit times—a route that most claimed traffic diversions will traverse.[34] The strength of UP's "spine" between Minneapolis and Kansas City as well as UP from Dallas and Topeka, KS has been noted in industry trade press.[35] Absent specific analysis, as opposed to general claims based on "experience"[36] it is impossible to make a reasoned assessment of, whether and to what extent, CPKC could attract shippers away from the existing competitors. Dr. Majure did not the investigate service-related quality differences (if any) to enhance CPKC's competitiveness.[37] Other witnesses that Dr. Majure relies on for diversions do not identify specific distinguishing service attributes of CPKC that other

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Updated Synergies Estimates – Proposed Adjustment, July 1, 2020, CP-HC-00007375 to CP-HC-00007383 at CP-[redacted]

Trade press document additional challenges with CP's network route as compared to UP. See Journal of Commerce online, "Merged CP-KCS would offer new cross-border intermodal growth ramp", April 2021. Available at https://www.joc.com/rail-intermodal/class-i-railroads/canadian-pacific-railway/merged-cp-kcs-offers-new-cross-border-intermodal-growth-ramp_20210325.html; "The CP route will require more locomotives and miles due to the route profile south of the Quad Cities and will be more expensive to operate compared to Union Pacific and BNSF." The Spine Line refers to UP's track between Minneapolis and Kansas City. Kayganich anticipates similar challenges to providing timely service between Shreveport, Louisiana, and Kansas City, compared with UP's track between Dallas and Topeka, Kansas."

[35] Ibid.

[36] [redacted]

In deposition testimony, [redacted]

railroads lack and do not analyze CPKC routes with other market competitors' rates or compare service attributes.[38]

Regarding the CPKC operating plan, while Applicants claim to {{ }}.[39, 40] Applicants also did not consider the potential growth of traffic from other carriers on shared routes in Texas, which could cause unforeseen service delays.[41] Applicants' responses to interrogatories regarding competitively significant service elements {{ }}[42] In sum, the Application does not adequately demonstrate tangible and likely enhanced efficiencies that are assumed by Dr. Majure in his vertical effects analysis and which he concludes create opportunities for procompetitive benefits.[43] The lack of that support renders his analysis incomplete and, from the perspective of standard competition analyses, inadequate to support any conclusion that the Proposed Transaction poses "would not

[38] Brown/Zebrowski V.S. ¶ 19-98; Mutén V.S. ¶ 45-52; Majure V.S. ¶ 18

[39] In deposition testimony {{ }}

See deposition of Mr. Elphick and Mr. Orr generally at 80-155 and 155:10-19.

[42] { }}

[43] Majure V.S. ¶ 10, 15-19.

substantially lessen competition."[44] Additional analysis would have been expected before the antitrust agencies[45] including within a legal proceeding.[46]

Regarding assurances regarding gateways, Dr. Majure also relies on other witnesses (Brooks)[47] to support the contention that the existing gateways with other carriers will remain open.[48] The plausibility of this assumption is a cornerstone of Dr. Majure's assertion that the Proposed Transaction will have no negative vertical impacts on competition that would reduce the claimed efficiencies from the Proposed Transaction.[49] Dr. Majure appropriately recognizes the importance of both service and rates to ensure transportation jointly provided with competitors, or would-be competitors, is not subject to competitive harm by CPKC. However, the witness Dr. Majure relies on for concluding CPKC will not discriminate against other carriers at Laredo—the only gateway Dr. Majure examines—is CP's Executive Vice President and Chief Marketing Officer John Brooks.[50] Mr. Brooks only provides general and non-specific commitments that lack reliable guarantees.[51] CP commits to working with shippers but does not promise concrete standards that would ensure that CP (1) sets commercially reasonable rates (and does not directly or indirectly raise rivals costs; and (2) provides service on a non-discriminatory basis, with no service related distortions involving rival railroads.[52] Mr. Brooks' vague and limited commitments provide no concrete assurance that CPKC will actually keep all of its gateways open.

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[44] "…not likely to impair competition through vertical effects." Majure V.S. ¶ 10, 24.

[45] The 2020 Vertical Merger Guidelines Section 4a "Unilateral Effects – Foreclosure and Raising Rivals' Costs" discusses the potential for a merged firm to profitably use its control of a related product to weaken or remove the competitive constraint from rivals in the relevant market (e.g., increase price or lower quality of the related product, or refuse supply to rivals entirely). *See* U.S. Department of Justice & The Federal Trade Commission, "Vertical Merger Guidelines", June 30, 2020, at pp. 4-6.

[46] For an illustrative example of empirical analysis, *see* Shapiro, Carl, "Vertical Mergers and Input Foreclosure Lessons from the AT&T/Time Warner Case", Review of Industrial Organization (2021) 59:303–341.

[47] Majure V.S. ¶ 17; Brooks V.S. ¶ 6-12, 28-36.

[48] Brooks V.S. ¶ 42-46.

[49] Majure V.S. ¶ 15 -19.

[50] Brooks V.S. ¶ 1.

[51] {{ [redacted] }}

Economic literature recognizes that the potential for refusal to deal exists when a monopolist of an indispensable input is vertically integrated in a consolidation.[53] While KCS made general commitments in acquiring the Tex-Mex and the STB required conditions,[54] any evaluation here must focus on the Proposed Transaction, not Tex-Mex. Applicants have not asked the STB to impose a condition on the Proposed Transaction like the one it required in Tex-Mex.[55] Yet the Proposed Transaction presents circumstances and potential competitive concerns different from those of any prior Transaction. It is distinctive because of international components not regulated by the Board, coupled with the substantially expanded geographic scope of potentially affected customers (as discussed below). Most important, CP serves substantial traffic and revenues that originate or terminate in Mexico (on KCS via KCSM).[56]

B. The Remainder of Applicants' Vertical Effects Analysis is Incomplete and Insufficient

If Applicants' expected diversions, which appear to be dramatically overstated, fail to materialize, the financial risks and pressures associated with the high Transaction price and substantial debt incurred by the new entity[57] could heighten CPKC's incentive to reduce competition to recoup transaction-related costs.

Dr. Majure provides an incomplete and inadequate competition analysis for the Proposed Transaction, particularly regarding potential harm relating to traffic to and from points on KCSM in Mexico. When evaluating vertical effects on competition, regulatory agencies (including antitrust agencies), assess the ability and incentive of the merged entity to engage in unilateral actions that

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[53] *See* Scherer, F.M., and Ross, David, "Industrial Market Structure and Economic Performance", Third Edition, pp. 524-527.

[54] The acquisition by KCS of control of Tex Mex was approved by the STB subject to certain conditions that were imposed to ensure the transaction wouldn't result in competitive harm. *See* Decision No. 12, STB Finance Docket No. 34342, Kansas City Southern – Control – The Kansas City Railway Company, Gateway Eastern Railway Company & The Texas Mexican Railway Company, Service Date November 29, 2004 at pp. 13-14, 18-19. *See also* {{ [redacted] }} {{ [redacted] }}. *See* Carey HC-WP "HC-Mexico.pdf"

[57] *See* Section IV.D.

may lessen competition.[58] The purpose of such an analysis is to evaluate CPKC's ability to cause anticompetitive harm by raising rivals' costs or creating other impediments to their ability to compete[59] as a result of the integration of an upstream input into the downstream product.[60]

As a starting point, Dr. Majure does not give due consideration to the fact that KCSM both originates and terminates cross-border U.S. – Mexico rail traffic movements. Economic concerns regarding both destinations and origins on KCSM's network in Mexico, where KCSM enjoys substantial market power, warrant detailed inspection. Specifically, since railroad movements on Applicants' system are bidirectional (north to south and south to north) the vertical effects analysis should study the integration of the upstream KCSM/KCS into the downstream CP, as well as the upstream CP into downstream KCSM/KCS. However, Dr, Majure did not consider the latter which involves railroad transportation to destinations in Mexico.[61]

KCSM has substantial market power over most traffic moving to and from KCSM over Laredo.[62] The primary railroad competitor to KCSM in Mexico is Ferromex ("FXE"). While FXE has certain trackage rights to access customers on KCSM's network, its rights are limited to domestic traffic movements and FXE cannot use these trackage rights for export/import traffic.[63] Within Mexico, KCSM serves substantial intermodal and automotive traffic, with certain locations directly connected to FXE's longer route to the US through UP.[64] Dr. Majure's limited reference to potential railroad competition in Mexico and FXE is solely theoretical in nature, and therefore, insufficient to

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[58] For instance, rival foreclosure. *See* U.S. Department of Justice & The Federal Trade Commission, "Vertical Merger Guidelines", June 30, 2020, at section 4a. While the FTC withdrew the 2020 Vertical Merger Guidelines, it recognized the substantial improvements over the prior 1984 Merger Guidelines on this topic. *See* Federal Trade Commission, "Statement of Chair Lina M. Khan, Commissioner Rohit Chopra, and Commissioner Rebecca Kelly Slaughter on the Withdrawal of the Vertical Merger Guidelines Commission File No. P810034", September 15, 2021, at 2.

[59] Ibid. For a seminal article on this topic, *see* Salop, Steven C.; Scheffman, David T; "Raising Rivals Costs", American Economic Review, May 1983, v. 73, iss. 2, pp. 267-71. For an illustrative example of an empirical analysis of raising rivals' costs, *see* Shapiro, Carl, "Vertical Mergers and Input Foreclosure Lessons from the AT&T/Time Warner Case", Review of Industrial Organization (2021) 59:303–341.

[60] Ibid.

[61] The need to conduct analysis of destination markets has been raised in prior mergers. *See* Burlington Northern Inc. and Burlington Northern Railroad Company–Control and Merger–Santa Fe Pacific Corporation and the Atchison, Topeka and Santa Fe Railway Company, Finance Docket No. 32549, Decision No. 38, Service Date August 23, 1995 at pp. 48-49 and other cases referenced.

[62] *See* Carey HC-WP "HC-Mexico.pdf"

[63] FXE has a trackage agreement to access KCSM customer locations for the sole purpose of traffic movements within Mexico (i.e., no cross-border trade with the U.S.). "In 2010, Ferromex and KCSM finally reached agreement on the most important segments: access by KCSM to Guadalajara and Silao, and access by Ferromex to the main KCSM line from Viborillas to Ramos Arizpe. These agreements will expand competitive access for domestic traffic. However, the companies agreed not to use these trackage rights for export/import traffic" *See* 2014 OECD, "Freight Railway Development in Mexico", p. 24, available at https://www.itf-oecd.org/sites/default/files/docs/14mexicorail.pdf

[64] While automotive facilities require specific station level access due to the specifics of transporting that commodity, certain locations on KCSM automotive traffic locations do have competitive access to FXE. *See* Carey HCWP "HC-Mexico.pdf"

support any conclusion regarding the potential for harm to competition from the Proposed Transaction.[65] FXE has a separate rail line west of KCSM that interchanges traffic movements with UP at Eagle Pass, TX (which is west of Laredo).[66] An investigation of Mexico's railroad rate regulatory regime indicates that railroads have regulation through price caps by commodity type and distance that allows pricing flexibility that can be used by KCMS to affect shippers' opportunities to use of competitive railroad rivals to CPKC north of Mexico.[67] The Proposed Transaction will create incentives for anticompetitive behavior that were not present pre-Transaction, particularly if financial pressures exist to pay the incremental transaction debt and heightened competition results in few traffic diversions.

Dr. Majure's vertical effects analysis is limited to an assessment of market shares for traffic moving north from a large area in Mexico[68] through Laredo to broad geographic market areas in the U.S. and Canada.[69] He did not assess the potential for competitive harm regarding traffic moving south to Mexico.[70]

Regarding this limited set of northbound traffic, Dr. Majure's assessment of the vertical effects of the Proposed Transaction were not sufficient to support his conclusions. Dr. Majure reviewed a market share of all the traffic that KCSM brings to Laredo from Mexico and analyzed

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[65] Majure V.S. at ¶ 24-5. Dr. Majure refers to vertical effects with respect to the "solely-served shipper who has no ready alternative to KCS for originating its movements" at Majure V.S. ¶ 24. In deposition: [redacted] }}

See Carey HC-WP "HC-Mexico.pdf". While both Eagle Pass and Laredo are important gateways for traffic to and from Mexico, the gateways are situated on different networks and in different geographic locations. As such, the gateways are not equivalent in all competitive circumstances, and the relative market power of each railroad service provider will depend on the specific circumstances of each shipper. *See* App. Vol. 1, p. 71. *See also* {{[redacted].}}

See OECD (2017), "Review of the Regulation of Freight Transport in Mexico", pp. 84-86, available at https://www.oecd.org/centrodemexico/publicaciones/OECD%20(2017)%20Review%20of%20%20Regulation%20Freight%20Transport.pdf; Art. 46 of LRSF, available at https://www.diputados.gob.mx/LeyesBiblio/pdf/209_061120.pdf. *See* Carey HC-WP "HC-Mexico.pdf".

[68] Dr. Majure acknowledges that Mexican states are larger geographic areas than U.S. BEA areas, stating that "the median Mexican state is 58,400 square kilometers. The median U.S. BEA area is 29,843 square kilometers…" *See* Majure V.S. ¶ 48 footnote 27. Further, a Mexican state is not always a coherent economic grouping. For example. Ciudad Juárez and Chihuahua are both in the state of Chihuahua and have populations of roughly 1 million people, but are over 200 miles apart. *See* "2020 Census of Population and Housing," Instituto Nacional de Estadística, Geografía e Informatic available at https://en.www.inegi.org.mx/programas/ccpv/2020/

[69] States in Mexico, BEAs in the U.S. and Economic Regions in Canada. *See* Majure V.S. at ¶ 48.

[70] {[redacted]3}}

KCS's market share in BEA market areas served by KCS in the U.S.[71] Dr. Majure references this single analysis of the potential vertical effects of the Proposed Transaction[72] frequently and, along with his reliance on Applicants' vague open gateway commitments and very limited plausible efficiency claims, he concludes that the Proposed Transaction is "…not likely to impair competition through vertical effects."[73]

In discussing his conclusion, Dr. Majure asserts that for KCSM traffic to Laredo, KCS has a {{ }} market share beyond the Laredo and Robstown interchanges for northbound traffic from Mexico to his assumed BEA geographic market area served by KCS, and CP has a {{ }} market share for BEA geographic market areas served by CP (i.e., mutually exclusive geographic areas). I have replicated Dr. Majure's analysis and report the results in Figure 2 below.

Dr. Majure's vertical effects analysis is deficient because it is limited to northbound traffic from Mexico and does not analyze southbound traffic to Mexico.[74] In this case the vertical integration of market power in Mexico affects traffic that moves in both directions, i.e., to Mexico and from Mexico.[75] Dr. Majure should have reviewed southbound traffic integration of CP into downstream KCS and KCSM for potential anticompetitive effects (i.e., a similar concern as the northbound traffic). Southbound movements to Mexico are analogous to the northbound routes for movements through the Laredo Gateway.[76] Accordingly, I have addressed southbound traffic using Dr. Majure's methodology. Figure 2 below shows the southbound traffic to Mexico to provide a more complete depiction of all traffic with Mexico, including large traffic volumes for southbound traffic movements to Mexico destinations as compared to northbound movements from Mexico origins.[77] For the southbound traffic from Laredo to KCSM in Mexico, KCS has a {{ }} market

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[71] Majure V.S. ¶ 30-31 and Exhibit 2.

[72] Section 3.2. "The vertical effects of a CP and KCS combination would enhance rather than diminish competition."

[73] Majure V.S. ¶ 30-38, Exhibit 2 and specifically ¶ 38.

[74] {{ }}

Anticompetitive problems may arise when one or both levels of the integration possess market power. Given the high market share on southbound traffic, the downstream level of the integration from this perspective may cause concern. *See* Viscusi et al., "Economics of Regulation and Antitrust", The MIT Press, 2nd Edition (1995) pp. 229, 234.

[76] To the extent that shipper decisions could be impacted by upstream routing decisions regarding UP and its connection at Eagle Pass, both Laredo and Eagle Pass generally have the same relative proportions of cross border traffic for both northbound and southbound traffic. *See* Carey HC-WP "HC-Mexico.pdf"

[77] The importance of both northbound and southbound trade is recognized by regional trade authorities. *See* "Texas-Mexico Border Transportation Master Plan 2021", p. 17, available at https://ftp.dot.state.tx.us/pub/txdot/tpp/btmp/btmp-lrd-regional-plan.pdf

share before the Laredo and Robstown interchanges for assumed BEA geographic market areas served by KCS and a {{ }} market share for BEA geographic market areas served by CP. These much higher market shares raise anticompetitive concerns.

Figure 2: KCS Market Shares for US Movements Involving Mexico Traffic (Northbound and Southbound through Laredo; BEA Defines Market)[78]

In addition to forgoing analysis of southbound movements to Laredo, Dr. Majure's limited vertical effects analysis evaluates no specific shippers, nor the competitive circumstances of those shippers and how they could be harmed.[79] I conducted a more granular market share analysis to further investigate the potential for harm to shippers through reduced competition by analyzing a more limited geographic area that represents specific stations rather than the broad BEA geographic area assumed by Dr. Majure. Once again, the market shares presented on the more granular geographic market area demonstrate a {{ }} for KCS than the limited analysis conducted by Dr. Majure, which assumed a broad geographic market scope and only a northbound route. As shown in Figure 3 below, for the KCSM traffic to Laredo, KCS has a {{ }} market share after the Laredo and Robstown interchanges for northbound traffic from

[78] *See* Carey HC-WP "HC-Combined Majure Tables Summary.xlsx".

[79] Dr. Majure refers to vertical effects with respect to the "solely-served shipper who has no ready alternative to KCS for originating its movements" at Majure V.S. ¶ 24. In deposition: {{ .}}

Mexico to station location geographic market area served by KCS and a {{ }} market share for station location geographic market areas served by CP (i.e., mutually exclusive geographic areas). For the southbound traffic from Laredo to KCSM in Mexico, KCS has a {{ }} market share for assumed BEA geographic market area served by KCS and a {{ }} market share before the Laredo and Robstown interchanges for station location geographic market areas served by CP (i.e., mutually exclusive geographic areas).

Figure 3: KCS Market Shares for US Movements Involving Mexico Traffic (Northbound and Southbound through Laredo; Station Locations)[80]

The {{ }} for the Applicants are indicators of CPKC's potential incentive and ability to engage in anticompetitive actions. While the DOJ does not set a market share threshold in its guidelines on vertical mergers it states that "levels of concentration may nonetheless be relevant. For example, high concentration in the relevant market may provide evidence about the likelihood, durability, or scope of anticompetitive effects in that relevant market."[81] Market shares of the level described above, along with other circumstances in Mexico, are sufficiently high to warrant a closer look. Higher market shares for a specific firm lead to a more concentrated market which

[80] *See* Carey HC-WP "HC-Combined Majure Tables Summary.xlsx".
[81] *See* U.S. Department of Justice & The Federal Trade Commission, "Vertical Merger Guidelines", June 30, 2020, at pp. pp 3-4. Market shares are squared to calculate HHI which is a measure of market concentration.

facilitates a firm's ability to influence profitability and prices.[82] Higher market shares indicate less opportunity for shippers to benefit from competition and more opportunity for CPKC to impair competition.

Beyond the market share analysis presented above, Dr. Majure could have conducted additional analyses of the competitive circumstances arising from the Proposed Transaction, particularly since the Proposed Transaction would be the first major restructuring of the North American railroad network since 1999.[83] Specifically, Dr. Majure should have analyzed potential CPKC pricing and profit strategies that could impair competition due to the vertical integration of the combined companies and the expansive network locations that were not integrated prior to the Transaction; i.e., whether the Transaction combines KCS/KCSM incentives with CP's ability to influence the market. This is an approach Dr. Majure discussed when {{ }} and presumably he would have considered such an analysis if evaluating the Transaction for the DOJ.[84] However, Dr. Majure provides no such discussion or analysis. Instead of conducting an applied economic analysis, Dr. Majure defers to a theoretical assumed outcome indicating that regardless of whether shippers face all, some, or no competition (i.e., regardless of how large the lump is) a vertical transaction is "not likely to suffer any incremental adverse effects."[85] He ignored the unique aspects of the combined CP and KCS networks regarding Mexico access and traffic flows that require a closer look.

The combined CPKC would have a unique economic opportunity and incentive to implement a pricing strategy that could harm shippers today and tomorrow which was not achievable pre-

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[82] *See* Scherer, F.M., and Ross, David, "Industrial Market Structure and Economic Performance", Third Edition, pp. 70-73, 428-429. Claims of monopolization in antitrust enforcement cases often have market shares in excess of 60%. *See* Swanson, Parker, Hungar, Richman and Ordover, "Is It Bad to Be Big: An Antitrust Update on Monopoly Law and Enforcement", Gibson Dunn, May 23, 2019 at 12-13.

[83] *See Canadian National, et al.-Control-Illinois Central, et al.*, 4 S.T.B. 122 (1999).

[84] Majure CN V.S. pp. 17-20. Dr. Majure acknowledged in deposition that his conclusions were based on theory that do not include documentary evidence, shipper- specific evaluations, or empirical analysis of the extent to which other rail or nonrail options are exerting competitive pressure on KCS and KCSM. Majure Dep. Tr. 70:5-14; 71:12-24; 84:11-24; and 88:6-15. For an illustrative example of an empirical analysis *see* Shapiro, Carl, "Vertical Mergers and Input Foreclosure Lessons from the AT&T/Time Warner Case", Review of Industrial Organization (2021) 59:303–341 and Majure Dep. Tr. 90:20-25. *See also* Scherer, F.M., and Ross, David, "Industrial Market Structure and Economic Performance", Third Edition, pp. 524-7.

[85] Majure V.S. ¶ 24-26. Dr. Majure points to numerous references to prior STB decisions, which are highly focused on coal transportation, which is not the product at issue for potential vertical effects of this Transaction. {{ }}

transaction.[86] CP's network serves many locations with movements to and from Mexico (i.e., that are either upstream or downstream of the U.S./Canada portion of the movements), as shown in Figure 4 below. The Figure shows the total railroad revenue by location for movements to and from Mexico, and can be used to analyze where the combined CPKC may have additional ability to influence routing as compared to the current KCS/KCSM network's incentives. For example, there will be no additional routing incentives on CPKC as compared to KCS for moves to Houston, while the new entity may wish to exert more control over moves to and from Chicago.

Figure 4: Combined CP-KCS Network Map and 2019 Revenues for Mexico Movements[87]

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[87] *See* Carey HC-WP "-CP and KCS Mexico Traffic Access.xlsx" and Carey HC-WP "CPKC Network Maps.png".

In addition, the combined CPKCS has more complete market and shipper knowledge and information than was available to each entity prior to the Transaction and is therefore more capable of strategic behavior to influence prices and competition. For example, CPKC will have cost information for the proposed downstream segment that will be vertically integrated (the two downstream segments include south into Mexico and north into the Midwest U.S./Canada). In addition, CPKC will have a much wider array of shipper specific information regarding, rates and terms as well as operational information unavailable without the Proposed Transaction. Meanwhile, KCSM maintains substantial market power in Mexico that was not vertically integrated with CP before the Transaction. As Figure 4 shows, the voluminous traffic between points in Mexico served directly Mexico and locations on CPKC locations (including large revenue on former CP locations) requires that the Board carefully assess and assure protection against the potential adverse vertical competition effects from the Proposed Transaction due to KCS's substantial market share of U.S.-Mexico cross-border traffic to and from points served by KCSM.[88]

Today KCSM must cooperate with UP to move traffic for customer locations north of KCS's network that both CP and UP can access (e.g. Chicago). However, CPKC need not cooperate with UP in the future for all of the gateways over which CPKC interchanges traffic between Mexico and the U.S. and Canada. Instead, CPKC will have an incentive to adopt a pricing strategy to foreclose competing railroad alternatives for the U.S. portion of the movement, such as UP (Laredo to Chicago) in order to serve customer locations on CP's network that were not available on the same network system pre-Transaction. As an example, consider traffic that KCSM moves to or from the Laredo gateway and interchanges with a competitor for delivery to or from locations accessible by CP's network (locations not available on a single line to either Applicant prior to the Transaction). CPKC could increase the KCSM rates to the targeted, newly accessible single-line destinations and origins (up to the allowed price caps in Mexico),[89] including for intermodal and automotive traffic. This strategy would substantially increase the revenues associated with the portion of the movement in Mexico.[90] Simultaneously, CPKC could reduce the rates for the U.S. portion of the movement (currently on a competitor) below the URCS variable cost estimate for traffic it can now serve with

[88] *See* Carey HC-WP "HC-Mexico.pdf". Specifically, automotive and intermodal traffic should be areas of particular investigation due to their importance to the Applicants' estimated diversions. *See* "8 – Diversion Identification.xlsx", Brown and Zebrowski V.S. *See* "FD 36500 – Work Paper – HC – Growth Initiative Calculations.xlsx", Wahba and Naatz V.S.

[89] *See* OECD (2017), Review of the Regulation of Freight Transport in Mexico, p.84-86, available at https://www.oecd.org/centrodemexico/publicaciones/OECD%20(2017)%20Review%20of%20%20Regulation%20Freight%20Transport.pdf; Art. 46 of LRSF available at https://www.diputados.gob.mx/LeyesBiblio/pdf/209_061120.pdf. *See* Carey HC-WP "HC-Mexico.pdf".

[90] KCSM and UP separately quote the customer confidential rates for the service each railroad provides.

the combined CPKC system.[91] The net effect of these changes would increase shipper costs for the use of competitor railroads but would hold costs constant for the use of CPKC (enticing shippers to shift to CPKC instead of the now higher cost competitive alternative).

As a result of the Proposed Transaction, the combined company would have the potential incentive and ability to influence prices and competition through the vertical integration of KCSM, KCS and CP and the combined network that extends from southern Mexico through the Midwestern US into Canada. This type of pricing strategy would be profitable for CPKC and could economically foreclose alternative railroad services from competing with CPKC for the Mexico traffic by leaving the competitor with little or no opportunity to add and contribute to its system.[92] There may be other profitable pricing strategies available to CPKC as well as related service disrupting impediments that could negatively impact competitor railroads (i.e., slower interchange).

C. Recommended Conditions

Substantial current and future cross-border rail traffic with Mexico is expected through the Laredo Gateway and it is important for the overall efficiency of the North American railroad network to ensure that traffic movements involving Mexico maintain the most economically efficient routing, consistent with the public interest. Taken together, economic analysis demonstrates that the multitude of locations not available to KCS/KCSM prior to the Proposed Transaction provide CPKC with the potential ability to adversely affect competition related to Mexico which are best addressed through conditions to be set by the STB that ensure that the Laredo gateway and all gateways used for traffic movements to and from Mexico remain open both in terms of commercially reasonable rates and service for rivals (such that competition is not distorted). The STB should also allow shippers to challenge rates and service for all segments of cross border movements and secure remedies that, absent conditions would not be available because of limits on STB jurisdiction.

These condition to ensure that the Laredo Gateway remain open both in terms of commercially reasonable rates and service should apply to all gateways used for traffic movements to and from Mexico because the significant amount of traffic involves a wide array of customer

[91] This analysis assumes that CPKC variable costs are approximately equal to its competitors. However, the analysis estimates that CPKC pricing strategy would still be successful even with 5% lower variable costs. This means that even if competitors' cost were lower, the pricing strategy would still be productive. Furthermore, this analysis is conservative because it includes Applicants' cost estimates that do not include additional line specific costs such as haulage and trackage (as is comparable to a railroad that owns the trackage being operated). *See* Carey HCWP "HC-Mexico Rate Foreclosure by Line of Business.xlsx"

[92] *See* Carey HC-WP "HC-Mexico Rate Foreclosure by Line of Business.xlsx".

locations throughout the midwestern and eastern U.S. and Canada, and beyond. Shippers in these diverse customer locations are potentially impacted from any anticompetitive behavior involving Mexico. Therefore, all gateways used for traffic movements to and from Mexico are potentially affected and require protection to ensure that shippers to and from Mexico and the U.S. are assured the opportunity for competition on commercially reasonable terms (and service) with CPKC.

The STB should also allow shippers to challenge rates and service for all segments of cross border movements and secure remedies that, absent conditions would not be available because of limits on STB jurisdiction.

III. APPLICANTS' LIMITED AND AMBIGUOUS COMMITMENTS TO KEEP "AFFECTED" GATEWAYS COMMERCIALLY OPEN

There are many impacted gateways where CPKC will interchange traffic with other railroads with substantial potential impact to shippers. In its Application, CPKC's commitments regarding gateways was expressly limited to "affected gateways," which are not clearly identified.[93] Adding further confusion, the Applicants' executives simply stated their verbal commitment to keep existing gateways open.[94] There was no identified list of affected gateways in the Application. Witness Brooks identified numerous gateways in his V.S.:

> "Though I have used Kansas City as an example, the same basic truths would be repeated for all of the other gateways where CP and KCS connect with other Class I railroads today. CPKC will continue to have strong incentives to work with our interline partners on efficient joint-line services at the gateways where CP connects today – most notably, at Kingsgate/Eastport (with UP); Coutts, AB (with BNSF); Emerson, MB/Noyes, MN (with BNSF); St. Paul (with BNSF and UP); Chicago (with BNSF, UP, and CN, as well as NS and CSX); and Kansas City (with UP and BNSF). Our incentives will be no less strong at the gateways where KCS connects with other carriers today, such as Laredo (with UP); Robstown, TX (with BNSF); New Orleans, LA (with BNSF, UP, CSX, NS, and CN); Shreveport, LA (with UP and BNSF); Jackson, MS (with CN); Meridian, MS (with NS); and Kansas City (with UP and BNSF). These aren't the only interchanges we will have an incentive to keep open in order to serve our customers well, but they account for the vast majority of all

[93] "Applicants' commitments to keep these and other affected gateways open both physically and commercially will assure that Applicants' incentives are backed up by the potential for enforcement under the auspices of Board oversight." App. Vol 1. P. 11-12

[94] Creel "In light of these incentives, it gives me no qualms to formally commit to the Board that CP/KCS will keep open all existing gateways on commercially reasonable terms, and that we will not create any new "bottlenecks" that might constrain shippers' existing access to the Board's regulatory processes." App. Vol. 1. P. 169 (Creel V.S. p. 14)

Ottensmeyer "This transaction is about growing our business by providing our customers the choice to use the combined network of CP and KCS in a single-line move or to continue with existing routes and interchanges (CP and KCS are committed to keeping existing gateways open on commercially reasonable terms)." App. Vol. 1. P. 191 (Ottensmeyer V.S. p. 5)

of CP and KCS's existing interline traffic to/from the United States that might conceivably be affected by the CP/KCS combination."[95]

This ambiguity raises additional concerns regarding the need to ensure that traffic movements involving CPKC can move over the most economically efficient routes, consistent with the public interest. Shippers must be assured of the opportunity for competition on commercially reasonable terms (and service) with CPKC for all gateways. As discussed above, the general and non-specific commitments offered by CP lack reliable guarantees.[96] While CP commits to working with shippers it does not promise concrete standards that would ensure that CP (1) sets commercially reasonable rates (and does not directly or indirectly raise rivals' costs); and (2) provides service on a non-discriminatory basis, with no service-related distortions involving rival railroads.[97]

IV. THE PROPOSED TRANSACTION OFFERS FEW PUBLIC BENEFITS: APPLICANTS' CLAIMED PUBLIC BENEFITS ARE OVERSTATED AND MOST ARE ONLY PRIVATE BENEFITS

A. Applicants' Claimed Public Benefits are Primarily Potential Private Benefits to the Combined CP and KCS railroads

The Applicants have claimed that the Proposed Transaction will cause substantial "merger benefits" equal to $888.4 million in what Applicants call a normal year and $1 billion dollars indexed to 2025.[98] However, upon inspection, as shown below, the Application reports mostly private benefits (approximately 81% of the total benefits) which Applicants characterize as "Operating Revenue Gains (Net Revenue Gains)" or incremental profits.[99] In addition, Applicants have not

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[95] Brooks V.S. ¶ 41

[96] {{ [redacted] *See also* Brooks V.S. ¶ 42-46. }}

Applicants also estimate one-time Transaction Benefits of less than $100 million over 3 years ($58.9, $23 and $18.1 million). *See* Application, App. Vol. 1, p. 74 (Appendix B, p. 1). Applicants identify $275 million in necessary investments. *See* Public Version of Application, App. Vol. 1, p. 23. *See* also Creel V.S., p. 14, P 33.

[99] Public Version of Application, Baranowski V.S., p. 26 at Table 16 (App. Vol. 1, p. 427) titled as "Summary of CP/KCS Merger Benefits". Table 16 provides for Year 3 (2025) the "Diverted Carloads/Units" as 509,490, the "Incremental Revenues" as $1,021.9 million, the "Total Incremental Costs" as $306.3 million, and the "Net Merger Benefits" as $715.6 million.

identified the potential public benefits to accrue to the U.S. as compared to Mexico or Canada, which should be required in the context of a U.S. public interest determination by a U.S. regulator. In the following discussion, I assume the accuracy of the so called "Operating Benefits" stated by the Applicants. To the extent that the "Operating Benefits" are not realized by the Applicants, then the Applicants' claimed benefits will be further reduced.

Figure 5: Applicants' "Merger Benefits" Consist of Mostly of Potential Private Benefits[100]

Line	Description in Application	Calculation	Normal Year	Indexed to 2025 Normal Year
1	Operating Revenue Gains (Net Revenue Gains)		$715.6 [1]	$805.8 [1]
2	Operating Benefits		$172.8 [1]	$194.6 [1]
3	Total Merger Benefits	Line 1 + Line 2	$888.4 [1]	$1,000.4 [1]
4	Operating Revenue Gains Relative to Total Merger Benefits by Claimed by Applicant	Line 1 / Line 3	81%	81%

Notes and Sources:

1 Public Version of Application, App. Vol. 1, p. 74 (Appendix B, p. 1).

While Applicants claim the "Total Merger Benefits" are quantified as consistent with the "Public Interest Justification" (as per the section title) the benefits asserted by Applicants to be "public" do not fit in the definition of public benefits established by the Board. Specifically, the STB describes public benefits as those achievable through efficiency gains that create lower costs and service improvements.[101] Lower costs are considered public benefits because the railroad service is being provided at the same service level using fewer resources or the service level is higher using the same level of resources.[102] Lower costs can occur in areas such as reduced overhead, elimination of duplicate facilities, and more efficient movement of traffic between the merging parties.[103] The impact of lower costs can be passed to shippers through reduced rates and/or improved services.[104]

[100] *See* Carey HC-WP "HC-Transaction Benefits.xls."

[101] Decision, 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. 44, August 6, 1996, 1 STB 233 (1996), at 363.

[102] Ibid.

[103] Ibid.

[104] Ibid.

In response to CSXT's interrogatories seeking Applicants' support for its assumed definition of public benefits (which its claimed benefits include 81% potential private benefits to accrue solely to Applicants), {{[redacted].}}[106]

The STB decided that the Proposed Transaction will follow the prior regulatory standards for approval, which may have been decided with consideration of the competition standard to use (and not with respect to the benefits).[107, 108] The prior regulatory standard only included a description of benefits that was general in nature. However, the STB's determinations with the prior regulatory standard relied only on quantified public benefits that excluded private benefits for the transaction described below in **Figure 6**.[109] The current standard on public benefits clarifies and builds upon the more generally described regulatory standard that was previously in effect. More recently, the STB has reaffirmed the importance of accurate information with respect to public benefits when

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[105] Applicants' Reponses to CSX Transportation's Second Set of Discovery Requests and Interrogatories, February 18, 2022, No. 62.

[106] Applicants' Reponses to CSX Transportation's Second Set of Discovery Requests and Interrogatories, February 18, 2022, No. 61a, pp 103-104. Response: [redacted]}

Code of Federal Regulations Title 49 at part 1180, subpart A (2000), available at https://www.govinfo.gov/content/pkg/CFR-2000-title49-vol6/pdf/CFR-2000-title49-vol6-part1180-id615.pdf .

[108] Decision, Canadian Pacific Railway Limited; Canadian Pacific Railway Company; Soo Line Railroad Company; Central Maine & Quebec Railway US Inc; Dakota, Minnesota & Eastern Railroad Corporation; and Delaware & Hudson Railway Company, Inc. – Control – Kansas City Southern; The Kansas City Southern Railway Company; Gateway Eastern Railway Company; and The Texas Mexican Railway Company, Docket No. FD 36500, Decision No. 4, April 23, 2021, available at https://dcms-external.s3.amazonaws.com/DCMS_External_PROD/1619216719308/50743.pdf; "Accordingly, review of this Transaction will be governed by the regulations contained in 49 C.F.R. part 1180, subpart A in effect before July 11, 2001", Decision at p. 2. "This transaction is subject to the regulations set forth at 49 C.F.R. part 1180 (2000)," Decision at p. 3.

[109] It is possible that the STB qualitatively considered the private benefits. Decision, 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. 44, August 6, 1996, 1 STB 233 (1996), at 363-364, 375-384. Decision, CSX Corporation and CSX Transportation, Inc., Norfolk Southern Corporation and Norfolk Southern Railway Corporation and Norfolk Southern Railway Company – Control and Operating Leases/Agreements – Conrail Inc and Consolidated Rail Corporation, Finance Docket No. 33388, Decision No. 89, 3 STB 196 (1998), at 333-341. Decision, Canadian National Railway Company, Grand Truck Corporation, and Grand Trunk Western Railroad Inc., - Control – Illinois Central Corporation, Illinois Central Railroad Company, Chicago, Central & Pacific Railroad Company, and Cedar River Railroad Company, Finance Docket No. 33556, Decision No. 37, May 21, 1999, pp. 45-49.

considering a Transaction.[110] The regulatory guidance developed regarding "Public interest considerations" is described in more detail in the current standards[111]and is a helpful guide to follow for this Transaction.[112]

The STB's regulatory guidance since 1996 clarifies that Applicants' private benefits, comprised of potential incremental profits which accrue solely to Applicants from traffic diversions from competitors, is not a public benefit from an economic perspective.[113] Traffic increases due to a transaction are simply shifting revenue from one industry railroad carrier to another.[114] They may or may not reflect any cost savings from reduced overhead costs, or reduced rates, or service improvements to shippers associated with the diverted traffic, and which would flow directly to the customer and therefore are not themselves a public benefit.[115] Accordingly, Applicants' incremental profit estimates from diverted traffic are private benefits to the combined railroad and not public benefits.[116]

To get another perspective on Applicants' claimed benefits, I compared the percentage of private benefits to total benefits for several other historical Major Transactions approved by the Board and the same percentage derived from Applicants claimed benefits. As shown in **Figure 6** below, Applicants' predicted private benefits that accrue solely to Applicants are an unusually high share (81%) of potential claimed total benefits. That percentage is between roughly 2 and 5 times higher than for the prior large railroad transactions, which ranged between 16% and 38%.[117]

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[110] "…it is important that we carefully calculate the net public benefits a merger would generate, and, to do so, the applicants must provide detailed and accurate data." Decision, Major Rail Consolidation Procedures, Ex Parte No. 582 (Sub-No. 1), June 11, 2001, p. 58.

[111]49 CFR 1180.1(c) (2020). *See also* eCFR (Electronic Code of Federal Regulations), available at https://www.ecfr.gov/current/title-49/subtitle-B/chapter-X/subchapter-B/part-1180; *see also* 49 CFR 1180.1(c) (2020) eCFR (Electronic Code of Federal Regulations), available at https://www.ecfr.gov/current/title-49/subtitle-B/chapter-X/subchapter-B/part-1180

[112] Decision, Major Rail Consolidation Procedures, Ex Parte No. 582 (Sub-No. 1), June 11, 2001, pp. 57-58.

[113] 1 STB 233 (1996), at 375-376, 379-380.

[114] 1 STB 233 (1996), at 380.

[115] 1 STB 233 (1996), at 380.

[116] The Public Version of the Application at Appendix B has a table title "Summary of Benefits", which has a "Benefit Component" category of "Operating Revenue Gains". This category has "Revenue Increase from Traffic Gains" minus "Cost of Handling Added Traffic" equaling "Net Revenue Gains". For the Normal Year, the Revenue Increase from Traffic Gains is $1,021.9 million and the Cost of Handling Added Traffic is $306.3 million, which is a Net Revenue Gain[s] of $175.6 million. For the Normal Year Index to 2025, the Revenue Increase from Traffic Gains is $1,150.8 million and the Cost of Handling Added Traffic is $345.0 million, which is a Net Revenue Gain[s] of $805.8 million. Public Version of Application, App. Vol. 1, p. 74 (Appendix B, p. 1).

[117] The dollar amounts presented are when the transactions occurred. Therefore, only the relative ratio statistics can be compared across the transactions and not the dollar amount of the benefit.

Figure 6: Applicants' Private Benefits as a Percentage of Total Benefits Compared to Prior Transactions[118]

Line	Description	Calculation	Incremental Net Revenue as Private Benefits [1] (millions) [a]	Annual Public Benefits [2] (millions) [b]	Annual Total Benefits (millions) [c]	Annual Private Benefits as a Percentage of Annual Total Benefits [a]/[c]= [d]
1	Union Pacific and Southern Pacific		$123.2	$627.4	$750.6	16%
2	CSX and Conrail		$145.9	$505.9	$651.8	22%
3	Norfolk Southern and Conrail		$299.5	$492.3	$791.8	38%
4	Canadian National and Illinois Central		$78.8	$137.4	$216.2	36%
5	Average	Ave (Lines 1 to 4)				28%
6	Normal Year Indexed to 2025		$805.8	$194.6	$1,000.4	81%
7	Normal Year Not Indexed to 2025		$715.6	$172.8	$888.4	81%
8	CP-KCS Transaction Amount Relative to the Average of Large Transactions	Lines 6 or 7 / Line 5				2.8

Notes and Sources:

1 Incremental net revenue for Union Pacific and Southern Pacific is $76 million in net revenues from diverted traffic plus $47 2 million in net trackage rights proceeds from BNSF that the STB determined are not a public benefit

2 Public benefits are cost savings and cost reductions, and does not include incremental net revenue from diverted traffic

For the Major Transactions reported in Figure 6 above, the STB assessed the quantifiable annual benefits associated with each Transactions based on the Public Benefits reported (Column [b]). The STB did not include the private benefits in its formal determination of merger benefits used in its approval. In the UP/SP case, the STB explicitly rejected the private benefits from inclusion in its quantification of public benefits because it was not a cost saving, and therefore implicitly gave it no weight in its evaluation of public benefits attributable to the merger.[119]

A further consideration for the STB's public interest determination is that Applicants have not demonstrated whether their private or public benefits occur in the U.S. (or Mexico or Canada). [120] Applicants' public benefits are not tailored specifically to the U.S. but rather encompass North America and, for example, do not quantify the cost savings or private benefits that are limited to the Board's jurisdiction. Definitionally, ascribing transaction benefits to the U.S. would necessitate some level of reduction of claimed Total Benefits. Applicants acknowledge in discovery responses that

[118] *See* Carey HC-WP "HC-Transaction Benefits.xls".

[119] *See* Decision, 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. 44, August 6, 1996, 1 STB 233 (1996), (1 STB 233 at 375-376)

[120] The Public Version of the Application at Appendix B has a table title "Summary of Benefits", but no information in which countries the benefits occur, App. Vol. 1, p. 74 (Appendix B, p. 1).

non-U.S. benefits are included in their claimed Total Benefits but contend they are appropriate to use.[121] In response to CSXT's interrogatories seeking Applicants' support for its assumed definition of public benefits, Applicants generally state that U.S. shippers benefit, even though they have provided limited details and no specific analysis.[122] Elsewhere in its Application, Applicants indicate that {{ }} of KCS' business is in Mexico and that substantial benefits exist regarding CP's Canadian originations, both of which suggest that any quantifiable analysis would observe a large benefit reduction if the Applicants were to only present the U.S. portion of the Total Benefits.[123] Furthermore, CPKC anticipates the new entity will serve {{)}} instead of a rail move from the U.S. west coast Port of Los Angeles to Chicago (with 100% of the route miles in the U.S.).[124, 125] In these and other examples, there will be some transfer of the potential public or private benefits out of the U.S. into Mexico or Canada. The STB should consider whether the potential public benefits to be

[121] Applicants' Reponses to CSX Transportation's Second Set of Discovery Requests and Interrogatories, February 18, 2022, No. 61 b-f, pp 103-104. {{ }}

Applicants' Reponses to CSX Transportation's Second Set of Discovery Requests and Interrogatories, February 18, 2022, No. 61(b), pp. 60-61. benefits include or reflect }}

Verified Statement of Patrick J. Ottensmeyer, App. Vol. 1, p. 204. "Today, our Mexico franchise represents about half of KCS. Any way you look at us, whether your measure miles, employees, or revenues, KCS is 50% in Mexico." Verified Statement of Patrick J. Ottensmeyer, App. Vol. 1, p. 218. "Similarly, we will provide new single-routes connecting KCS's strong originations of ***automotive shipments from Mexico***, forest products from Mississippi, chemicals from the Gulf, ***perishables from Mexico***, among many others, with destinations reached by CP's, network in the Upper Midwest and Canada." Emphasis added to the original.

[124] A CPKCS movement from Lazaro Caredenas, Mexico to Chicago, IL has 35% of the route miles in Mexico. The total distance is 2,651 miles with 926 miles in Mexico and 1,725 miles in the U.S. Route miles were determined using PC Miler. { }} Route miles determined using PC Miler.

[125] *See* Carey HC-WP "HC-Mexico Mileage WP.xlsx"

used in evaluating the Proposed Transaction should only reflect benefits realized in the U.S. and if so, what further reduction to the Applicants' claimed public benefits will be required.

B. The Application Overstates Incremental Profits from Traffic Diversions

The Applicants' Total Benefits estimated for the Proposed Transaction include 81% potential private benefits that will accrue solely to CPKC. These asserted transaction benefits associated with substantial incremental profit forecast by CPKC traffic diversions sum to $715.6 million. Applicants' estimated private benefits include three categories of traffic diversions: rail to rail diversions carloads, growth initiative traffic, and truck to rail diversions, as shown in Figure 7.[126]

Figure 7: Summary of Applicant's Private Benefits Estimates by Category[127]
(dollar amounts are in millions)

	Applicants Claims			
	Rail to Rail	**Truck to Rail**	**Growth Initiative**	**Total**
Diverted Carloads/Units	216,675	63,644	229,171	509,490
Incremental Revenues	$513.1M	$97.5M	$411.4M	$1021.9M
Incremental Costs	$129.1M	$20.7M	$156.6M	$306.3M
Incremental Profits	$384.0M	$76.8M	$254.8M	$715.6M

Applicants' assumptions are flawed in numerous material ways and raise concerns regarding the reliability of traffic diversions and the underlying assumptions. The plausibility of these assumptions require review even if the Board follows its prior decisions and segregates these private benefits from public benefits. The accuracy of these assumptions bears on the Board's mandated consideration of competitive effects and fixed charges competition and fixed costs even if the Board though STB did not rely on these private benefits for its quantifiable annual benefits its determination of public benefits associated with Major Transactions.

First, Applicants' expected incremental profits assume substantial traffic diversions away from competitor railroads, trucks, or other growth initiative traffic[128] despite offering many longer,

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[126] Applicants' traffic diversions are sponsored by three witnesses, including rail-to-rail diversion (Brown/Zebrowski), truck-to-rail diversions (Mutén) and other growth initiative volumes (Wabba and Nanttz). Brown & Zebrowski V.S. ¶ 5; Mutén V.S. ¶ 6; Wahba & Naatz V.S ¶ 10. *See* Brown and Zebrowski WP "8 - Diversion Identification.xlsx"; *see* Muten WP "FD 36500 – Work Paper – HC – Truck to Intermodal Diversion Estimate w Perishable Double Counts.xlsx"; *see* Wabba and Naatz WP "FD 36500 – Work Paper – HC – Growth Initiative Calculations.xlsx". The Applicants' testimony did specifically discuss the quantum of traffic associated with the "Growth Initiative" or even indicate that these witnesses were sponsoring specific assumptions included in the Applicants' public benefits estimates.

[127] *See* Carey HC-WP "HC-Summary of Corrected Claims.xlsx at tab "Final Table". The source data is Work Paper – HC – URCS Phase III Calculation For Growth Traffic.xlsx", Verified Statement of Michael Baranowski.

[128] *See* Carey HC-WP "HC-Rail Truck Diversions.pdf"

disadvantaged routes. Applicants fail to demonstrate how CPKC will accomplish diversion on new single line routes that face superior, shorter and efficient interline routes from competitive railroads with no rate reduction.[129] As an example, CPKCS's Laredo to Chicago route has a more circuitous, longer distance route than UP's.[130] Nearly {{ }} of the Applicants' traffic diversions involve long haul railroad movements between Mexico and the {{ }}.[131] Applicants' traffic diversions involving Mexico include all three categories of traffic diversions presented by Applicants (rail-to-rail, truck-to-rail and growth initiative).[132] As another example, Applicants rely on many diversions of movements involving the {{ }}. However, the CPKC route is not a straight line between cities, but requires the combination of a longer east-west and north-south route move that takes the shape of an "S" instead of diagonal line.[133]

The Applicants' just make assumptions regarding assignments to apply what traffic will be diverted.[134] This approach is inconsistent with that relied upon in Applicants' normal course of business communications prior to the announcement of the Proposed Transaction. CP's responsible personnel acknowledged .}} The assumed traffic diversions claimed lack economic analysis of price-based competition, unique factors regarding the competitive dynamics of specific lanes, or current economic circumstances, all of which are needed to determine whether the Applicants' route can effectively compete with the existing competitors and their network and economic advantages. Applicants' traffic diversions are developed in a vacuum and do not anticipate responses of other carriers while assuming no rate reductions are needed to acquire traffic diversions on most lanes, eventually cumulating to a monumental level of total

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[129] Applicants acknowledge that the diversion opportunity routes are on average 200 miles longer than existing routes. Brown and Zebrowski V.S., ¶31-34 and Table 7.

[130] Applicants acknowledge that its route from Chicago to Laredo would be longer than UP's more direct route. Wahba and Naatz V.S. ¶48.

[131] { } out of 509,490 units. When considering all diversions to all destinations and origins, over {{ }} of diversion units involve routes which include Mexico. *See* Carey HC-WP "HC-Mexico Diversion Claims.xlsm."

[132] Applicants' truck to rail diversions from Minneapolis, MN, Detroit, MI and Columbus, OH to Dallas, TX or Mexico that covers a longer route on CP/KCS compared to a more direct route on UP also require use of another carrier's rail facilities (trackage or haulage), which adds costs and further disadvantage the traffic.

[133] Brown & Zebrowski V.S ¶ 49; Mutén V.S Appendix A; Wahba & Naatz V.S ¶ 52. Dallas to Chicago is the primary route for which Applicants propose a rate decrease. *See* Brown & Zebrowski V.S. ¶ 32.

[134] Brown and Zebrowski V.S., ¶34 and Table 7. The starting assumptions are in Table 7, which is titled "Starting Point Diversion Rules for Traffic Susceptible to Diversion." The starting diversion rules are based on limited regression studies in Brown and Zebrowski V.S., Appendix B: "…our diversion estimates considered further individualized factors that led us to apply adjustments that affected these percentages."

potential private benefits as compared to the combination of UP/SP and BN/SF.[135] This is implausible.

Second, Applicants include many traffic movements achievable without the Proposed Transaction. For example, Applicants' incremental profits attributed to the Transaction assume substantial traffic diversions that remain on either CP or KCS's individual networks. Applicants include traffic movements between Mexico and Texas or Kansas City that could be provided today solely by KCS as an independent entity.[136] Applicants also include traffic movements between Canada and Kansas City that could be provided today solely by CP as an independent entity.[137] Applicants also include substantial diversions of crude by rail (DRUbit[138]) movements from Alberta to Texas in the Growth Initiative traffic, however this was likely a business goal without the proposed Transaction and CP already maintains a strong market position regarding this traffic.[139] Even CP's internal investor documents do not indicate this traffic is only achievable as a result of the Proposed Transaction (rather suggesting it is more likely than without the Transaction).[140] CP does not claim that DRUbit is not achievable without the Transaction or that railroads face substantial competition from low cost pipelines.[141]

Third, additional questions arise as to what traffic movements are appropriately identified as resulting from the Transaction. The Growth Initiative volumes may duplicate business forecasts for the company.[142] For example, if CP or KCS include volumes in their individual company business forecasts, then it is not appropriate to attribute that traffic diversion as resulting from the Transaction.

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[135] *See* Brown and Zebrowski HC WP "HC – 8 - Diversion Identification.xlsx"

[136] *See* Carey HC-WP "HC-Growth Initiative.pdf" and Carey HC-WP "HC-Rail and Truck Diversion.pdf." { [redacted] } *See* Applicants Responses to CSXT's Second Set of Discovery and Interrogatory Requests, February 18, 2022, No. [8].

[137] *See* Carey HC-WP "HC-Growth Initiative.pdf" and Carey HC-WP "HC-Rail and Truck Diversion.pdf."

[138] DRUbit refers to the approach that relies on a Diluent Recovery Unit to remove some of the light hydrocarbons (diluent) for rai transportation of more concentrated oil products. *See* USD Group, "Diluent Recovery Unit, AB, CA", available at https://usdg.com/terminal/dru/#:~:text=DRUbit%E2%84%A2%20is%20crude%20oil,Gulf%20Coast%20and%20in%20other

[139] Wahba and Naatz V.S. ¶84-94. The Applicants assert this traffic volume will be created in the future since "[w]e anticipate that CP/KCS will be the catalyst for further investments in the Hardisty DRU facility to expand its capacity." Wahba and Naatz V.S., ¶92. { [redacted] } *See* Carey HC-WP "HC-Growth Initiative.pdf".

[142] *See* Applicants Responses to CSXT's Second Set of Discovery and Interrogatory Requests, February 18, 2022, No. 1-7. {{ [redacted] }}

The Growth Initiative traffic diversions are more suspect because they don't identify the specific pre-Transaction Origin/Destination movement it proposes to displace and lack supporting analyses. For example, Growth Initiative traffic diversions include substantial new intermodal traffic from the Port of Lazaro Cardenas on the west coast of Mexico that CPKCS appear to claim it will divert traffic from Los Angeles area ports. [143] The idea that organic growth was not considered separately from transaction-specific growth appears to be supported by deposition testimony of Applicants' witnesses.[144]

Applicants provide no analyses of the rates or distances or other aspects of the railroad movements from different ports (or even the waterborne movement to each port from Asia or other origin locations). Applicants indicate that KCS's only has "…very small volumes of shipments from Port of Lazaro Cardenas) that reach as far as Houston (Kendleton)," which uses KCS's trackage rights agreement with UP.[145] However, KCS has advised its investors that KCS considers Texas as the important destination for movements from Mexico ports (which they call the Texas Shortcut).[146] Lastly, Applicants also appear not to consider in the Application certain challenges of operating in Mexico and the Port of Lazaro Cardenas.[147]

Fourth, Applicants contend these large traffic diversions do not require a rate reduction in most instances. As a threshold point, the Applicants' estimated rates for all traffic diversions include the current CP or KCS prior rates for specific segments plus an estimate of another carriers' rates. There is no economic analysis to support whether the Applicants' estimated rates for traffic

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[143] Wahba and Naatz V.S. ¶ 57, 60-66.

[144] {{ [redacted] }}
Wahba and Naatz V.S., ¶58

[146] "I expect we'd see some interline movements tested in 2022 as an opportunity. It's actually 300 miles shorter to Houston than L.A. So there's absolutely an opportunity to take advantage of what we call the Texas shortcut." - Executive Vice-President and Chief Financial Officer Nadeem Velani, Canadian Pacific, CBIC Western Institutional Investor Conference, January 2022. Transcript available at https://investor.cpr.ca/events/event-details/2022/CIBC-Western-Institutional-Investors-Conference/default.aspx

[147] *See* Carey HC-WP "HC-Mexico.pdf". "KCS has been forced to embargo traffic to and from Mexico's busiest port, the railroad said. No detours are available. The railroad said it was working with state and federal governments to resolve the blockades." "Protests by teachers and other labor groups in Mexico are nothing new: They've been blocking the rail lines of KCS de Mexico and its predecessors periodically for 37 years. The latest round of protests — which have nothing to do with KCS — began on June 11, effectively shutting down rail traffic to and from the Port of Lazaro Cardenas. The protests can have a significant impact on KCS volume and revenue. The port traffic that KCS hauls in stack trains between Lazaro and the Mexico City area represents about a quarter of KCS's overall intermodal volume. Last year protests shut down the line for 59 days from September through Dec. 1. Intermodal volume from Lazaro fell to 5,800 containers in the fourth quarter, down from 47,700 a year earlier. The impact of the protest has lingered into this year as shippers have been slow to return to KCS between Lazaro and Mexico City and instead are relying on trucks, executives have said." *See* Bill Stephens, "Civil protests once again block KCS de Mexico main line to busy port", Trains, June 17, 2021, available at https://www.trains.com/trn/news-reviews/news-wire/civil-protests-once-again-block-kcs-de-mexico-main-line-to-busy-port/

diversions approximate any competitor's single line rate (or the lowest rate in the market) and indeed to the extent that CP and KC are not competitive with other carriers today, their rate may be higher than competitors' rates. Reliance on masked CWS rates and revenue could further overstate the estimated rate CPKC would receive in their hypothetical diversion. Further, Applicants' approach assumes a 5% rate discount where the CPKC will face single-line competitor railroads. Applicants exclude the majority of traffic movements that involve Mexico, approximately {[redacted]}} of all diversions.[148] Dallas to Chicago is the primary route for which Applicants propose a rate decrease. As discussed above, this CPKC route would face substantial competition and has much longer distances and more challenging terrain than competing routes. The Applicants lack necessary economic rigor to confirm the sufficiency of a 5% rate reduction to divert the traffic.[149] In discovery responses, Applicants confirmed that intermodal movements between Dallas and Chicago comprise {[redacted]}} of all Diversions the Applicants assume will result from a 5% rate reduction.[150]

Fifth, the Applicants do not include all the unique costs associated with the traffic movements assumed to be diverted or the full array of necessary investments. Applicants rely on an estimate of system average costs from URCS instead of lane specific costs. The economic costs need to account for the additional costs associated with haulage agreements or trackage agreements that would reduce the assumed incremental profit from the diverted traffic involving the numerous applicable segments where CP or KC have haulage or trackage rights).[151, 152] Further, the Applicants' cost analysis also relied on a highly efficient blocking and organization of operating trains developed in the Operating Plan, however the operating plan does not consider block swapping that occurred outside of a yard "processed" car.[153] Therefore, to the extent that block swapping activities which

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[148] "All else equal, assuming another railroad currently priced this traffic at 200% R/VC, CPKCS could offer a 5% rate discount to the shipper and still move the traffic at an R/VC level of 175%." Brown and Zebrowski V.S., ¶ 31 footnote 16.

[149] Brown & Zebrowski V.S. ¶ 32.

[150] {{[redacted]}}

[151] Baranowski V.S. ¶16-22. The Applicants rely on the analysis Mr. Baranowski who uses URCS variable costs to create his cost estimates. See "FD 36500 – Work Paper – HC – URCS Phase III Calculation For Growth Traffic.xlsx", Baranowski V.S. However, URCS relies on system average variable cost and does not account for haulage or trackage fees on a given route. For example, in {{[redacted]}}; Baranowski V.S. Table 16. *See* Carey HC-WP "HC-Rail and Truck Diversion.pdf."

[152] Additionally, there is no equivalent of KCSM URCS-like cost estimate, and instead Applicants rely on KCS U.S. URCS to estimate KCSM costs. To the extent these costs are understated, Applicants have overstated the estimated incremental profits from the traffic diversions involving Mexico.

[153] Elphick and Orr Dep. Tr. 49-50 and 217-218.

occur on the mainline are not accounted for in the Operating plan, they could add to expected cost and decrease service quality. Finally, Applicants may have also failed to account for the full costs of maintaining their operations in Mexico by not disclosing the costs of investing in additional railcars and containers needed for the assumed traffic growth.[154]

In total, excluding the substantial amount of traffic diversions associated with the longer, disadvantaged routes which Applicants have not shown to be capable of sustaining competition (with no "hard analysis" of CPKC competitiveness compared to UP or BNSF[155] and excluding those traffic movements demonstrably achievable without the Transaction, dramatically reduces Applicants' estimated incremental net profits and private benefits from approximately [redacted]}}, as shown in Figure 8 below.

[154] *See* Carey HC-WP "HC-Public Benefits.pdf"
[155] {{[redacted]}}

Figure 8: Summary of Corrected CPKCS Private Benefits to Exclude Disadvantaged Routes and Traffic Achievable without the Transaction[156]
(dollar amounts are in millions) {{

C. Analysis of Proposed Transaction Benefits and the Purchase Price Indicates that CPKCS has Less Benefits per Dollar Paid as Compared to Other Transactions

To consider whether the Applicants' claimed public benefits are purchased at a high price relative to other historical Transactions accepted before the STB, an analysis was done to compare the Applicants' claimed public benefits (i.e., excluding private benefits) relative to the purchase price to other Transactions of similar size. This analysis may aid the STB in considering the public interest standard and to ensure that Proposed Transactions are not accepted at any high purchase price or low

[156] *See* Carey HC-WP "HC-Summary of Corrected Claims.xlsm" at tab "Final Table"

level of public benefits. While the purchase prices and the quantum of public benefits vary among transactions, the STB can consider public benefits per dollar of the purchase price to evaluate the relative economics of the Transaction.[157] As shown in Figure 9 below, the Applicants' Transaction has about 7% of the annual public benefits relative to the average of the four largest prior Transactions as measured per dollar of purchase price.[158] This indicates that this Transaction has low level of public benefits compared to prior Transactions. The relatively high purchase price implies that there may be an incentive by the Applicants to harm competition if the benefits claimed in the Application are not realized.

Figure 9: Summary of Public Benefits and Purchase Price for Prior Transactions and the Applicants[159]

Line	Description	CP/KCS Transaction	Union Pacific and Southern Pacific	CSX and Conrail	Norfolk Southern and Conrail	Canadian National and Illinois Central
1	Annual Public Benefits (millions) [1]	$194.6	$627.4	$505.9	$492.3	$137.4
2	Purchase Price (millions) [2]	$27,200	$4,100	$4,200	$5,800	$2,400
3	Annual Public Benefits per dollar of Purchase Price [3]	$0.0072	$0.1530	$0.1205	$0.0849	$0.0573
4	Average of 4 Large Transactions	$0.1039				
5	CP/KCS Percentage of Average Large Transactions	6.9%				

Notes and Sources:
1 Annual public benefits excludes the incremental profits, which are private benefits
2 Purchase price excludes assumed debt
3 The public benefits relative to the purchase price are contemporaneous amounts to the transaction

The Proposed Transaction would produce far fewer total benefits relative to the purchase price (excluding assumed debt) as compared to transactions of a similar size. The Transaction has total benefits on a per dollar of purchase price (excluding assumed debt) that is approximately 26% of the average for the large railroad transactions shown below in Figure 10.

[157] Standardization of dollar amounts by contemporaneous measures is a standard finance technique. For example, {[redacted]}

[158] The public benefits amounts are those determined or accepted by the STB in those transaction approval decisions.

[159] *See* Carey HC-WP "HC-Transaction Benefits.xls"

Figure 10: Summary of Total Benefits and Purchase Price for Prior Transactions and the Applicants[160]

Line	Description	Calculation	CP/KCS Transaction	Union Pacific and Southern Pacific	CSX and Conrail	Norfolk Southern and Conrail	Canadian National and Illinois Central
1	Annual Total Benefits (millions) [1]		$1,000.4	$750.6	$651.8	$791.8	$216.2
2	Purchase Price (millions) [2]		$27,200	$4,100	$4,200	$5,800	$2,400
3	Annual Total Benefits per dollar of Purchase Price [3]	Line 1 / Line 2	$0.0368	$0.1831	$0.1552	$0.1365	$0.0901
4	Average of 4 Large Transactions [4]	Ave (Line 3 except CP/KCS)	$0.1412				
5	CP/KCS Percentage of Average of Large Transactions [5]	Line 3 / Line 4	26%				
6	Payback Period Based on Purchase Price divided by Annual Total Benefits [6]	Line 2 / Line 1	27.2	5.5	6.4	7.3	11.1
7	Average of 4 Large Transactions [7]	Ave (Line 6 except CP/KCS)	7.6				
8	CP-KCS Transaction Amount Relative to the Average of Large Transactions [8]	Line 6 / Line 7	3.6				

Notes and Sources:
1 Total benefits are the sum of the incremental net revenue as private benefits and the public benefits. CPKCS Transaction annual total benefits are indexed by the Applicants to 2025.
2 Purchase price excludes assumed debt.
3 The public benefits relative to the purchase price are contemporaneous amounts to the transaction.

An alternative view of the annual total benefits and purchase price is to examine the time it will take for the annual total benefits to be equal to the purchase price. This widely accepted financial metric for investment decision making is known as the payback period, which examines nominal cashflow amounts relative to the initial investment.[161] Comparing the Applicants Proposed Transaction payback period of about 27 years with the average for the large transactions of 7.6 years shows the Applicants payback period is over 3 times longer. This suggests there is a lot more risk involved with this Transaction relative to prior large transactions because the asserted transaction benefits will need to occur for a much longer time.

Examining the Applicants' claimed benefits and purchase price relative to prior larger transactions indicates that the Applicants" Proposed Transaction may not be in the public interest. The overstatement of incremental traffic due to diversions strongly suggests that the Applicants transaction is even more anomalous relative to prior large transactions. Also, given that 81% of the Applicants' total benefits are due to net incremental revenue due to diverted traffic, if that incremental revenue does not materialize, then the Applicants could attempt to recover its overall acquisition investment through higher rates on shippers.

[160] *See* Carey HC-WP "HC-Transaction Benefits.xls".
[161] *See* Aswath Damodaran, "Corporate Finance: Theory and Practice", 2nd edition, 2001, at pp. 294-296; Richard A. Brealey, Stewart C. Myers and Franklin Allen, "Principles of Corporate Finance", 8th edition, 2006, at pp. 89-90; Ehsan Nikbakht and A.A. Groppelli, "Finance", Barron's Business Review Books, at p. 169.

D. The High Incremental Debt Incurred for the Proposed Transaction Is Unlikely To Be Offset By Incremental Transaction Benefits Claimed

Applicants identified substantial incremental debt of [redacted]}} associated with the Proposed Transaction. This high level of debt coupled with concerns regarding Applicants' ability to achieve the Claimed Total Benefits (mostly private benefits) should lead the Board to review whether the Applicants' incremental debt[162] incurred for this Proposed Transaction can be supported by the potential additional revenues or costs savings from the Proposed Transaction (excluding the economically unsupported private benefits).

Presentations to the Board of Directors of KCS by both Morgan Stanley and Bank of America Securities (BoA) in September 2021 {{[redacted]}}.[163] {{[redacted]}} for the Proposed Transaction as shown in Figure 11 below.[164] {{[redacted].}} {{[redacted]}}

A few important observations. First, even if all the asserted benefits from the Proposed Transaction materialize, the Applicants are at risk for not achieving enough incremental profits to cover the new debt. Second, as a result, the Board should review whether the Applicants' incremental debt incurred for this Proposed Transaction can be supported by the potential additional revenues or costs savings from the Proposed Transaction, which excludes the economically unsupported private benefits as described in Section IV.B. Third, {{[redacted]}}

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[162] This figure appears to exclude a small amount of annual incremental dividends ($82 million), that if added, would be consistent with the STB's statutory definition of fixed charges (Section 1180.6(a)(2)(iii). *See* Application, App. Vol. 1, p. 22, and Exhibit 18, pp. 7-10; App Vol. 1, pp. 150-153.

[163] {[redacted]}

Figure 11: KCS Investment Bankers' Valuation of Transaction Synergies Compared to Increased Net Debt from the Transaction[166] {{

Figure 12 below, reports the corrected merger benefits for the Applicants by removing the unsupported diversion traffic for longer and disadvantaged routes and traffic movements that are achievable without the Transaction. The corrected merger benefits associated with the Proposed Transaction are just [redacted]}[167] These corrections remove most, but not all of the Applicants' Claimed Private Benefits associated with the Proposed Transaction that the Company will solely receive. In the normal course of business prior to the announcement of the Proposed Transaction, CP's estimated Transaction related synergies were {{[redacted]}} claimed benefits reported in its Application. The CP internal business communication recommendation for estimated CPKC Transaction synergies was equal to [redacted] for 2021-2023. These revenue synergies are similar to the corrected incremental profit estimate equal to [redacted]} than CPKCS' $715 million claimed in its STB Application.[168] In addition, the internal business estimates for operating expense synergies ranging from [redacted]}} to Applicants' claimed $172.8 million.[169] To put the corrected potential private benefits

[166] *See* Carey HC-WP "HC-Value of Transaction Benefits.xls"
[167] 68% = (888-286) / 888)
[168] {{[redacted].}}
[169] Ibid.

that will accrue solely to Applicants of }} into context, {{ }} and it is much higher than the revenue reduction associated with Applicants' assumed 5% rate reduction to limited routes in the traffic diversions, which approximates which will benefit shippers.[170]

Figure 12: Correction to Applicants Claimed Public Benefits (Including Those Properly Categorized as Private Benefits) Using Corrected Diversion Traffic[171]

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The percentage reduction in merger benefits of {{ }} was applied to {{ }} for the Proposed Transaction as shown in Figure 13 below.[172, 173] This figure demonstrates that the {{

[170] Brown & Zebrowski V.S. ¶ 32; Carey HC-WP "HC-CPKC Diversion from Single Line Competition.xlsx". The 5% rate decrease is assumed for Dallas to Chicago route and a few other routes.

[171] *See* Carey HC-WP "HC-Diversion Traffic and Transaction Benefits.xls"

[172] {

}

The actual amount of debt raised to fund the Transaction was about $8.4 billion (US Dollars). Canadian Pacific, Press Release, "CP delivers sold fourth-quarter results; prepared to make history in 2022", January 27, 2022, Financial Information, Note 5 (Debt), available at https://s21.q4cdn.com/736796105/files/doc_financials/2021/q4/Exhibit-99.1-Q4-2021-Earnings-Release.pdf. Canadian dollar proceeds of $2.2 billion for Nov. 24, 2021 debt issuance converted to US dollars using the Bank of Canada Canadian Dollar to US Dollar exchange rate on November 24, 2021 of 1.2677, which was the issue date for the Canadian dollar debt issued by CP. The $2.2 billion in Canadian dollars converts to $1.74 billion US dollars. The Dec. 2, 2021 debt issued of $6.7 billion was in US dollars. The combined US dollar amount for the debt issued is about $8.44 billion. Canadian dollar to US Dollar exchange rates from Bank of Canada, available at https://www.bankofcanada.ca/rates/exchange/daily-exchange-rates-lookup/.

[redacted]}} In sum, the {{[redacted].}}. An important consideration is that the incremental debt raised is an obligation of the combined company, and that if the Applicants' claimed benefits do not materialize then the burden to recover the Applicants' investment in the transaction may affect all existing shippers, including potentially resulting in higher rates.

Figure 13: KCS Investment Bankers' Valuation of Transaction Synergies Adjusted for Unsupported Diversion Traffic Compared to Incremental Debt Raised for the Transaction[174]

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[redacted]

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V. COMPETITIVE ISSUES WITH MERIDIAN SPEEDWAY

A. NSR's Request for Expanded Market Division and Asset Control on the Meridian Speedway and Conditions Necessary to Ameliorate Competitive Concerns

In addition to the issues posed directly by the Application, the following sections assess the potential for the transactions described in NSR's Description of Anticipated Responsive Application[175] to enshrine impaired competition and harm customers in the Eastern U.S. The existing

[174] *See* Carey HC-WP "HC-Value of Transaction Benefits.xls"

[175] See STB Finance Docket No. 36500, Description of Anticipated Responsive Application by Norfolk Southern Railway Company, January 12, 2022.

KCS and Norfolk Southern Railway Company (NSR) Meridian Speedway Agreements create competitive concern and could be aggravated as a result of the Anticipated Responsive Application. I discuss the anticompetitive concerns that arise from the Meridian Speedway's use of an explicit market allocation scheme which divides the control of certain geographic areas and products between KCS and NSR.[176] This type of market division is prohibited by antitrust agencies when it results in adverse vertical effects on competition. However, the agreement was granted an exemption as an intra-corporate transaction in 2006 and therefore the STB did not complete a regulatory review for the agreement's competitive implications, despite the establishment of the Market Division. The KCS/NSR arrangement has provided NSR with exclusive rights over the Speedway and enabled NSR to vertically integrate (economically) across the Meridian Segment to and from its Eastern rail system by granting NSR exclusive right to move traffic (via haulage) between Shreveport and Meridian for transcontinental intermodal traffic originating or terminating West of Dallas and East of Meridian at points not served directly by KCS. That traffic is referred to in the MSLLC Agreements (defined below in Section V.B) as "NS Traffic" and is exclusive to NSR and therefore hereafter referred to as "NSR Exclusivity Traffic"[177] Both NSR's existing exclusive rights and its proposed expansion of those rights raise anticompetitive concerns and distort competition between NSR, KCSR, and CSXT for the NSR Traffic for which the most efficient route is over the Speedway. Additionally, if the Anticipated Responsive Application is approved, I also discuss the need for conditions to remedy these anticompetitive impacts on shippers.

B. Competitive Concerns Arising from the Market Allocation Scheme on the KCS/NSR Meridian Speedway's

KCS and NSR together own a joint venture company called the Meridian Speedway, LLC ("MSLLC"). MSLLC owns the Meridian Speedway, with KCS owning 70% and NSR owning 30%.[178] As NSR recognizes, this asset is a "critical rail line" connecting Meridian, Mississippi and Shreveport, Louisiana which provides an advantaged gateway with distinctive circumstances for NSR intermodal traffic between the Western and Eastern U.S.[179]

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[176] I understand that CPKC plans to address NSR's proposed expansion in their forthcoming filing. I will supplement my analysis and opinions to address the NSR proposal.

[177] {{ [redacted] }}

[179] *See* STB Finance Docket No. 36500, Description of Anticipated Responsive Application by Norfolk Southern Railway Company, January 12, 2022.

I begin with a review of the original agreement and the unique attributes associated with the MSLLC and the absence of sufficient prior economic analyses. KCS sought an exemption for an intra-corporate transaction in which the parties entered a horizontal market division.[180] The request was not presented as a transaction that affected KCS's control of the segment of the Speedway to be owned by the MSLLC joint venture. Further, it did not provide or suggest the need for a competitive effects analysis to consider the potential harm to customers that could arise from the creation of the MSLLC or the other related agreements (together, the "MSLLC Agreements") presented in the Notice of Exemption.[181]

From an economic perspective, the MSLLC agreements encompasses two important components: (1) the market division or allocation scheme that provides exclusivity rights to each owner for distinct types of customers and rail traffic accessed through the Meridian Speedway, which has the economic effect of (2) transferring economic control of the MSLLC for purposes of protecting NSR's exclusive right to move NSR Traffic and {{ }}.[182]

Meridian Speedway Agreements provided NSR with effective ownership and economic control of the portion of the Meridian Speedway dedicated to overhead transcontinental, intermodal traffic between Southwest U.S. (West of Dallas) and Southeast U.S. regions (East of Meridian) which gives rise to competitive concerns.[183, 184] Through the Meridian Speedway Agreements, KCS

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[180] FD No. 34821-23, Decision, April 2006, p.2, available at https://dcms-external.s3.amazonaws.com/MPD/62491/32B24610D6F3FC1D85257148005B37FF/36922.pdf

[181] *See* {{ }}
In competition analyses before energy regulators the economic concept of control is adopted. An academic article discussing the economic aspects of leasing cites the prevailing definition of lease agreements as contracts that "convey the right to control the use of…an identified asset… for a period of time." *See* Merrill, Thomas W., "The Economics of Leasing", Journal of Legal Analysis, The John M. Olin Center for Law, Economics and Business at Harvard Law School, 2020, at 9.

[183] *See* Carey HC-WP "HC-Meridian.pdf" {{ }}

[184] { }

received sole use, and therefore effective exclusivity of the Meridian Speedway, for traffic originating at Dallas or elsewhere.[185, 186] KCS interchanges traffic it moves across the Meridian Speedway with NSR at Meridian, MS.[187]

NSR's newly acquired exclusive transcontinental traffic lane for NSR Traffic includes the Los Angeles port, which is an artery for substantial international trade between the U.S. and important trading partners in the Asia Pacific region. NSR uses the Meridian Speedway to connect Western U.S. traffic with U.S. locations east of Meridian, MS including Atlanta GA, Charlotte, NC, and locations further north.[188]

Further, the Meridian Speedway Agreements stipulate that neither KCS nor MSLLC can compete for the NSR Exclusivity Traffic , nor provide haulage for, or interchange with another carrier to handle this traffic between Shreveport and Meridian.[189] NSR's exclusive control of the specified intermodal traffic carried by the Meridian Speedway does not have a term limit.[190] To facilitate NSR's cross country intermodal business, the Meridian Speedway Agreements provide NSR the ability to interchange traffic at Shreveport with UP[191] for origination and termination in the Southeast U.S. and mid-Atlantic region.[192] The NSR Haulage Agreement and the broader Meridian

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[185] {{ [redacted] }}

[186] "Norfolk Southern will be the sole provider via a haulage agreement of domestic intermodal services on the Shreveport-to-Meridian portion of the Speedway to and from points in the United States west of Fort Worth (including transcontinental traffic originating at West Coast ports) and points east of Meridian. KCS and Norfolk Southern will jointly market local Dallas intermodal traffic to and from Norfolk Southern's network in the East. KCS will handle all other business over the line, including traffic local to the line and the KCS system and traffic to and from Mexico." *See* SEC Archives, "Remarks by Henry C. Wolf", December 2005, available at https://www.sec.gov/Archives/edgar/data/702165/000070216505000255/hcw-remarks1.htm

[187] { [redacted] .}} *See* Carey HC-WP "HC-Transcontinental Meridian Traffic.xls".

[188] *See* NS "Crescent Corridor", available at http://www nscorp.com/content/nscorp/en/shipping-options/corridors/crescent-corridor.html

[189] {{ [redacted] }}

[190] { [redacted] }}

[191] {{ [redacted] .}}

Speedway Agreements provide NSR with substantial operational flexibility to efficiently and effectively interchange and operate over its owned and controlled intermodal traffic.[193] The rates identified in the Meridian Speedway Agreements are reported in the Joint Use Agreement[194] and the Western Haulage Agreement.[195]

Agreements that divide a market into exclusive scopes and/or allocate customers by sellers in an exclusive manner, such as the Meridian Speedway Agreements, are conspiracies that seek to limit price competition and are generally viewed as anticompetitive because they result in a restraint of trade.[196] Antitrust agencies prohibit such understandings or formal agreements that divide or allocate a market, regardless if they are tacit or explicit.[197] Agreements that solely divide markets among competing firms have been considered illegal, with the FTC stating that "[p]lain agreements among competitors to divide sales territories or assign customers are almost always illegal." The FTC views such arrangements as "… essentially agreements not to compete" where parties say "I won't sell in your market if you don't sell in mine.""[198] Only in circumstances where the agreement not to compete is not the primary aspect of the arrangement, described as "ancillary" by the FTC, is the arrangement

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[193] { [redacted] }}

[194] {{ [redacted] }}

[195] { [redacted] }

[196] *See* Scherer, F.M., and Ross, David, "Industrial Market Structure and Economic Performance", Third Edition, pp. 317, 320 and 321. Notably, addressing the consistent court rulings of the unlawful price fixing conspiracies and arrangements, including market division agreements, since the mid-1930's.regardless of whether it was effective or not. *Id. See also* Miles, Jeff. "Principles of Antitrust Law", April 2016, at 67.

[197] *See* Federal Trade Commission, "Market Division or Customer Allocation", available at https://www ftc.gov/tips-advice/competition-guidance/guide-antitrust-laws/dealings-competitors/market-division-or.

[198] Ibid.

not of material concern.[199, 200] However, the market division is the principal competitive effect flowing from the Meridian Speedway Agreements.

Further, types of arrangements that rely on market division and allocations as their main purpose, such as the KCS and NSR Meridian Speedway Agreement, are in the same category of anti-competitive conduct as price-fixing.[201, 202] The FTC's stringent enforcement against such collusive, anticompetitive market allocation schemes has been recognized as an important and positive contribution to the economy.[203] From an economic perspective, collusive practices are recognized to increase profits to participating companies while decreasing output and therefore causing a welfare loss. This contrasts with a competitive equilibrium where consumer welfare is maximized as the result of competitive price and output levels.[204] The substantial economic impact of cartel/collusive behavior is analyzed to be the basis for recommending the establishment or enhancement of antitrust enforcement.[205]

However, whether the horizontal effects of the KCS-NSR market division (which, among other things, ceded a competitive advantage that KCS had for some traffic that NSR might otherwise carry or receive over other gateways) would have passed review by the Board as a pooling arrangement, or a change of control, or review under the antitrust laws is less significant than the fact

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[199] Ibid.

[200] Certain vertical agreements among suppliers and retailers, or wholesalers and distributors, may be considered to enhance efficiencies and have the effect of resolving free-rider problems and promoting intra-brand competition at the retail level by limiting competition among retailers or distributors in downstream markets. E.g., certain instances of resale price maintenance and territorial restrictions. However, such characteristics are not present in the circumstances of the Meridian Speedway as the relevant agreements are horizontal in nature. Two competing firms in the same market have allocated among themselves certain customers and types of services, which thereby eliminates competition for those customers and services entirely. *See* Jarmuth, Jeffrey J., "Horizontal Market-Division Agreements Under the Ancillary Restraints Doctrine", Loyola University Chicago Law Journal, Vol 16, No. 4, 1985 at 775-785; Miles, Jeff. "Principles of Antitrust Law", April 2016, at 73-74; Gelfand, David I. and Bernhardt, Linden, "Vertical Restraints: Evolution from Per Se to Rule of Reason Analysis", ABA Antitrust Section Fall Forum, 2017 at pp. 5-7.

[201] *See* Viscusi, Kip W. et al., "Economics of Regulation and Antitrust", Second Edition, The MIT Press, 1995, at 125.

[202] Market allocation agreements have been considered to cause more competitive harm than other forms of collusive arrangements such as price-fixing. Whereas price-fixing eliminates price competition among companies, market division eliminates all competition among companies. *See* Miles, Jeff. "Principles of Antitrust Law", April 2016, at 66-67.

[203] Kovacic, William E., "Antitrust Policy and Horizontal Collusion in the 21st Century", Loyola Consumer Law Reporter 9, no. 2 (1996-1997): 97-112 at p. 97.

[204] Clarkson, Kenneth W. and Miller, Roger L., "Industrial Organization: Theory, Evidence and Public Policy", McGraw Hill, 1982 at pp. 317-318.

[205] Analysis of the behavior of U.S. firms during periods without effective antitrust enforcement concludes that "the benefits of antitrust enforcement to consumers and social welfare-particularly in deterring the harms from anticompetitive conduct across the economy-appear to be far larger than what the government spends on antitrust enforcement…" *See* Baker, Jonathan, "The Case for Antitrust Enforcement", Journal of Economic Perspectives, Vol. 17, No. 4 Fall 2003.

the arrangements creating NSR's exclusivity of asset control and market division scheme (also referred to as a market allocation) has never been subjected to a competition review and the arrangements have vertical effects that are patently anticompetitive.

NSR's exclusive right to handle intermodal traffic over the MSLLC track today, as well as its proposed expansion (more products and broader geographic scope) are anticompetitive and distort competition between NSR, KCSR, and CSXT for NSR Traffic for which the most efficient route is over the Speedway, and therefore impacts railroad markets East of Shreveport.[206] The MSLLC Agreements enabled NSR to vertically integrate (economically) across the MSLLC Line into its Eastern rail system (through elimination of KCS's right to haul NSR Exclusivity Traffic).

NSR participates in the handling of the majority of the traffic over the Meridian Speedway. NSR is responsible for {{ }} carloads of transcontinental intermodal traffic over the Meridian Speedway (i.e., NSR Exclusivity Traffic). NSR also receives or delivers in interchange with KCS at Meridian {{ }} cars of other traffic types carried over the Meridian Speedway. Separately, KCS solely handles only {{ }} carloads on the Speedway that NSR does not handle at any point. In sum, NSR is a substantial beneficiary of the substantial traffic that is carried over the Meridian Speedway.[207]

Due to NSR's exclusivity over the Meridian Speedway,[208] UP and BNSF interchanges with CSXT that compete with the exclusive NSR Traffic for which the Speedway is the best route, are over routes that are longer or operationally disadvantaged such as the New Orleans[209] or Memphis gateways.[210] The Meridian Speedway gateway has a direct route and shorter mileage between southwest originating and terminating traffic with certain customers in the southeastern U.S.[211] The competitiveness of trucking is distance limited, and the cross country lanes of focus across the

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[206] The fact that intermodal traffic is exempt from STB regulation does not make it exempt from competitive scrutiny by the STB or antitrust agencies.

[207] *See* Carey HC-WP "HC-Transcontinental Meridian Traffic.xlsx".

[208] {{ }}

[209] *See* CSXT witness Anthony Dideo V.S.

[210] Industry trade press has discussed congestion at Memphis. *See* Journal of Commerce, "Memphis shippers ask STB to intervene on intermodal congestion", , April 21, 2021,available at https://www.joc.com/rail-intermodal/intermodal-shipping/memphis-shippers-ask-stb-intervene-intermodal-congestion_20210420 html; Railway Age, "What's Really Going On in Memphis?", June 9, 2021,available at https://www.railwayage.com/news/whats-really-going-on-in-memphis/

[211] *See* Carey HC-WP "HC-Meridian.pdf".

Meridian Speedway exceed the general distance of the competitiveness of a route exclusively carried by a truck versus a railroad.[212]

Figure 14, below, reports market shares for NSR Exclusivity Traffic for specific BEA origin and termination market lanes (or pairs) between the west coast and Southeast U.S. for intermodal traffic not directly served by a single railroad.[213] This NSR Exclusivity Traffic has approximately {{ }} market share.[214] Analysis of specific market lanes is common in competition analyses of railroads.[215] The BEA area is the assumed geographic scope of the market for intermodal traffic, used as a starting point to determine if there is economic indicia of competitive harm for the area accessible by trucking to and from the intermodal terminal across the entire BEA region.[216] The high market shares for specific BEA origin and termination market lanes shown in Figure 14 indicates that trucking from more distant BEAs is generally not economical and therefore not competitive. For the NSR Exclusivity Traffic, the high market shares for certain BEA origin and destination market lanes raise concerns of competitive harm to customers today, with particular regard to traffic between: {{ }}.

[212] A truck competitor for intermodal traffic is estimated to extend to routes as long as 500 miles. *See* Bernstein, "North American Transportation", December 2021, p.5.

[213] Bureau of Economic Analysis Areas or BEAs are economic areas which define the relevant regional markets surrounding metropolitan or micropolitan statistical areas. They are created by the Bureau of Economic Analysis and are included in as geographic area of analysis in the STB CWS. Further information is available at https://apps.bea.gov/scb/pdf/2004/11November/1104Econ-areas.pdf

[214] *See* Carey HC-WP "HC-Transcontinental Meridian Traffic.xlsx". Only BEA route pairs or lanes were selected that do not have a single railroad alternative for the entire route, such as BNSF from the west coast U.S. to Atlanta, via Memphis.

[215] *See* Verified Statement of Curtis Grimm, Norfolk Southern Railway Company - Acquisition and Operation – Certain Rail Lines of the Delaware and Hudson Railway, Finance Docket No. 35873, Nov. 5, 2014.

[216] *See* Carey HC-WP "HC-Meridian.pdf".

Figure 14: NSR-Meridian Speedway Market Shares:
Intermodal Traffic Between West Coast and Southeast
(No-Single Line Service)[217]

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These {[redacted]}} market shares on specific BEA route pairs between the U.S. West Coast and Southeast U.S. raise concerns for anticompetitive effects and lessening of competition. [218, 219] Insofar as this direct Meridian Speedway route is advantaged for certain locations in the Southeast U.S.,[220] the Meridian Speedway Agreements extended NSR's route westward (and removed/eliminated KCS) as a carrier, expanding the market being divided and changing the competitive dynamic among NSR and other carriers competing for traffic to be delivered into/from the Eastern U.S with the Southwest U.S. Market shares statistics are often used to evaluate the potential for competitive concerns; with larger market shares indicating increasing market concentration and heightened concerns for undue

[217] Analysis performed on the STB Confidential Carload Waybill Sample. *See* Carey HC-WP "HC-Transcontinental Meridian Traffic.xlsx". Table reports "expanded carloads," total intermodal units may be larger than carloads due to the utilization of "double stack" intermodal containers.

[218] For instance, rival foreclosure. *See* U.S. Department of Justice & The Federal Trade Commission, "Vertical Merger Guidelines", June 30, 2020, at section 4a. While the FTC withdrew the 2020 Vertical Merger Guidelines, it recognized the substantial improvements over the prior 1984 Merger Guidelines on this topic. *See* FTC, "Statement of Chair Lina M. Khan, Commissioner Rohit Chopra, and Commissioner Rebecca Kelly Slaughter on the Withdrawal of the Vertical Merger Guidelines Commission File No. P810034", September 15, 2021, at p. 2.

[219] It is recognized that anticompetitive problems may arise when one or both levels of the integration possess market power. *See* Viscusi et al., "Economics of Regulation and Antitrust", The MIT Press, 2nd Edition (1995) *at* pp. 229, 234.

[220] *See* Carey HC-WP "HC-Meridian.pdf".

influence on a competitive outcome.[221] The STB also considers the impacts of reduced competition from eliminating a competitive alternative.[222]

C. Expansion of NSR' Exclusive Share of Traffic that can move over the Speedway Will Further Reduce Competition in the Eastern Railroad Markets

Next, in light of NSR's Notice[223] regarding Responsive application, I consider the competitive implications of NSR expanding its exclusive rights to move certain traffic over the MSLLC Line (which I will supplement once a detailed explanation of its request is submitted in its formal filing). NSR's Notice indicates that it will seek authority from the Board to expand its market division to include a wider geographic area and a wider range of products that will be made exclusively NSR Traffic. This expansion of the NSR exclusivity Traffic will diminish competition for that traffic East of Meridian. NSR says it will be seeking the exclusive right to use the Meridian Speedway for traffic that originates or terminates west of Shreveport (instead of Dallas) for automotive, and "premium boxcar" traffic, in addition to intermodal traffic, and to exercise its exclusive rights through trackage rights rather than haulage rights.[224] NSR's request to expand the geographic area and expand its exclusivity rights to traffic that originates and terminates from key business areas in and around Texas (e.g. Dallas, Houston, Austin, Tulsa), and potentially in Mexico.[225] NSR's formal request is needed to clarify the specific traffic that it seeks to expand which is generally mentioned in its notice.

Expanding the of NSR's exclusive rights will have a substantial beneficial impact on NSR, and a corresponding adverse impact on competition and shippers. I illustrate the impact by attempting to estimate the additional carloads and revenue for expanded traffic NSR appears to seek. First, regarding product expansion the addition of premium boxcar traffic and automotive traffic, this

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[221] *See* U.S. Department of Justice & The Federal Trade Commission, "Horizontal Merger Guidelines", August 19, 2010 at pp. 18-19.

[222] "[T]he Board focuses on preserving competition between two rail carriers; it protects against "2-to-1" reductions in competition, but in minor transactions it does not generally remedy transaction-related reductions of competitive options from three carriers to two carriers absent a showing of specific harm. See Union Pac. Corp.—Control & Merger—S. Pac. Rail Corp. (UP/SP Merger 1996), 1 S.T.B. 233, 351 (STB served Aug. 12, 1996)" *See* Norfolk Southern Railway Company – Acquisition and Operation – Certain Rail Lines of the Delaware and Hudson Railway Company, Inc., Finance Docket No. 35873 (Decision No. 6 served May 15, 2015), p. 17. For discussion of whether competition is diminished by a proposed merger moving firm count from 3-to-2 and 2-to-1, *see* Union Pac. Corp.—Control & Merger—S. Pac. Rail Corp., Decision No. 44, Finance Docket No. 32760, August 6, 1996, at pp. 119-124.

[223] *See* STB Finance Docket No. 36500, Description of Anticipated Responsive Application by Norfolk Southern Railway Company, January 12, 2022.

[224] While the STB generally considers these product types to be exempt from recourse for rate setting disputes before the STB, that is separate and distinct from approval of agreements and expansion of such agreements that require approval and should be expected to be evaluated for the competitive effects arising therefrom.

[225] NSR's Inconsistent Application provides limited details to the specific locations west of Shreveport and was particularly vague with respect to the specific locations in Mexico it intends to include in its request.

creates new opportunities for more than {{ }} automotive and premium box cars, along with substantial revenue as shown in the first panel of Figure 15 below. Figure 15 below (panel 1) also reports gross revenues of potentially }}.[226] Further, the expansion of the geographic scope between Shreveport and Dallas includes approximately {{ }} premium box cars, {{ }} automotive cars and {{) as shown in panel 2 of Figure 15 below. These additional carloads associated with the expanded geographic scope, report gross revenue equal to approximately }}.

Figure 15: Traffic Revenue and Cars Associated with NSR's Request for Expanded Product Types - West of Dallas- and Geographic Expansion West of Shreveport/East of Dallas[227]

[226] This revenue estimate is illustrative because it attempts to subtract revenues that NSR receives today from a portion of the move as well as BNSF and UP revenue that NSR cannot access.

[227] Analysis performed on the STB Confidential Carload Waybill Sample. *See* Carey HC-WP "HC-Transcontinental Meridian Traffic.xls".

D. Recommended Conditions to Ameliorate Competitive Concerns Regarding the Meridian Speedway and Affecting Eastern Rail Markets

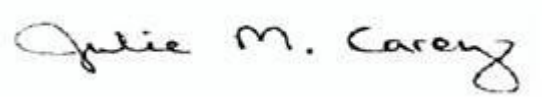
The competitive concerns arising from NSR's current exclusivity right to serve certain intermodal traffic over the Meridian Speedway, coupled with the potential for further diminution in competition across the Meridian gateway by NSR's proposed expansion, indicate the STB should consider conditions to this Transaction that abolish the NSR exclusivity provisions in the Meridian Speedway Agreement. With NSR's exclusivity provision abolished; CPKC is freed to work with its connecting carriers to develop commercially reasonable terms to interchange or otherwise move traffic that is carried over the Meridian Speedway. This will remedy the current anticompetitive circumstance and lead to a procompetitive benefit with increase competition in the Eastern U.S. railroad markets associated with traffic movements that have economic advantages across the Meridian Gateway.

Further, to the extent that the STB allows the NSR to expand the allowable products and the geographic scope for use over the Meridian Speedway, additional conditions to protect competition should be imposed.

VERIFICATION

I, Julie M. Carey, declare under penalty of perjury that I have read the foregoing Verified Statement, that I know the facts asserted therein, and that the same are true as stated. Further, I certify that I am qualified to and authorized to submit this Verified Statement.

Executed on February 28, 2022



_____

Julie M. Carey

VERIFICATION

I, Albert W. Bremser, declare under penalty of perjury that I have read the foregoing Verified Statement, that I know the facts asserted therein, and that the same are true as stated. Further, I certify that I am qualified to and authorized to submit this Verified Statement.

Executed on February 28, 2022

Albert W. Bremser

Attachment 1: Carey CV

NERA
ECONOMIC CONSULTING

Julie M. Carey
Managing Director
NERA Economic Consulting
1255 23rd Street NW, Suite 600
Washington, DC 20037
Tel: +1 202 466 9203 Fax: +1 202 466 3605
Mobile: + 1 703 622 5032
julie.carey@nera.com
www.nera.com

JULIE M. CAREY
MANAGING DIRECTOR

Julie M. Carey is a Managing Director at NERA Economic Consulting. She has substantial experience as an economist, providing expert evidence in energy and transportation related commercial and regulatory disputes. She has more than 20 years of experience addressing economic issues in oil and gas, pipelines, power/coal/renewables, and railroad sectors. Ms. Carey is recognized as a leading energy expert (2019-2021) and a leading arbitration expert (2021-2022) by Who's Who Legal.

In addition to her expert consultancy assignments, Ms. Carey is also an adjunct professor at Georgetown University where she teaches a graduate level course in energy economics and policy, which includes instruction on economics of energy products and transportation and regulatory economics.

Ms. Carey provides expert consulting and testifying services on energy economic issues in commercial disputes before U.S. federal and state courts, and before arbitration panels in the U.S. and internationally, including international arbitration venues. She also routinely assists clients in matters before energy and transportation regulators including U.S. Federal Energy Regulatory Commission (FERC) and U.S. Surface Transportation Board (STB) as well as many other regulatory agencies in the U.S. and Canada.

Ms. Carey has substantial expertise in economic analyses of energy and transportation markets. She routinely conducts economic analyses of energy and transportation markets to understand historical and forecasted market conditions (supply, demand and prices), as well as to evaluate competition, claims of market manipulation, and other anticompetitive acts. She has conducted these analyses many dozens of times for the purposes of the regulatory approval of mergers and acquisitions, market-based rate authority, market rules, negotiated rates, as well as within investigations and commercial disputes. Her work includes evaluation of the reasonableness of rates and whether market participant bidding, trading and other behavior is discriminatory or otherwise manipulative, and whether prices reflect competitive market prices. Ms. Carey's work includes a variety of other regulatory economic analysis including affiliate relationships, cost of service and forward-looking costs, among others.

Within her commercial dispute work, Ms. Carey has been involved in many claims of breach of contract including oil and gas products, oil pipeline transportation, railroads and coal, power, renewables, spent nuclear fuel. She has also been involved in cases concerning partnership disputes, delayed plant operations, diminished value claims, replacement power, antitrust and manipulation claims, clean air act, fiduciary duty, and bankruptcy, among others. Ms. Carey has substantial experience with economic damages (historical and future lost profit analyses) and conducts valuation analyses. She has assessed and quantified economic damages and valuations in dozens of cases which include breach of contract, antitrust, class action, and other types of disputes.

Ms. Carey also has experience with environmental analysis (e.g., greenhouse gases and other types of

emissions) and macroeconomic modeling (i.e., jobs, GDP, taxes) in which she studies the impact of energy infrastructure construction and operations on the economy for regulatory and business decision-making.

EDUCATION

- **Pennsylvania State University**
  Doctoral Studies Program Coursework/M.A., Economics, 1993

- **Allegheny College**
  Bachelor of Science, Economics, 1991

PROFESSIONAL EXPERIENCE

2020-Present	**NERA Economic Consulting** – Managing Director
2017-2019	**NERA Economic Consulting** - Director
2016-Present	**Georgetown University (Washington, DC) -** Adjunct Professor
2011-2017	**Navigant Consulting, Inc. (Washington, DC) -** Director
2004-2010	**LECG, Inc. (Washington, DC) -** Principal
2000-2004	**FTI Consulting, Inc. (Washington, DC) -** Director, Manager
1996-2000	**LECG, Inc. (Washington, DC) -** Economist, Senior Associate, Associate
1994-1996	**American Public Power Association (Washington, DC) -** Research Analyst

CERTIFICATIONS, MEMBERSHIPS, AND AWARDS

- Leading Energy Expert by Who's Who Legal (2019-2021)
- Leading Arbitration Expert by Who's Who Legal (2021 and 2022)
- International Association for Energy Economists
- U.S. Association for Energy Economists

SELECTED ENERGY PROJECT EXPERIENCE

Railroad

- Expert reports in numerous STB regulatory proceedings addressing appropriate rate to use for a trackage rights fees, including addressing economic and regulatory analyses, including numerous valuation methodologies. Economic analysis of plastics, chemical and petroleum railroad transportation services, rates, costs and contribution margins.
- Expert report and expert testimony in commercial arbitration regarding multiple breach of contract claims for joint-line transportation service, and financial, economic and regulatory considerations regarding the contracts, negotiations and the financial impact as well as economic damages.
- Expert consultation analyzing economics of containerized freight transportation, including intermodal rail and competition with alternative transportation modes in a transportation contract dispute and claims of anticompetitive behavior for a commercial arbitration.
- Expert report in STB proceeding regarding the potential introduction of indirect competition analyses within market dominance determinations for coal transportation rates to utility generation facilities.

- Expert consultation analyzing economics of coal railroad transportation and fuel surcharges and claims of anticompetitive behavior for commercial disputes.
- Expert reports in a coal contract commercial dispute analyzing economic damages and replacement coal source and transportation alternatives.
- Expert reports in numerous regulatory proceedings involving rail transportation rate reasonableness disputes for coal, including evaluation of appropriate regulatory economic approach to assess the reasonableness of a railroad rate, railroad transportation rate analyses (historical and future) for coal and other products, coal demand and coal plant performance analyses, and revenue attribution methodologies for shared facilities.

Oil and Gas

- Expert report and economic analysis in an ongoing matter to provide economic evidence regarding potential competitiveness of refined product pipeline markets (gasoline, distillates, fuel oil, jet fuel) for a proceeding before the FERC involving a complaint regarding the reasonableness of current rates and continuation of its market-based rate authority. This work includes evaluation of product and transportation (pipeline, waterborne, trucking and rail), competition, and competitive prices for U.S. and international transactions of refined products and transportation.
- Expert report and economic analysis of wholesale propane markets, supply and demand and potential transportation alternatives for propane in the Midwestern U.S. in a claimed discrimination by a shipper on an NGL pipeline.
- Economic consulting and expert report before the NEB regarding potential of discriminatory behavior that can arise from an unregulated affiliate of a regulated oil pipeline and other economic issues pertaining to a crude oil pipeline including evaluation of appropriate code of conduct. The economic analysis includes evaluation of substantial quantities of NGL - butane and other oil products injections into the pipeline system and the impact on the quality and financial harm and economic damages for the diminution of crude oil value.
- Economic and competition analyses in numerous regulatory proceedings pertaining to refined petroleum product, crude oil, natural gas liquids and transportation markets for oil pipelines market-based rate authority. This work includes analysis of product and geographic markets and the evaluation of origin and destination market, analysis of refined petroleum product and crude oil markets and transportation economics (rail, truck, waterborne, and pipeline) throughout most U.S. markets, Canada and many other international markets and analysis of competitive prices and market concentration.
- Expert report and testimony in an international arbitration regarding economic analysis of crude oil markets (Western Canadian and global markets), economics of conventional and unconventional oil and gas production resources, and the potential causal linkage of falling crude oil prices since 2014 and impact thereof on the energy construction industry and certain companies located in Western Canada.
- Expert consulting providing economic analysis of the competitiveness of crude oil transportation market in Western Canada to evaluate competition within pipeline markets (including railroad competition) before the NEB. This work also included economic analysis of the negotiations process and negotiated rates for new transportation contract sales to determine if the process was competitive and the rates were consistent with fair market value prices.
- Expert consulting in a refined product transportation contract dispute involving economic analysis of rail, truck, and pipeline transportation. This work involved the midwestern and Gulf Coast regions.

- Expert consulting assisting the Canadian Competition Bureau (CCB) in an investigation of potential energy market manipulation within the wholesale natural gas liquids product markets and price spikes, pertaining to propane. This work includes market analysis and econometric analysis to evaluate whether the actual market prices reflect competitive market prices (i.e., consistent with supply, demand, prices, constraints, etc.) or if manipulative or anticompetitive behavior occurred. This work included economic analysis of product and transportation markets (including pipeline, railroad, and trucking).
- Expert consulting in a claimed breach of a refined petroleum products contract in a commercial arbitration for a U.S. refinery involving economic analysis of crude oil and refined product markets, as well as rail, truck, waterborne and pipeline transportation economics and economic damages.
- Expert consulting in a crude oil product contract dispute for a commercial arbitration to conduct economic analysis of crude oil markets, pricing, and alternative transportation economics (rail, truck, waterborne, and pipeline). This work involved California and international markets (including Ecuador (Oriente), Alaska and Western Canada.)
- Expert consulting in numerous disputes/investigations involving claims of market manipulation and anticompetitive behavior within natural gas product markets. This work included evaluation of economic purpose of natural gas product purchases and sales as well as economic analysis to evaluate whether the market prices reflect competitive market prices (i.e., consistent with supply, demand, prices and constraints, etc.).

Power and Renewables

- Expert reports and testimony regarding competition in U.S. wholesale power markets and impact to coal producers in the Powder River Basin (PRB). Analysis of generating resources economics (units, purchases and sales), short run marginal costs of generating units and least cost economic dispatch and inter-fuel competition, such as natural gas and renewables, within ISO and non-ISO areas. Evaluation of generating unit commitment designations and bidding and other market rules. Statistical analysis of transmission constraints and analysis of recent and proposed transmission expansions and the impact on geographic scope of competition.
- Expert evidence and consulting in many dozens of matters related to competition within wholesale electricity markets for regulatory approval of mergers and acquisitions and market-based rate authority in regions across U.S. This work includes market power screens and delivered price test analyses and analysis of product (energy, capacity, and ancillary service) and geographic markets, including assessments of transmission constraints. The economic analysis includes evaluation of delivered fuel costs (natural gas, coal, etc.) and operational characteristics of power plants (seasonal capabilities, short run marginal costs, efficiency rates, etc.).
- Expert economic analysis and damages for a claim of tortious interference and unfair competition in wholesale solar panel market in the U.S.
- Expert report to respond to quantum issues associated with a $1 billion economic damage claim in an energy contract dispute in an international arbitration. In addition, economic analysis was conducted on the market (supply, demand and pricing) and the claimant's commercial activities pertaining to the contractual negotiations.
- Expert reports and expert testimony analyzing economic and environmental analysis of the greenhouse gases (GHG) impact from the construction and operation of a new coal terminal export facility and downstream power markets for regulatory approval. This work included long term market and economic analysis of the elasticity of demand of coal, forecast of GHG emission and other energy market impacts within downstream energy markets (U.S. and Pacific Basin). This work included

economic analysis of coal transportation economics and delivered cost of coal within U.S. and internationally.

- Expert consulting and economic damages analyses in a dispute regarding the failed performance of a steam generator turbine in an ICC international arbitration (for California power plant). The damages claim was approximately $7 billion. This work included economic theory and quantification of damages under a benefit of the bargain and rescission damages theories as well as evaluation of long term energy forecasts, economic performance and replacement power purchases.
- Expert for a North American ISO regarding wholesale power markets, addressing economics transition away from coal, including the decommissioning of coal-fired generating units and conversion of other coal-fired generating units to natural gas.
- Expert testimony regarding a claim of economic damages (past and future) associated with the alleged breach of a power purchase agreement within an international arbitration. This work included analysis of the appropriate economic theory of damages, quantification of economic damages and energy market related analysis.
- Expert consulting in a regulatory investigation into the reasonableness of market prices paid for natural gas purchases and bidding behavior of certain natural gas fired power generation facilities made during the 2013/2014 winter often referred to as the polar vortex. This work involved the eastern U.S markets.
- Expert report in an international arbitration providing an analysis of the Chinese and global solar panel market, reasonableness and competitiveness of the sales negotiations and negotiated prices, market value of solar power products and other valuation related issues. The dispute surrounds the performance of numerous agreements to acquire, construct and operation numerous PV manufacturing production lines.
- Expert consulting regarding a joint venture/ joint ownership contractual arrangement and the financial impact to ratepayers and counterparties from a bankruptcy of one of the parties. Additional analysis of historical benefits derived from the arrangement as well as other regulatory and market analyses.
- Expert consulting regarding antitrust claims regarding the solar panel manufacturing industry. This work included economic analysis of the potential anticompetitive behavior and a valuation analysis of a solar panel company, including the development of a discounted cash flow analysis analyzing the future cash flows and net present value of the enterprise.
- Expert testimony regarding the impact of a proposed wholesale power market rule regarding the transmission allocation among market participants, incentives for new entry, and an evaluation of economic efficiency and potential market power within the wholesale electricity market.
- Expert consulting in numerous disputes/investigations involving claims of market manipulation and anticompetitive behavior within electricity product markets. This work included evaluation of decision-making surrounding power plant outages and trading related activities and evaluation whether the market prices reflect competitive market prices (i.e., consistent with supply, demand, prices and constraints, etc.). Demand simulations were conducted to evaluate the impact on market prices. This work involved the western U.S markets, including California.
- Expert report regarding past and future economic damages and economics of the silane gas market and supply, demand and pricing in the solar power panel market in a contract dispute before a bankruptcy court.

SELECTED EXPERT AFFIDAVITS AND TESTIMONY

Highly Confidential Commercial Arbitration regarding development service agreements, Japan Commercial Arbitration Association Rules, Expert Report of Julie M. Carey, January 12, 2022.

Texas PUC Docket Numbers 52321and 52322; Application of The Electric Reliability Council of Texas, Inc. For A Debt Obligation Order Under Pura Chapter 39, Subchapter M And N, And Request for A Good Cause Exception, Reply Expert Report of Julie M. Carey, August 12, 2021.

Highly Confidential Commercial Arbitration regarding Railroad Transportation Rate, Expert Report of Julie M. Carey, May 26, 2021, Expert Testimony July 9 and 12, 2021.

FERC Docket No. ER11-47, Triennial Update for Market Based Rate Authority for American Electric Power Company, et al. in the Southwestern Power Pool region, Affidavit of Julie M. Carey and Al Bremser, June 29, 2021.

Surface Transportation Board ("STB"), FD 32760 (Sub-No. 46), BNSF Railway Company – Terminal Trackage Rights – The Kansas City Southern Railway Company and The Union Pacific Railroad Company, Opening Verified Statement (VS) of Julie M. Carey, January 26, 2021; Reply VS on April 12, 2021 and Rebuttal VS on May 11, 2021.

FERC Docket Nos. OR18-7-002, et al. (Consolidated), Epsilon Trading, LLC, Chevron Products Company, and Valero Marketing and Supply Company v. Colonial Pipeline Company, In Market-Based Rate Proceeding, Prepared Answering Testimony of Julie M. Carey to Complainants, January 24, 2020; Prepared Answering Testimony to Trial Staff, April 6, 2020. Trial Testimony - December 3, 4 and 7-9, 2020.

FTC v. Peabody Energy Corporation and Arch Coal, Inc., Civil Action No. 4:20-cv-000317-SEP before the U.S. District Court Eastern District of Missouri, Expert Report of Julie M. Carey (May 29, 2020), Response Expert Report (June 19, 2020), Deposition Testimony (June 29, 2020), Trial Testimony - July 21, 2020.

FERC Docket No. OR20-5-000, NGL Supply Wholesale, LLC v. Phillips 66 Pipeline LLC and Phillips 66 Company, Affidavit of Julie M. Carey, January 2, 2020.

In the Matter of Arbitration, under the London Court of International Arbitration ("LCIA") Arbitration Rules, LCIA Case No. 183933, Between Hemlock Semiconductor Pte. Ltd, Claimant and Yingli Green Energy International Trading Limited, Respondent, Expert Report, May 9, 2019.

Surface Transportation Board ("STB"), FD 32760 (Sub-No. 46), BNSF Railway Company – Terminal Trackage Rights – The Kansas City Southern Railway Company and The Union Pacific Railroad Company, Verified Statement of Julie M. Carey, February 4, 2019.

Canadian National Energy Board Hearing Order RHW-002-2017, File OF-Tolls-Group2-T309-2017-01 01, TEML Westspur Pipelines Limited, Notice of Complaint pursuant to Part IV of the National Energy Board Act by Crescent Point Resources Partnership, Reply to Sur-Reply Expert Report of Julie M. Carey, November 23, 2018. Reply Expert Report of Julie M. Carey (submitted jointly with other subject matter experts), August 31, 2018.

FERC Docket No. ER11-47, Triennial Update for Market Based Rate Authority for American Electric Power Company, et al. in the Southwestern Power Pool region, Affidavit of Julie M. Carey and Laura Olive, June 27, 2018.

In the Matter of Arbitration Proceeding Concern disputes with respect to a share purchase agreement dated June 26, 2014 Between Pacer Construction Holdings Corporation, Pacer Construction Management Corporation, Pacer Mamisiwin Corporation, Pacer Construction Corporation, Pacer Foundations

Corporation, Pacer Projects Corporation, FTI Consulting Canada Inc. (in its capacity as receiver and manager of Pacer Promec Energy Corporation and Pacer Promec Energy Construction Corporation) and Mastec, Inc. and Richard Pelletier holdings Inc., Richard Pelletier, Resman holdings ltd., Don Taylor, 592652 Alberta ltd., and John Simpson; Hearing Testimony of Julie M. Carey and Bradley A. Heys, June 18, 2018. Reply Expert Report - April 9, 2018.

Millennium Bulk Terminals - Longview, LLC, A Delaware Limited Liability Corporation V. Washington Department of Ecology, An Agency of The State of Washington; Superior Court of Washington For Thurston County, Case No. 17-2-06442-34, Declaration of Julie M. Carey, May 9, 2018.

In the Matter of Arbitration Between CSX Transportation, Inc., Claimant and Central Railroad Company of Indianapolis d/b/a Chicago, Fort Wayne & Eastern Railroad; the Columbus & Ohio River Railroad Company; First Coast Railroad Inc.; Golden Isles Terminal Railroad, Inc.; Indiana & Ohio Railway Company; Marquette Rail, LLC; Meridian & Bigbee Railroad, LLC; Mid-Michigan Railroad, Inc. d/b/a Michigan Shore Railroad, Inc.; and Riceboro Southern Railway, LLC, Hearing Testimony of Julie M. Carey, April 20, 2018. Expert Report - November 15, 2017.

In the Matter of New England Central Railroad, Inc., Trackage Rights Order, Pan Am Southern, LLC. Surface Transportation Board ("STB"), Docket No. FD 35842, Verified Statement of Julie M. Carey, December 6, 2017.

Application of Millennium Bulk Terminals-Longview, LLC for Shoreline Substantial Development Permit and Conditional Use Permit, File Number 12-04-0375, Shoreline Permit Number 17-0992, Expert Testimony of Julie M. Carey, November 6, 2017.

Application of Millennium Bulk Terminals-Longview, LLC for Shoreline Substantial Development Permit and Conditional Use Permit, File Number 12-04-0375, Shoreline Permit Number 17-0992, Expert Report of Julie M. Carey and Peter Rawlings (ERM), October 26, 2017.

National Energy Board Hearing Order RHW-002-2017, File OF-Tolls-Group2-T309-2017-01 01, TEML Westspur Pipelines Limited, Notice of Complaint pursuant to Part IV of the National Energy Board Act by Crescent Point Resources Partnership, Expert Report of Julie M. Carey, September 15, 2017.

Minnesota Public Utilities Commission, Docket No. PL-9/PPL-15-137, In the Matter of the Application of Enbridge Energy, Limited Partnership for a Routing Permit for the Line 3 Replacement Project in Minnesota from the North Dakota Border to the Wisconsin Border., Expert Report of Julie M. Carey (With Dr. Rick Lichty), January 30, 2017.

FERC Docket No. ER10-2179 et al., Triennial Update for Market Based Rate Authority for Calvert Cliffs Nuclear Power Plant, LLC, et al. in the Northeast region, Affidavit of Julie M. Carey (with Julie R. Solomon), December 29, 2016.

FERC Docket No. ER13-1536 et al., Triennial Update for Market Based Rate Authority for Exelon in the Northeast region, Affidavit of Julie M. Carey (with Julie R. Solomon). December 29, 2016.

FERC Docket No. ER10-1823 et al., Triennial Update for Market Based Rate Authority for Dominion Energy Marketing, et al. in the Northeast region, Affidavit of Julie M. Carey (with Julie R. Solomon). December 29, 2016.

FERC Docket No. ER11-1933 et al., Triennial Update for Market Based Rate Authority for Green Mountain Power, et al. in the Northeast region, Affidavit of Julie M. Carey, December 23, 2016

FERC Docket No. ER11-47 et al., Triennial Update for Market Based Rate Authority for American Electric Power Company, et al. in the Northeast region, Affidavit of Julie M. Carey. December 27, 2016.

U.S. Army Corps of Engineers, Seattle District, Response to Draft Environmental Impact Statement for the National Environmental Policy Act Regarding the Proposed Millennium Bulk Terminals Longview Project, Expert Evidence. November 29, 2016.

Cowlitz County and the Washington State Department of Ecology, Response to Draft Environmental Impact Statement for the State Environmental Policy Act Regarding the Proposed Millennium Bulk Terminals Longview Project, Expert Evidence. June 13, 2016.

FERC Docket No. Docket No. EC16-, Supplemental Affidavit of Julie M. Carey to Support Ohio Valley Electric Corporation's Application for Market Based Rate Authority in PJM, MISO, and other market areas. January 17, 2016. (Initial Report November 6, 2015)

Wisconsin Public Service Commission, Docket No. 6800-CE-176, Application for a CPCN To Build an Natural Gas-Fueled Power Plant at its Riverside Energy Center Facility, Surrebuttal Testimony of Julie M. Carey, December 16, 2015. (Rebuttal Testimony December 4, 2015)

FERC Docket No. Docket No. EC15-, Supplemental Affidavit of Julie M. Carey to Support PNM's Application for Authorization of Disposition of Jurisdictional Facilities. November 6, 2015. (Initial Report September 25, 2015.)

FERC Docket No. ER11-47, Triennial Update for Market Based Rate Authority for American Electric Power Company, et al. in the Southwestern Power Pool region, Affidavit of Julie M. Carey. June 30, 2015.

FERC Docket No. ER10-2302, Change in Status Filing for Public Service Company of New Mexico, et al., Affidavit of Julie M. Carey. August 15, 2014.

FERC Docket No. ER14-, Change in Status Filing for American Electric Power Company, et al., Affidavit of Julie M. Carey (with Ben Ullman). December 27, 2013.

FERC Docket No. ER11-47 et al., Triennial Update for Market Based Rate Authority for American Electric Power Company, et al. in the PJM RTO region, Affidavit of Julie M. Carey. December 20, 2013.

FERC Docket No. ER13-1896-000, Application of American Generation Resources Inc. for Market Based Rate Authority, Affidavit of Julie Carey. July 5, 2013.

ULVAC, INC vs. China Solar Power (Holdings) Ltd., In the Matter of a Commercial Arbitration, Hong Kong International Arbitration Centre, HKIAC /A11013, Expert Report of Julie Carey. June 11, 2013.

Energy Conversion Devices, Inc., et al., Chapter 11, Case No. 12-43166, U.S. Bankruptcy Court Eastern District of Michigan Southern Division, Expert Report for Praxair by Julie Carey (with Graham Stevens). April 17, 2013.

HS Orka hf. vs. Nordural Grundartangi, ehf and Orkauveita Reykjavikur, In the Matter of a Commercial Arbitration, Stockholm Chamber of Commerce Arbitration V (191/2011), Expert Testimony of Julie M. Carey. February 5, 2013. (Rebuttal Report on October 24, 2012. Initial Report on August 29, 2012.)

STB Ex. Parte No. 717, Reply to Petition of Association of American Railroads to Institute a Rulemaking Proceeding to Reintroduce Indirect Competition as A Factor Considered in Market Dominance Determinations for Coal Transported to Utility Generation Facilities. Verified Statement of Julie M. Carey (with James M. Speyer), January 14, 2013.

FERC Docket No. ER96-1551 and ER01-615 and ER09-74, Triennial Update for Market Based Rate Authority for Public Service Company of New Mexico, Affidavit of Julie M. Carey. December 21, 2012.

On behalf of Montana Alberta Tie Ltd ("Enbridge – MATL"), Alberta Utilities Commission, Proceeding 1633, Expert Testimony of Julie M. Carey (with Cliff Hamal). September 18-19, 2012. Expert Report June 15, 2012)

FERC Docket No. ER11-47, Triennial Update for Market Based Rate Authority for American Electric Power Company, et al. (Southwestern Power Pool), Affidavit of Julie M. Carey. June 29, 2012.

FERC Docket No. ER10-727-001, Request for Market Based Rate Authority for AEP Retail Energy Partners LLC, Affidavit of Julie M. Carey. March 23, 2010.

FERC Docket No. ER96-1551and ER01-615 and ER09-74, Triennial Update for Market Based Rate

Authority for Public Service Company of New Mexico, Affidavit of Julie M. Carey. March 8, 2010.

On behalf of COALSALES II, L.L.C., In the matter of Gulf Power Company v. COALSALES II, L.L.C. Docket no. 3:06 CV 270/MCR/MD, before the US District Court for the Northern District of Florida, Pensacola Division, Expert Reports of Julie M. Carey (with Cliff Hamal). December 11, 2008 and August 19, 2008.

FERC Docket Nos. ER96-2495, ER97-4143, ER97-1238, ER98-2075 and ER98-542, Change in Status Filing for American Electric Power for Market-Based Rate Authority, Affidavit of Julie M. Carey. May 25, 2007.

FERC Docket No. Docket EC06-113-000, Application for Asset Transfer of Contra Costa #8 for Pacific Gas and Electric Company, Mirant Delta, LLC and Mirant Special Procurement, Inc., Affidavit of Julie A. Murphy (now Julie M. Carey). April 17, 2006.

FERC Docket No. ER96-1551 and ER01-615, Change in Status Filing for Public Service Company of New Mexico for Market-Based Rate Authority, Affidavit of Julie A. Murphy. January 12, 2006.

FERC Docket No. ER05-1244-000 and ER05-1244-001, Application by Societe Generale Energie (USA) Corp. for Market-Based Rate Authority, Affidavit of Julie A. Murphy. July 21, 2005.

Testimony of Julie Murphy on behalf of Onvoy, Inc., Onvoy, Inc. v. Allete, Inc. f/k/a Minnesota Power, Inc. d/b/a Minnesota Power and Light Company and, Enventis Telecom, Inc., Sixth Judicial District Court File No. 69-C9-03-601595, St. Louis County, Minnesota. April 21, 2005.

STB Docket No. 42071, Otter Tail Power Co. v. BNSF Railway Co, Sponsored Evidence within Section III-A Stand-Alone Traffic Group of the Supplemental Response. March 1, 2005. Additional Reply Evidence, March 22, 2004. Reply Evidence, October 8, 2003.

Expert Report Julie A. Murphy (with John Klick) on behalf of Onvoy, Inc., Onvoy, Inc. v. Allete, Inc. f/k/a Minnesota Power, Inc. d/b/a Minnesota Power and Light Company and, Enventis Telecom, Inc., Sixth Judicial District Court File No. 69-C9-03-601595, St. Louis County, Minnesota. December 5, 2004.

STB Docket No. 41191 (Sub-No. 1), AEP Texas North Company v. Burlington Northern and Santa Fe Railway Company, Verified Statement of Julie A. Murphy. September 9, 2004. Reply Evidence Section III-A Stand-Alone Traffic Group, May 24, 2004.

MI PSC Case No. U-13531, In the Matter of the Commission's Own Motion to Review the Costs of Telecommunication Services Provided by SBC Michigan, Final Reply Declaration of Julie A. Murphy (with Michael Baranowski). May 10, 2004. Initial Declaration, January 20, 2004.

STB Docket No. 41185, Arizona Public Service and PacifiCorp v. Burlington Northern Santa Fe Railway Company, Verified Statement of Julie Murphy. April 18, 2004.

Texas PUC SOAH Docket. No.473-04-0001, PUC Project No. 27957, Application of CenturyTel of San Marcos, Inc. for Approval of a Plan for Disaggregation of State and Federal Universal Service Support, Testimony of Julie Murphy on Behalf of Grande Communications Networks, Inc. February 19, 2004. (Direct Testimony, December 29, 2003.)

STB Docket No. 42058. Arizona Electric Power Cooperative Inc. v. the Burlington Northern and Santa Fe Railway Company and Union Pacific Railroad Company, Sponsored Testimony within Section III-A Stand-Alone Traffic Group of Reply Evidence and Argument of Burlington Northern Santa Fe Railway Co. January 26, 2004. Verified Statement of Julie Murphy (with John Klick). April 18, 2003.

STB Docket No. 42072, Carolina Power & Light Co v. Norfolk Southern Railway Company, Sponsored Testimony within Section III-A Stand-Alone Traffic Group, Supplemental Reply Evidence January 12, 2004. Reply Evidence, October 11, 2002.

STB Docket No. 42069, Duke Energy Corporation v. Norfolk Southern Railway Company, Sponsored Testimony within Section III-A Stand-Alone Traffic Group of Supplemental Reply Evidence and Argument of Norfolk Southern Railway Co. January 12, 2004. Reply Evidence, September 27, 2002.

STB Docket No. 42070, Duke Energy v. CSX Transportation, Inc., Sponsored Testimony within Section III-A Stand-Alone Traffic Group of Supplemental Testimony of CSX Transportation, Inc. January 5, 2004. Reply Evidence, September 20, 2002.

FCC WCB Docket No.03-18. In the Matter of Alascom, Inc. Request for Waiver of Commission Rule and Orders Requiring Annual Tariff Revision, Alascom, Inc. Petition for Waiver, Response Declaration Julie Murphy (with John Klick), Supplement to Waiver Request and Response to FOIA Request. April 4, 2003. Additional Evidence provided March 13, 2003, March 5, 2003, January 7, 2003.

STB Docket No. 42057, Xcel v. BNSF Railway Co., Sponsored Testimony within Section III-A Stand-Alone Traffic Group of Reply Evidence and Argument of Burlington Northern Santa Fe Railway Co. April 4, 2003.

SELECTED REPORTS, PUBLICATIONS AND PRESENTATIONS

Washington Arbitration Update Conference, Assessing Damages in Non-Expropriatory Breaches, Presentation and Panel Discussion, October 14, 2021.

Round Table Discussion Energy International Arbitration Update, Financier Worldwide. October 22, 2021.

Oil Pipelines Markets, Presentation at Association of Oil Pipelines (AOPL) Annual Business Conference, September 23, 2021.

Measuring Economic Damages with Maximum Certainty, Global Arbitration Review, May 21, 2021. (with Christian Dippon and Will Taylor). (Updated from April 2, 2019 publication)

Oil Pipelines: The Regulatory and Market Landscape, Presentation at open session at FERC on behalf of Association of Oil Pipelines (AOPL), May 7, 2020.

Evolution of Forecasting Techniques for Dynamic Energy Markets, Chapter in the Handbook of Energy Finance, Theories, Practices and Simulations, Julie Carey (with Derya Eryilmaz) March 2020.

The Future of the U.S. Renewable Energy Disputes: Decoding Recent Trends and Updates, Presentation for the Knowledge Group, March 24, 2020. (with Al Bremser)

Analysis of Economic Benefits of the PEPCO's Long Term Capital Plan, Potomac Electric Power Company (PEPCO), January 2020 (updated September 2020).

Energy Disputes and Litigation: Effective Strategies and Best Practices for the Year Ahead Energy, Presentation for the Knowledge Group, December 5, 2019. (with Al Bremser)

Oil Pipeline Transportation Markets, Presentation at AOPL Annual Business Conference, September 2019.

A Practical Guide to Economic Damages in Complex Commercial Disputes, Presentation for the Knowledge Group, May 2, 2019. (with Christian Dippon)

Crude Oil and Refined Products and Transportation Markets, Presentation at open session at FERC on behalf of AOPL, April 24, 2019.

Economic Benefits Analysis of PROJECTpipes on the District of Columbia, November 2018 (Julie Carey and Derya Eryilmaz).

Crude Oil and Refined Products and Transportation Markets, Presentation at open session at FERC on behalf of AOPL, January 31, 2018.

Infrastructure Development and Impact on the Supply Chain, including implementation of the FAST Act. The Association of Transportation Law Professionals, Transportation Forum, XIV, October 16, 2017.

Crude Oil and Transportation Market and Regulatory Developments, Julie Carey and Laura Olive Association of Oil Pipeline Business Conference, September 20, 2017.

Analysis of Economic Benefits of the Capital Grid Project in the District of Columbia and Maryland, Potomac Electric Power Company (PEPCO), August 31, 2017.

Comments to the FERC Notice of Inquiry: Modifications to Commission Requirements for Review of Transactions under Section 203 of the Federal Power Act and Market-Based Rate Applications under Section 205 of the Federal Power Act RM16-21-000, Julie Carey and others, November 28, 2016.

Crude Oil and Transportation Market and Regulatory Developments, Julie Carey, Association of Oil Pipeline Business Conference, September 16, 2016.

Economic Analysis of Electric Vehicle Market from Illinois' Proposed Legislation, Julie M. Carey (with Celia David and John Gartner), May 17, 2016 (Updated August 10, 2016).

Will Trudeau and Obama Fulfill Their Energy Promises? Julie Carey, The Energy Advisors, March 25, 2016.

NGL Market Development Panel, Infocast Midstream Summit, February 17, 2016.

Energy Market Trends, Economic Implications, and the Outlook for Infrastructure, Construction Superconference, December 8, 2015.

Effects of Rising Demand for Energy Infrastructure Development on Labor, Other Resources, and the Economy, Julie Carey (with Chris Ring and Rebekah Hannif-Ali), Navigant Construction Forum, December 2015.

Trials, Tribulations and Turmoil in Crude Oil Markets, Association of Corporate Counsel, Nov. 24, 2015.

Near Term Energy Market Dynamics and the Clean Power Plan, Western Coal Traffic League Fall Meetings, Julie Carey (with Maggie Shober), November 19, 2015.

The Impact of Crude Oil and Natural Gas Market Trends on Litigation, Energy Litigation Journal (ABA Section), Julie M. Carey (with Bob Broxson and Sonya Kwon), November 2015.

Today's Energy Market and the Cost of Artificially Suppressing Demand with the Crude Oil Export Ban, Kelley, Drye, and Warren, Energy Regulatory Conference, October 22, 2015.

Regulation and Competition in Oil Pipelines and Related Industries, Association of Oil Pipelines Business Conference, Julie Carey (with Julie Solomon), September 17, 2015.

Evaluation of the Economic Contributions of Littoral Combat Ship (LCS) Program, Lockheed Martin Corporation, Julie M. Carey (with Kate Rodenrys), January 7, 2015 (Supplemented December 2015).

Economic Impact Assessment Study of Enbridge Line 3 Replacement Program; National Energy Board Application, Hearing Order OH-002-2015, November 5, 2014. (OF-Fac-Oil-E101-2014-11 01)

An Analysis of a Refined Product Pipeline Competitive Tariff Rates and of the Current Competitiveness of the Refined Product Pipelines Market-Based Rate Markets, Confidential Report, Julie M. Carey (with Kate Rodenrys and George Schink), June 9, 2014.

Low Crude Oil Price Impacts: Market Dynamics, Economic Implications and Disputes, Texas Lawyers Houston, Julie Carey (with Robert Lang), May 21, 2015.

Rising Tide: Litigation Wave from Low Oil Prices & Economic Implications, Texas Lawyers- Dallas, Julie Carey (with Robert Lang), May 8, 2015.

What Is the Future of the Long-Delayed Keystone XL Pipeline? Inter-American Dialogue's Latin America Advisor – Energy, May 5, 2014.

Enforcement Shifts Energy-Trading Strategies, Energy Litigation Journal (ABA Section), Julie M. Carey (with Cliff Hamal and Ben Ullman), March 2014.

Energy Commodity Trading's Evolving Regulatory Frontier, Natural Gas Notes, January 2014.

Oil Pipeline Regulation and Competition, Confidential White Paper for the Association of Oil Pipe Lines, Julie Carey (with George Schink, Rick Smead, and Julie Solomon), August 2013.

Report on the Preliminary Analysis of the Potential Competition Faced by a Reversed Crude Oil Pipeline and Competition Faced by an Existing System, Confidential Report, Julie Carey (with Kate Rodenrys and George Schink), June 24, 2013.

Trading Firms in the Bullseye Amid Stepped Up Oversight of Energy Markets, *Forbes*, October 11, 2013.

Rail Emerging as Long-Term North American Crude Option, Oil and Gas Journal, August 5, 2013.

Report on the Preliminary Analysis of the Competition Faced by a Crude Oil Pipeline System, Confidential Report, Julie Carey (with Kate Rodenrys and George Schink), June 7, 2013.

How Unconventional Oil and Gas Is Supercharging the U.S. Economy, Forbes (online), December 13, 2012.

Unconventional Resources, Economic Growth and Power Generation Implications, Julie M. Carey, PowerGen Conference, Orlando, Florida, December 13, 2012.

Surprise Side Effect of Shale Gas Boom: A Plunge in U.S. Greenhouse Gas Emissions, Forbes, December 7, 2012.

The Economics of Unconventional Oil and Gas, North American Gas Summit, Julie M. Carey, November 15, 2012.

The Unconventional Path for Domestic Crude Oil and Natural Gas Resources, U.S. Association for Energy Economists Dialog, Julie M. Carey and Christopher L. Ring, September 2012.

Shale Gas and Oil: Economy-Wide Game Changers, Natural Gas Notes, August 1, 2012.

The Renewable Transformation and Nine Trends to Watch For, Julie Carey (with Cliff W. Hamal), US Association for Energy Economists Dialog, November 2010.

Clean Energy Policy Initiative Impacts on the Environment and the Economy, Confidential Client Report, May 2009.

Strategic Recommendations for Expiring Power Contracts, Confidential Report, Julie Carey (with Cliff W. Hamal), Prepared on Behalf of Ontario Power Authority, January 22, 2009.

Force Majeure Risks and Ontario Power Authority's Power Contracts, Julie Carey (with Cliff W. Hamal), Prepared on Behalf of Ontario Power Authority, March 31, 2008.

Financial Accommodation for Force Majeure Events, Julie Carey (with Cliff W. Hamal), Prepared on Behalf of Ontario Power Authority, January 21, 2008.

Attachment 2: Bremser CV

NERA
ECONOMIC CONSULTING

Dr. Albert W. Bremser
Associate Director

NERA Economic Consulting
1255 23rd Street NW, Suite 600
Washington, DC 20037
Tel: +1 202 466 9222
al.bremser@nera.com
www.nera.com

ALBERT W. BREMSER, Ph.D., CFA

Dr. Bremser is a financial economist who has a Ph.D. in Finance and is a Chartered Financial Analyst® (CFA®) charterholder. He has more than 20 years of experience providing expert services involving primarily the energy industry (regulated and unregulated) in different areas such as electric generation, electric transmission, and pipelines (crude oil, refined products, NGLs and natural gas). Dr. Bremser has testified as an expert witness before the Federal Energy Regulatory Commission and the Public Service Commission of Wisconsin. Dr. Bremser applies economic, finance, accounting, and quantitative principles to those matters, which also includes regulatory principles and practices such as those of the Federal Energy Regulatory Commission.

Prior to his current private sector position, Dr. Bremser was an expert witness with the US Federal Government at the Federal Energy Regulatory Commission (FERC) in the Office of Administrative Litigation as a member of FERC Trial Staff from 2015 to 2019. While at FERC, he was involved in energy issues for electric transmission, electric generation, electric generator-based reactive power, and crude oil pipelines issues (tariff rate and non-rate tariff issues in settlement and hearing proceedings). On behalf of FERC Trial Staff, Dr. Bremser testified as an expert witness on energy related issues through written testimony, cross-examination at hearing and deposition.

In the private sector, Dr. Bremser has experience with electricity market services (i.e., energy, ancillary services), market rules and business processes for certain wholesale electric markets. Dr. Bremser has experience with certain rate matters involving wholesale electric rates and wholesale transmission rates. Dr. Bremser has testified as an expert witness on certain energy issues before the Public Service Commission of Wisconsin (written testimony), and FERC (affidavit).

In the private sector, Dr. Bremser has also worked on many regulatory engagements involving crude oil, refined product (gasoline, diesel, jet fuel) and natural gas liquid (NGL) pipelines and their tariff rate and non-rate tariff issues. Tariff rate issues include cost-of-service tariff rates, settlement tariff rates, market-based rate authority, grandfathered rates, indexing, uncommitted rates and committed rates. Non-rate tariff issues include proration policies, FERC Form No. 6 (annual financial report), and petition for declaratory order (FERC) for rate design. Dr. Bremser also has experience with natural gas pipelines and natural gas storage involving the acquisition of assets and ownership interests.

In addition, Dr. Bremser has assisted clients with economic analysis for commercial disputes. He has analyzed merchant electricity generation, natural gas storage, spent nuclear fuel and crude oil contracts for economic damages in proceedings involving alleged breach of contract. Dr. Bremser has experience with MTBE gasoline and underground storage tanks, and solar panels in the context of economic damages analysis not related to an alleged breach of contract.

Dr. Bremser has taught finance courses at Virginia Tech. He has published articles in the *Journal of Legal Economics*. He has also made presentations on various energy topics.

EDUCATION

- **Virginia Tech**
  Ph.D. in Finance, 1997.

- **University of Pittsburgh**
  Master of Business Administration, 1992.

- **University of Virginia**
  Bachelor of Science, Commerce, 1989.
  Concentrations in Finance and Management Information Systems.

EDUCATION (NON-DEGREE)

- **Northern Virginia Community College**
  Accounting Career Studies Certificate, 2017.
  The accounting courses taken meet the accounting course requirements of the Virginia Board for Accountancy to take the Certified Public Accountancy (C.P.A.) examination.

- **Harvard Law School, Executive Education from the Harvard Negotiation Institute**
  Negotiation Workshop: Improving Your Negotiating Effectiveness; taught by Bruce Patton - co-founder of the Harvard Negotiation Project (part of the Program on Negotiation). One week all day course. 2016.

- **Chartered Financial Analyst (CFA) exam curriculum**
  Passed Exams 1, 2 and 3. 1999-2001.

PROFESSIONAL EXPERIENCE

2019-Present	**NERA Economic Consulting** – Senior Consultant (2019-2021); Associate Director (2022-Present)
2015-2019	**Federal Energy Regulatory Commission, Office of Administrative Litigation (Washington, DC) –** Energy Industry Analyst (Litigation)
2013-2015	**Bremser Finance and Economics (Vienna, VA) -** Principal
2011-2013	**Exponent (Alexandria, VA) -** Manager
2009-2011	**Bremser Finance and Economics (Vienna, VA) -** Principal
1999-2009	**LECG, Inc. (Washington, DC) –** Senior Consultant, Managing Consultant, Senior Managing Consultant
1997-1999	**KPMG, Economic Consulting Services (Washington, DC) –** Senior Consultant
1990-1991	**MCI Telecommunications, Revenue Reporting (Arlington, VA) –** Financial Systems Analyst
1989-1990	**Freddie Mac, Loan Administration (Vienna, VA) –** Accountant
1988-1989	**University of Virginia Medical Center, Department of Finance, Property Accounting (Charlottesville, VA) –** Fiscal Technician

PROFESSIONAL DESIGNATIONS AND MEMBERSHIPS

- Chartered Financial Analyst (CFA) charterholder, 2001 – 2016 (discontinued dues payment in 2016), 2019 – present.
- National Capital Area Chapter of the U.S. Association for Energy Economics.
- Energy Bar Association.

PRIMARY AREAS OF GOVERNMENT AND PRIVATE SECTOR CONSULTING EXPERIENCE

ENERGY – REGULATED AND UNREGULATED (FERC TRIAL STAFF AND PRIVATE SECTOR)

Electric:

- Electric generator reactive power capability compensation (cost of service; cost allocation) including wind, solar, natural gas fueled (combined cycle; combustion turbine), coal fueled, nuclear fueled, co-generation, hydro and other fuel sources. Testimony on behalf of FERC Trial Staff in a reactive power compensation proceeding for a newly built natural gas fueled power plant.
- Electric transmission rates (cost of service formula rates and stated rates), and cost of capital (including return on equity) for cost of service.
- Regulatory cost of capital including the return on equity (cost of equity). Testimony filed on behalf of FERC Trial Staff in three proceedings (one proceeding is the above listed reactive power compensation proceeding; another proceeding involves an electric transmission revenue requirement; another proceeding involves a wholesale rate for electric generation for a nuclear power plant). While in the private sector, testimony filed on return on equity at the Public Service Commission of Wisconsin on behalf of a private sector company.
- Energy related breach of contract cases involving electricity tolling agreements and spent nuclear fuel.
- Knowledge of certain aspects of PJM, MISO, ERCOT and other RTOs/ISOs.

Pipelines and Other Non-Electric Energy Areas:

- Crude oil, refined product and natural gas liquid (NGL) pipeline FERC (Federal Energy Regulatory Commission) tariff rates (market-based rates, cost of service rates, settlement rates). Testimony in a market-based rate application proceeding on behalf of FERC Trial Staff. An application for the authorization to charge market-based rates is a competition analysis (i.e., calculation of HHIs and other market share metrics). FERC cost of service, cost of service elements, cost allocation and rate design, which includes tariff rate filings and Page 700 (FERC Form No. 6).
- Knowledge of natural gas pipelines and natural gas storage involving the acquisition of assets and ownership interests.
- Energy related breach of contract cases involving natural gas storage and crude oil purchase contacts. Energy related business tort involving MTBE gasoline and underground storage tanks. Energy related dispute involving solar panels.

ECONOMIC DAMAGES

- Breach of contract involving electric generation, natural gas storage, crude oil, mining equipment, and automotive parts.
- Breach of fiduciary duty involving management of investment portfolios and trust management of life insurance policies.
- Economic damages due to alleged false statements involving the sale of solar panels.
- Business torts litigation involving MTBE gasoline and underground storage tanks.
- Securities litigation. Investment portfolios (Institutional and individual investor) - Portfolio trading analysis, calculation of portfolio profit and losses, and benchmark damages. Section 10b-5 (non-class action and class action). Event study analysis.

FINANCIAL, ECONOMIC AND ACCOUNTING ANALYSIS

- Valuation analysis for an arbitration for a railroad.
- Valuation analysis for a railroad regulatory proceeding.
- Option pricing techniques to estimate value for derivate securities and contingent guarantees.
- International trade. Department of Commerce testimony in a countervailing duty matter.
- Intellectual property – patent, trademark, copyright, trade secrets.
- Valuation – power plants, refined product pipelines, biological samples, terms in a settlement agreement.
- Analysis of financial statements, accounting records, and financial and business documents.

UNIVERSITY TEACHING

Virginia Tech - Finance Instructor, College of Business, Department of Finance, Summer 1995, 1996 – 1997. Introductory corporate finance (Summer Session 1995), and real estate finance (Fall Semester 1996 and Spring Semester 1997).

PUBLICATIONS AND DISSERTATION

"Two Essays on Convertible Debt", Ph.D. dissertation, March 1997.

"Calculating a Taxable Damages Award: A Comparison of Two Calculation Methods", *Journal of Legal Economics,* 16(2), April 2010, pp. 1-18.

"Valuation of a Trade Subsidy Using Option Pricing Theory", *Journal of Legal Economics,* 17(2), April 2011, pp. 1-22.

Cantor, R and A. Bremser. "Market Share Liability from an Economics Perspective", *BRG Review*, 4(1), Winter 2014, pp. 4-9.

SELECTED PRESENTATIONS

Presentation on issues in discounting cash flows, presentation to the Western States Petroleum Association (WSPA), South Lake Tahoe, CA, August 2007.

"Lost Profits: Principles, Methods and Strategies to Prove and Defend Damages", presentation for The Knowledge Group, with Richard Eichmann of NERA, October 7, 2019.

"Energy Disputes and Litigation: Effective Strategies and Best Practices for the Year Ahead", presentation for The Knowledge Group, with Julie Carey of NERA, December 5, 2019.

"The Future of the U.S. Renewable Energy Disputes: Decoding Recent Trends and Updates", presentation for The Knowledge Group, with Julie Carey of NERA, March 24, 2020.

"Cost-of-Service and Rate Design for Oil Pipelines", presentation to Bracewell LLP, with Julia Williams of NERA, August 31, 2021.

SELECTED PROFESSIONAL ACTIVITIES

Expert witness for lawyer deposition training at Weil, Gotshal & Manges, New York, NY, January 2020.

Expert witness for lawyer deposition training at Weil, Gotshal & Manges, virtual, December 2020.

DIRECT WRITTEN TESTIMONY

Prepared Direct and Answering Testimony on Behalf of the Trial Staff of the Federal Energy Regulatory Commission (FERC) in FERC Docket No. OR15-6-000, Application of Seaway Crude Pipeline Company LLC to Charge Market Based Rates, March 24, 2016.

Prepared Rebuttal Testimony on Behalf of the Trial Staff of the Federal Energy Regulatory Commission (FERC) in FERC Docket No. OR15-6-000, Application of Seaway Crude Pipeline Company LLC to Charge Market Based Rates, May 26, 2016.

Prepared Answering Testimony on Behalf of the Trial Staff of the Federal Energy Regulatory Commission (FERC) in FERC Docket No. ER17-1821-002, Panda Stonewall, LLC, Section 205 Federal Power Act filing for a proposed Reactive Supply and Voltage Control from Generation and Other Sources Service Tariff (cost of service) under Schedule 2 of the Open Access Transmission Tariff of PJM Interconnection, L.L.C., October 4, 2018.

Prepared Direct and Answering Testimony on Behalf of the Trial Staff of the Federal Energy Regulatory Commission (FERC) in FERC Docket No. ER17-998-001 and EL17-61-001, DATC Path 15, LLC, Section 205 Federal Power Act filing for a proposed stated rate annual transmission revenue requirement pursuant to a settlement agreement, October 16, 2018.

Prepared Supplemental Direct and Answering Testimony on Behalf of the Trial Staff of the Federal Energy Regulatory Commission (FERC) in FERC Docket No. ER17-998-001 and EL17-61-001, DATC Path 15, LLC, Section 205 Federal Power Act filing for a proposed stated rate annual transmission revenue requirement pursuant to a settlement agreement, March 7, 2019.

Prepared Updated Return on Equity Analysis Testimony on Behalf of the Trial Staff of the Federal Energy Regulatory Commission (FERC) in FERC Docket No. ER17-998-001 and EL17-61-001, DATC Path 15, LLC, Section 205 Federal Power Act filing for a proposed stated rate annual transmission revenue requirement pursuant to a settlement agreement, April 12, 2019.

Prepared Direct and Answering Testimony on Behalf of the Trial Staff of the Federal Energy Regulatory Commission (FERC) in FERC Docket No. EL17-41-001, Arkansas Public Service Commission, Mississippi Public Service Commission v. System Energy Resources, Inc., and EL18-142-000 (consolidated), Louisiana Public Service Commission v. System Energy Resources, Inc., two separate compliant cases (consolidated for hearing) under Section 206 of the Federal Power Act regarding the return on equity used in System Energy Resources, Inc.'s cost of service formula rate for wholesale electric power, May 1, 2019.

Prepared Direct Testimony on Behalf of Verso Corporation and Verso Minnesota Wisconsin LLC in Public Service Commission of Wisconsin Docket No. 1330-ER-104, Application of Consolidated Water Power Company, as an Electric Public Utility, for Authority to Adjust Electric Rates, October 6, 2020.

Prepared Rebuttal Testimony on Behalf of Verso Corporation and Verso Minnesota Wisconsin LLC in Public Service Commission of Wisconsin Docket No. 1330-ER-104, Application of Consolidated Water Power Company, as an Electric Public Utility, for Authority to Adjust Electric Rates, October 20, 2020.

Prepared Sur-rebuttal Testimony on Behalf of Verso Corporation and Verso Minnesota Wisconsin LLC in Public Service Commission of Wisconsin Docket No. 1330-ER-104, Application of Consolidated Water Power Company, as an Electric Public Utility, for Authority to Adjust Electric Rates, October 26, 2020.

CROSS-EXAMINATION TESTIMONY AT HEARING

Offered for Cross-Examination on Behalf of the Trial Staff of the Federal Energy Regulatory Commission (FERC) in FERC Docket No. OR15-6-000, Application of Seaway Crude Pipeline Company LLC to Charge Market Based Rates, July 7, 2016.

Offered for Cross-Examination on Behalf of the Trial Staff of the Federal Energy Regulatory Commission (FERC) in FERC Docket No. ER17-1821-002, Panda Stonewall, LLC, Section 205 Federal Power Act filing for a proposed Reactive Supply and Voltage Control from Generation and Other Sources Service Tariff (cost of service) under Schedule 2 of the Open Access Transmission Tariff of PJM Interconnection, L.L.C., November 7 and 8, 2018.

Offered for Cross-Examination on Behalf of the Trial Staff of the Federal Energy Regulatory Commission (FERC) in FERC Docket No. ER17-998-001 and EL17-61-001, DATC Path 15, LLC, Section 205 Federal Power Act filing for a proposed stated rate annual transmission revenue requirement pursuant to a settlement agreement, May 7 and 8, 2019.

DEPOSITION TESTIMONY

Deposition on Behalf of the Trial Staff of the Federal Energy Regulatory Commission (FERC) in FERC Docket No. ER17-1821-002, Panda Stonewall, LLC, Section 205 Federal Power Act filing for a proposed Reactive Supply and Voltage Control from Generation and Other Sources Service Tariff (cost of service) under Schedule 2 of the Open Access Transmission Tariff of PJM Interconnection, L.L.C., October 23, 2018.

Deposition on Behalf of the Trial Staff of the Federal Energy Regulatory Commission (FERC) in FERC Docket No. EL17-41-001, Arkansas Public Service Commission, Mississippi Public Service Commission v. System Energy Resources, Inc., and EL18-142-000 (consolidated), Louisiana Public Service Commission v. System Energy Resources, Inc., two separate compliant cases (consolidated for hearing) under Section 206 of the Federal Power Act regarding the return on equity used in System Energy Resources, Inc.'s cost of service formula rate for wholesale electric power, June 25-26, 2019.

AFFIDAVIT

Joint Affidavit with Julie M. Carey on Behalf of the American Electric Power Service Corporation (Appalachian Power Company, et al), in FERC Docket No. ER11-47-016, et al, Triennial Update for Market-Based Rate Authority for American Electric Power Service Corporation for the Southwestern Power Pool Region, June 30, 2021.

OTHER ORAL TESTIMONY AND EXPERT REPORTS/ANALYSES

Analyses were conducted on portfolio turnover, commissions, portfolio concentration, time securities were held, margin use, calculation of out-of-pocket losses, and calculation of benchmark portfolio damages. Expert analyses were provided to a NASD (National Association of Securities Dealers) Arbitration panel to facilitate mediation. Case settled. 2000.

At hearing, oral rebuttal on behalf of Petitioners to the oral presentation made by Respondents. Department of Commerce, International Trade Administration, Countervailing Duty investigation of certain Durum Wheat (Docket C-122-846) and Hard Red Spring Wheat (Docket C-122-848) from Canada. Petitioners were the North Dakota Wheat Commission (hard red spring wheat), United States Durum Growers (durum wheat), and the Durum Growers Trade Action Committee (durum wheat). Respondents were the Canadian Wheat Board, Government of Canada, Government of Alberta, and Government of Saskatchewan. Hearing was July 8, 2003.

February 28, 2022

Exhibit B

VERIFIED STATEMENT OF ANTHONY DIDEO

I am Anthony DiDeo, Director Joint Facilities with CSX Transportation, Inc. ("CSXT"). The purpose of this statement is to explain that the continuation of the existing Interchange Allowance Agreement effective January 1, 2021 between CSXT and The Kansas City Southern Railway Company ("KCS") (the "2021 Agreement")[1] is necessary to continue competitive rail service in the interchange of traffic in New Orleans, LA.

New Orleans is one of the major gateways in the United States for traffic moving between the east and the west. CSXT and KCS interchange about 50,000 cars per year in New Orleans. CSXT and KCS, and their predecessors, have interchanged traffic in New Orleans since at least 1909. Interchange between CSXT and KCS is facilitated by use of the New Orleans Public Belt Railroad Commission ("NOPB").

In 1985, KCS began to abandon two segments of its line that were integral to the interchange between KCS and CSXT. Through its subsidiary, the Louisiana & Arkansas Railway Company (the "L&A"), KCS sought authority from the Interstate Commerce Commission (the "ICC") to (1) abandon (a) 4,060 feet of its line between milepost 855.60 and milepost 856.37 and (b) 28,375 feet of its line extending between the westerly right-of-way line of Worth Street at milepost 856.78 and the easterly right-of-way line of Turnbull Drive at milepost 862.14; (2) acquire trackage rights (a) over the line of Illinois Central Gulf Railroad Company ("ICG") between Alliance Avenue near Frellsen and East Bridge Junction in Shrewsbury, a distance of approximately five miles in Jefferson Parish, and (b) over those portions of the lines on NOT in Shrewsbury between milepost 0.05-A and milepost 0.09-A and over that portion of New Orleans Terminal Company ("NOT") Track 1-9 between the southwesterly switching point of this line and

[1] See the Agreement in Exhibit A.

the point of connection with L&A, a distance of approximately 352 feet; and (3) construct (a) two connections between its line and the line of ICG, and (b) certain tracks on an easement of NOT. The ICC found that the "relocation of L&A's line does not affect any shippers." *Louisiana & Arkansas Railway Company-Trackage Rights Exemption-Illinois Central Gulf Railroad Company and New Orleans Terminal Company*, ICC Finance Docket No. 30639 (served April 17, 1985). CSXT and KCS were still able to interchange through NOPB.

In 2006, KCS sought to abandon a 0.71-mile segment of the former L&A main line that was relocated to an ICG Line. The segment abandoned was between milepost 862.14 (near Turnbull Drive) and Milepost 862.85 (near Causeway Blvd.). KCS certified that no local traffic has moved for at least two years and that any overhead traffic can be rerouted. *The Kansas City Southern Railway Company-Abandonment Exemption-Line in Jefferson Parish, LA*, STB Docket No. AB-103 (Sub-No. 20X) (served June 5, 2006). This abandonment increased the length of haul and eliminated the ability for CSXT and KCS to directly interchange via CSXT's trackage rights over NOT.

For several years prior to 2006 CSXT paid NOPB { } per car for westbound intermediate switch to KCS. In 2006 and 2007 NOPB unilaterally increased their rate multiple times to { }, { }, { }, and { } per car. These increased charges to CSXT led to negotiations resulting in several agreements. By 2009 KCS had entered into an agreement with NOPB whereby KCS paid for both sides of the intermediate switch expense. From 2009-2020 KCS was responsible for this expense. Most recently, the 2021 Agreement, where KCS agreed to pay NOPB to handle cars interchanged from CSX to KCS and cars interchanged from KCS to CSX during the term of this Agreement." Section 2. In Section 3, CSXT agreed to "pay KCS an

interchange allowance of" {)} "for each car interchanged via NOPB from CSX to KCS." This was a reasonable commercial resolution between CSXT and KCS.

However, Section 6 provides:

> This Agreement shall remain in effect for one (1) year from the Effective Date (the "Initial Term"), and shall automatically renew thereafter annually on each anniversary of the Effective Date for an additional one-year term ("Renewal Term"). **Notwithstanding the provisions of the preceding sentence, either Party may terminate this Agreement for any reason during either the Initial Term or a Renewal Term by providing the other Party with thirty (30) days' advance written notice.** (emphasis in original)

CSXT is not asking that the economic underpinnings of the Agreement be modified. CSXT requests that the Board to modify the termination provision of Section 6 to replace "either Party may" with "upon mutual agreement, the Parties may" "terminate this Agreement...."

Unilateral termination of the Agreement by KCS would certainly adversely affect shippers who rely on service from CSXT, contrary to the conclusion of the ICC in Finance Docket No. 30936, termination of the Agreement would result in the rerouting of traffic to a more circuitous route or continuing the current routing of traffic, but with CSXT being charged a significantly higher interchange allowance, which most likely would be passed on the shippers. Either action by KCS would harm shippers.

The acquisition of control of KCS by Canadian Pacific Railway Limited ("Canadian Pacific") will significantly increase the fixed charges (interest on debt and increased dividend payments because of the issuance of approximately 265,000,000 shares of Canadian Pacific common stock) incurred by Canadian Pacific. Canadian Pacific has also been forthright in its plan to divert significant traffic from other railroads, including rerouting traffic from New Orleans to the Meridian Speedway, and to reduce costs, which could include imposing its existing costs on other railroads. Keeping the Agreement in effect for the long term will maintain the status quo by

continuing another competitive option for rail traffic moving between points in the southwest and southeast and other parts of the country, and provide shippers with an existing efficient and economical routing over New Orleans.

CSXT respectfully requests that the Board exercise its power to preempt agreements and revise the Agreement as requested by CSXT.

VERIFICATION

I, Anthony DiDeo, declare under penalty of perjury under the laws of the United States that the foregoing is true and correct. Further, I certify that I am qualified and authorized to file this statement.

Executed the 28th day of February, 2022.

Anthony DiDeo

EXHIBIT A

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Interchange Allowance Agreement
Between CSX Transportation, Inc., and
The Kansas City Southern Railway Company

This Interchange Allowance Agreement ("Agreement") is effective January 1, 2021 ("Effective Date") between CSX Transportation, Inc. ("CSX") and The Kansas City Southern Railway Company ("KCS") (CSX and KCS being sometimes referred to herein individually as a "Party" or together as the "Parties").

Recitals

WHEREAS, CSX and KCS interchange rail traffic in New Orleans, but lack a direct connection between the Parties' tracks in New Orleans; and

WHEREAS, the Parties have utilized the services of the New Orleans Public Belt Railroad Commission for the Port of New Orleans ("NOPB") to move between their respective yards cars being interchanged from one Party to the other Party at New Orleans; and

WHEREAS, NOPB has substantially increased its charges, effective January 1, 2021, for handling cars interchanged between the Parties;

NOW, THEREFORE, the Parties, in order to maintain interchange at New Orleans to meet customer needs, enter this Agreement to allocate between them a portion of the increased cost of their interchange.

Agreement

1. The foregoing recitals are hereby incorporated as substantive terms of this Agreement.

2. KCS agrees to pay NOPB to handle cars interchanged from CSX to KCS and cars interchanged from KCS to CSX during the term of this Agreement.

3. CSX agrees to pay KCS an interchange allowance of
for each car interchanged via NOPB from CSX to KCS (the "Interchange Allowance") during the term of this Agreement. Following the end of each month NOPB has agreed to e-mail the Parties a list of all cars interchanged from CSX to KCS via NOPB in that month. KCS shall then invoice CSX by e-mail for the total number of cars in said list, multiplied by the Interchange Allowance. CSX shall pay KCS's Interchange Allowance invoice within thirty (30) days of the date it is issued.

4. The Interchange Allowance shall be adjusted annually by an amount equal to

Such percentage changes shall be determined by the ratio of the index for the third quarter (Q3) of the current calendar year versus the third quarter (Q3) of the previous calendar year. This percentage adjustment will be applied annually on the anniversary of the Effective Date. The Interchange Allowance cannot be adjusted negatively below the original rate In the event the Surface Transportation Board no longer publishes the RCAF-U, the Parties will

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agree upon an alternative index or, in the absence of such agreement, apply the annual indexes of charge-out prices and wage rates published by the Association of American Railroads.

5. The Parties agree to work expeditiously to complete mutually-satisfactory arrangements for an interchange of traffic between them at Montgomery, AL via the Meridian & Bigbee Railroad, L.L.C., with the intent of shifting interchange of cars currently interchanged between the Parties at New Orleans or other interchanges to Montgomery when consistent with customers' and the Parties' needs.

6. This Agreement shall remain in effect for one (1) year from the Effective Date (the "Initial Term"), and shall automatically renew thereafter annually on each anniversary of the Effective Date for an additional one-year term ("Renewal Term"). **Notwithstanding the provisions of the preceding sentence, either Party may terminate this Agreement for any reason during either the Initial Term or a Renewal Term by providing the other Party with thirty (30) days' advance written notice.** All notices under this Agreement shall be sent by United States registered or certified mail, or by a national overnight courier service such as (but not limited to) FedEx or UPS, to each Party's respective designated contact, as provided below and shall be deemed effective upon receipt.

For KCS: Mike Naatz, Executive Vice President
The Kansas City Southern Railway Company
427 West 12th Street
Kansas City, MO 64105-1403

For CSX: Anthony DiDeo, Director Joint Facilities
CSX Transportation, Inc.
500 Water Street, J801
Jacksonville, FL 32202

Each Party shall be responsible for immediately notifying the other Party in writing of any change in its respective designated contact during a term of this Agreement. Failure to do so shall not nullify the effectiveness of any notice properly delivered to the address provided to the previously designated contact.

[*Remainder of this page intentionally left blank; Signatures appear on the following page*]

IN WITNESS WHEREOF, the Parties, intending to be legally bound, have executed this Agreement by their duly-authorized officers.

CSX Transportation, Inc.

DocuSigned by:
By: Tom Tisa
ED2A12E621CC43B...

Tom Tisa
(Printed name)

Head of Business Development
(Title)

1/15/2021 | 10:17 AM CST
(Date)

The Kansas City Southern Railway Company

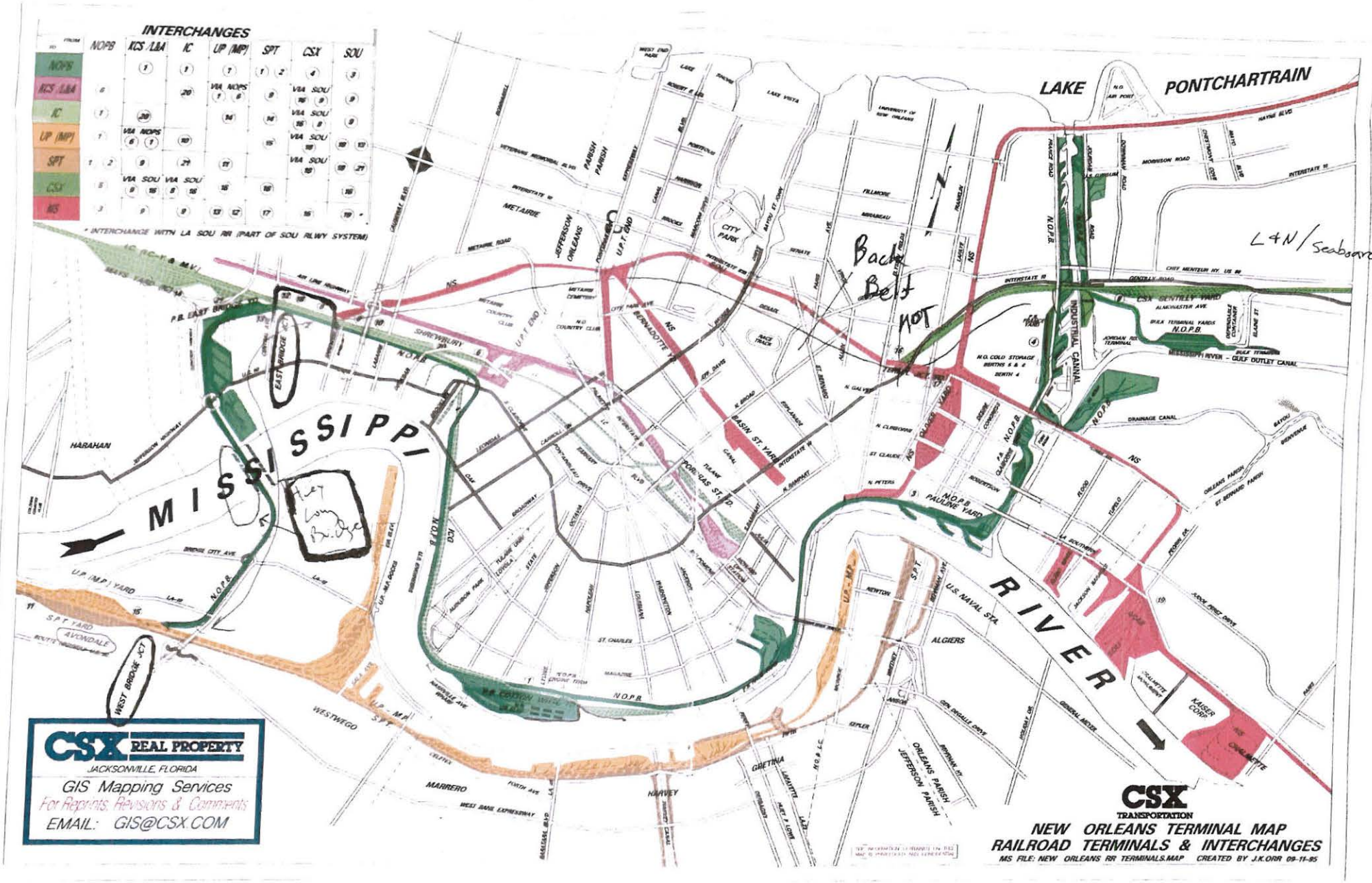
DocuSigned by:
By: Michael Naatz
FD5BF2DEC92345C...

Michael Naatz
(Printed name)

EVP
(Title)

1/18/2021 | 8:29 AM CST
(Date)

EXHIBIT B - MAP


INTERCHANGES
NOPB
KCS /L&A
IC
UP (MP)
SPT
CSX
NS
* INTERCHANGE WITH LA SOU RR (PART OF SOU RLWY SYSTEM)
LAKE PONTCHARTRAIN
MISSISSIPPI RIVER
Back Belt
HOT
L&N/Seaboard
Hey Long Bridge
EAST BRIDGE JCT
WEST BRIDGE JCT
HARAHAN
METAIRIE
JEFFERSON PARISH
ORLEANS PARISH
CITY PARK
BASIN ST. YARD
PORTRAS ST. YD.
INDUSTRIAL CANNAL
CSX GENTILLY YARD
N.O.P.B. PAULINE YARD
U.S. NAVAL STA.
ALGIERS
KAISER CORP.
WESTWEGO
MARRERO
HARVEY
GRETNA
ORLEANS PARISH
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CSX TRANSPORTATION
NEW ORLEANS TERMINAL MAP
RAILROAD TERMINALS & INTERCHANGES
MS FILE: NEW ORLEANS RR TERMINALS.MAP CREATED BY J.K.ORR 09-11-95

Exhibit C

VERIFIED STATEMENT OF ANTHONY DIDEO

I am Anthony DiDeo, Director Joint Facilities with CSX Transportation, Inc. ("CSXT"). The purpose of this statement is to describe the potential for reduced competition for traffic moving between Kansas City and the East.

As part of the cost savings projected by Canadian Pacific Limited ("CP") in seeking authority to obtain control of the Kansas City Southern Railway Company ("KCSR") and its railroad subsidiaries, CP intends to downgrade the KCS railroad line between Kansas City and East St. Louis (the "KC-ESTL Line") and to divert traffic from that line to the CP line running between Kansas City and Chicago. The KC-ESTL Line between Kansas City and its interchange with CSXT in East St. Louis is a significant competitive route for traffic moving between the East served by CSXT and Kansas City. Today competition exists between the single-line route between Kansas City and points in the East over the Norfolk Southern Railway Company ("NSR") and the joint-line CSXT-KCS route over East St. Louis. The downgrading of the KC-ESTL Line and diversion of traffic to Chicago, as proposed by CP will reduce the level of competition NSR faces for traffic to and from Kansas City. The downgrading and diversion will result in slower trains and lower volumes that will degrade service and reduce competition with NSR.

{

}

To avoid this reduction in competition, CSXT requests that the Board impose the following conditions on the CP control of KCS:

1. Require CP to maintain the KC-ESTL Line in the same or better condition than it is currently.
2. Provide an open gateway on reasonable commercial terms as determined by CP and CSXT in order to allow the KC-ESTL Line and CSXT routes to and from the East to compete with NSR.

VERIFICATION

I, Anthony DiDeo, declare under penalty of perjury under the laws of the United States that the foregoing is true and correct. Further, I certify that I am qualified and authorized to file this statement.

Executed the 28th day of February, 2022.

Anthony DiDeo

Exhibit G

CN-13, FD 36500
PUBLIC VERSION

BEFORE THE
SURFACE TRANSPORTATION BOARD

STB Finance Docket No. 36500

CANADIAN PACIFIC RAILWAY LIMITED; CANADIAN PACIFIC RAILWAY COMPANY; SOO LINE RAILROAD COMPANY; CENTRAL MAINE & QUEBEC RAILWAY US INC.; DAKOTA, MINNESOTA & EASTERN RAILROAD CORPORATION; AND DELAWARE & HUDSON RAILWAY COMPANY, INC. – CONTROL – KANSAS CITY SOUTHERN, THE KANSAS CITY SOUTHERN RAILWAY COMPANY, GATEWAY EASTERN RAILWAY COMPANY, AND THE TEXAS MEXICAN RAILWAY COMPANY

CN'S COMMENTS ON APPLICATION AND REQUEST FOR CONDITIONS

Sean Finn
Olivier Chouc
CN
935 de La Gauchetière Street West,
16th Floor
Montreal, QC H3B 2M9
CANADA

Kathryn J. Gainey
CN
601 Pennsylvania Ave, NW
Suite 500, North Building
Washington, DC 20004
(202) 347-7840
Kathryn.gainey@cn.ca

Raymond A. Atkins
Terence M. Hynes
Matthew J. Warren
Sidley Austin LLP
1501 K Street, N.W.
Washington, DC 20005
(202) 736-8000
ratkins@sidley.com

Counsel for Canadian National Railway Company, Grand Trunk Corporation, and CN's Rail Operating Subsidiaries

Dated: February 28, 2022

TABLE OF CONTENTS

EXECUTIVE SUMMARY 1

I. THE APPLICATION IS RIDDLED WITH ERRORS, INCONSISTENCIES, AND FLAWED ASSUMPTIONS THAT CANNOT PROVIDE A BASIS FOR THE BOARD TO FIND THAT THE MERGER IS CONSISTENT WITH THE PUBLIC INTEREST. 16

A. Applicants' Projected Traffic Diversions and Revenue Projections Are Grossly Exaggerated and Invalid. 17

B. Applicants' Operating Plan Is "Essentially Meaningless." 23

C. Applicants' Financial Plan Is Inadequate and Understates Operating Costs by More Than $2.0 Billion. 28

II. APPLICANTS' ASSERTED BENEFITS ARE VASTLY OVERSTATED & UNSUPPORTED. 33

A. Traffic Diversions and Private Profits Are Not Public Benefits. 33

B. Applicants' Assumed Public Benefits Are Unsupported and Overshadowed by the Significant Risks of the Proposed Merger. 35

III. THE APPLICATION DOWNPLAYS THE SERIOUS PUBLIC INTEREST RISKS OF THE PROPOSED MERGER. 37

A. The Net Competition Benefits of the Proposed Transaction Are Negative Unless Remedial Conditions are Proposed. 37

1. A combined CP-KCS is not a "pure" end-to-end merger and raises significant horizontal competition concerns. 37

2. CP's acquisition of KCS will fundamentally undermine KCS's existing incentives to interchange traffic with other railroads on commercially reasonable terms 45

3. CP's pre-merger actions to foreclose competition from KCS raise serious concerns. 51

B. The Application's Inadequate and Unreliable Operating Plan Poses A Serious Risk to the Post-Merger Service of CPKC and Other Rail Carriers. 53

C. Applicants' Unsubstantiated Growth Synergies, Combined with CP's Plan to Not Reduce Earnings, Poses Significant Public Interest Risks. 59

IV. CONDITIONS ARE NECESSARY TO ENSURE THE PUBLIC INTEREST IS PROTECTED. 64

A. If the Board Approves the Merger, It Should Order Divestiture of the Springfield Line to CN as a Condition of the Merger 64

B. The Board Should Impose Conditions Needed to Prevent a Combined CP-KCS from Engaging in Foreclosure. 68

C. Applicants Should Be Required to Provide A Service Assurance Plan or Its Equivalent. 76

CONCLUSION..... 77

EXHIBIT 1: Verified Statement of David T Hunt

EXHIBIT 2: Verified Statement of Carl Van Dyke

EXHIBIT 3: Verified Statement of Hugh Randall

EXHIBIT 4: Verified Statement of Mark E. Zmijewski

EXHIBIT 5: Excerpts from Transcript of February 4, 2022 Deposition of John Brooks

EXHIBIT 6: Excerpts from Transcript of February 7, 2022 Deposition of W. Robert Majure, Ph.D.

EXHIBIT 7: Excerpts Transcript of February 18, 2022 Deposition of Raymond A. Elphick and John F. Orr

EXHIBIT 8: Excerpts from Transcript of February 22, 2022 Deposition of Patrick J. Ottensmeyer

EXHIBIT 9: Excerpts from 2016 KCS Annual Report

EXHIBIT 10: Excerpts from 2017 KCS Annual Report

EXHIBIT 11: December 3, 2019 Gibson Energy Press Release

EXHIBIT 12: Excerpts from October 20, 2020 KCS Board of Directors Meeting Slides

EXHIBIT 13: Excerpts from February 4, 2021 KCS Board of Directors Meeting Materials

EXHIBIT 14: June 3, 2021 CN-KCS Presentation Slides, Bernstein's 37th Annual Strategic Decisions Conference

EXHIBIT 15: Excerpts from Canadian Pacific Railway Limited Form F-4 Registration Statement, filed with the Securities and Exchange Commission on October 1, 2021

EXECUTIVE SUMMARY

Applicants claim that a combined CP-KCS will deliver massive pro-competitive benefits, while causing no competitive harm, and they assert that joining their networks would generate substantial operating efficiencies, without any risk of harm to service.[1] Based on this rosy picture, Applicants choose not to offer meaningful protective conditions.

Applicants' position is flatly inconsistent with their own prior advocacy. For example, after CP spent much of 2021 raising alarms about the competitive risks of mergers involving parallel lines (and claiming that even a proposed divestiture of a parallel line would be insufficient to mitigate competitive harm), Applicants simply ignore the fact that KCS's Springfield Line is parallel to CP's north-south mainline. Applicants not only fail to propose conditions to remedy this loss of horizontal competition, they entirely abandon KCS's prior plans to invest in the line to improve track speeds to better compete with trucks and propose no merger-related capital investment in it.

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[1] Railroad Control Application, *Canadian Pacific Railway, et. al.—Control—Kansas City Southern, et al.*, STB Docket No. FD 36500 (filed Oct. 29, 2021) ("Application"), Vol. 1, at 1 § 1180.6 ("The CP/KCS combination presents a once-in-a-lifetime opportunity to inject new and invigorated competition into North-South transportation corridors connecting the United States, Mexico, and Canada, supporting U.S. and North American economic growth. The Transaction is unambiguously and uniformly beneficial for competition and the public interest."); *id.* at 11 § 1180.6(a)(2)(i) ("The Transaction will generate competitive benefits and cause no competitive harm."); *id.*, Verified Statement of Keith Creel ¶ 28 ("CP/KCS will enhance competition against the larger Class I railroads in the central United States and do so without harming competition anywhere.").

Applicants concede they must offer gateway protections to address the well-recognized risk of vertical foreclosure from Applicants' obvious incentive to favor single-line CP-KCS movements over participation in joint-line movements with other railroads. The Application, however, proposed only an ill-defined gateway commitment, without specifying the locations at which it would apply, an enforcement mechanism, or any limitation on what "commercially reasonable" rates the proposed condition would permit Applicants to charge (short of a maximum reasonable rate as determined in a rate reasonableness case).

Moreover, Applicants present no evidence that they have adequately considered – much less planned for – the types of implementation-related service disruptions that have plagued multiple recent rail mergers. They appear to have forgotten their pledge to provide "all the information [the Board] needs to satisfy itself that Applicants have carefully planned for the integration of these railroads and will implement measures to monitor and adjust service levels during the integration process so that shippers' service levels are safeguarded . . ."[2] Indeed, they do not propose any future Board oversight of their merger, despite the fact that such oversight has been a standard condition in prior major mergers and that CP

[2] Applicants' Reply to Objections to KCS Waiver from 2001 Major Merger Rules, *Canadian Pacific Railway, et. al.—Control—Kansas City Southern, et al.*, STB Docket No. FD 36500, at 19 (filed Apr. 12, 2021) ("Applicants' Reply to Objections to KCS Waiver").

itself has advocated for oversight in connection with a recent *significant* transaction.[3]

Applicants' request for a virtually unconditioned merger would be inappropriate even if their Application had made a compelling, well-supported case demonstrating that their merger was clearly in the public interest. But they have not come close to doing so. The Application is riddled with errors, omissions, inconsistencies, and plainly unreasonable assumptions.

For example, Applicants' Base Year Operating Plan is not based on their traffic or operations during the "Base Year" that they selected (and the Board accepted).[4] Instead, it is based on a single month of unrepresentative traffic data from disparate (and inconsistent) time periods, with arbitrary alterations, and the CP and KCS train service plans that were in effect during the 1st Quarter of 2021. Further, neither Applicants' operating expense estimates nor their financial *pro formas* are based on their Operating Plan. Rather, those exhibits are based on a spreadsheet of operating statistics untethered to Applicants' Operating Plan and unsupported by any other record evidence. Applicants' traffic diversion estimates are similarly full of errors and invalid assumptions. For example, the single largest "revenue synergy" they identify—accounting for {{Redacted Redacted}} of their alleged

[3] Canadian Pacific's Comments to Application, *CSX Corporation and CSX Transportation, Inc., et al.—Control and Merger—Pan Am Systems, Inc., et al.*, STB Docket No. FD 36472, at 27–28 (filed Aug. 27, 2021) (requesting indefinite oversight).

[4] *See* Decision No. 11, *Canadian Pacific Railway Ltd.—Control—Kansas City Southern, et al,*, STB Docket No. FD 36500 (STB served Nov. 23, 2021).

merger-related synergies—is for a movement from a crude oil facility *that Applicants had already contracted with the shipper to move in joint CP-KCS service before the merger was contemplated.* Redacted

} He Redacted

} Finally, Applicants publicly disavowed their own density charts in January 2022, claiming that it would be a "misrepresentation" to use them to identify projected density changes on CPKC lines.[8] Based on these and other errors, the Board cannot rely on the Application in evaluating this proposed transaction.

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[5] Exhibit 8, Excerpts from Transcript of February 22, 2022 Deposition of Patrick J. Ottensmeyer ("Ottensmeyer Dep."), at 88:11–90:13.

[6] *Id.* at 89:9–16.

[7] *Id.* at 88:11–90:13.

[8] *See* Applicants' Reply to Canadian National's Description of Anticipated Responsive Application, *Canadian Pacific Railway Ltd., et al.—Control—Kansas City Southern, et al.*, STB Docket No. FD 36500, at 9, n.7 (filed Jan. 28, 2022) (claiming three times that density figures from Exhibit 14 were "figures presented by CN").

Canadian National Railway Company and its U.S. subsidiaries (referred to collectively herein as "CN") understand that rail mergers that deliver more efficient service and create more effective competition can deliver public benefits to customers—if such mergers are appropriately conditioned to guard against harms to the public interest. That was why CN voluntarily requested that its proposed merger with KCS be reviewed under the Board's current, more stringent merger rules, and publicly committed to conditions to assuage concerns about competitive harm—including a divestiture of a parallel line and a robust gateway commitment with an arbitration remedy, and additional conditions to enhance competition.[9] That was why CN volunteered to comply with the new rules requirement to provide a full Service Assurance Plan and would have complied with the Board's performance of a full Environmental Impact Statement for the proposed CN-KCS merger.[10] Railroads proposing major mergers must commit to real protective

[9] *See* CN Letter, *Canadian Pacific Railway, Ltd., et al.—Control—Kansas City Southern, et al.*, STB Docket No. FD 36500, at 2 (filed Apr. 26, 2021) ("CN will submit an application that fully complies with the current major merger rules."); CN Letter, *Canadian Pacific Railway, Ltd., et. al.—Control—Kansas City Southern, et al.*, STB Finance Docket 36500, at 3 (filed Apr. 23, 2021) ("CN would commit to keep all existing gateways between KCS and other rail carriers open on commercially reasonable terms, including the Kansas City gateway between KCS and CP."); Applicants' Reply to Comments on Proposed Voting Trust Agreement, *Canadian National Railway Company et al.—Control—Kansas City Southern, et al.*, STB Docket No. FD 36514, at 60 (filed July 6, 2021) (noting CN's commitment to "divest the KCS line between Baton Rouge and New Orleans"); *See id.*, Reply Verified Statement of James Cairns at 4 (noting arbitration commitment).

[10] *See* CN Letter, *Canadian National Railway Company et al.—Control—Kansas City Southern, et al.*, STB Docket No. FD 36514, at 1 (filed May 3, 2021) ("CN … is committed to filing an application that includes all elements required by the current merger rules.").

conditions that guard against harms to service, competition, or other aspects of the public interest.

As CN shows herein, the CP-KCS merger will provide far fewer and smaller public benefits than Applicants have represented and will cause competitive harms and operational and service problems that Applicants have ignored. As explained above, the Application itself is replete with material inconsistencies and obvious errors. The Board should require Applicants to make concrete commitments to mitigate the competitive harms and operational and service problems the merger will create, including by imposing conditions on merger approval. Indeed, the numerous errors in Applicants' data and Operating Plan undermine any confidence in the Application's basic assertions.

As the Board is aware, even under the old merger rules, the Board can approve a combination only if it is in the public interest.[11] Congress expressly set a higher bar for major mergers, based on its recognition that a merger of Class I railroads requires a thorough assessment of all relevant factors.[12] Thus, Applicants are required to prove that their proposed combination would benefit the public interest and that these benefits would outweigh any potential harms. That is why

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[11] *See generally Railroad Consolidation Procedures*, 47 Fed. Reg. 9844, 9845 (Mar. 8, 1982); *id.* § 1111.1 (c); Decision No. 44, *Union Pacific Corp., et al. – Control and Merger – S. Pac. Rail Corp., et al.*, STB Docket No. FD 32760, 1 S.T.B. 233, 367 (1999) ("*UP-SP*"); *S. Pac. Transp. Co. v. ICC*, 736 F.2d 708, 712 (D.C. Cir. 1984) ("In deciding whether and what conditions to impose, the Commission's guide is the public interest.").

[12] 49 U.S.C. § 11324(b)–(c).

applicants in successful merger applications, including applications under the old rules, have proven and quantified specific, concrete benefits to the *public*—not simply increases in the railroads' profitability.[13]

Relatedly, the Board has statutory authority to condition its approval of mergers to address competitive and other public-interest concerns.[14] The Board has

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[13] *See, e.g.*, Decision No. 10, *Canadian National Railway Co., et al.—Control—Wisconsin Central Transportation Corp.*, STB Docket No. FD 34000 (STB served Sept. 7, 2001), slip op. at 11–12 (in approving the acquisition, recognizing public benefits such as, "expanded single-line service and other large network advantages," the "availability of a larger supply of well-maintained locomotives and railcars, "cost-saving[s] … without large labor force reductions," "shortened car transit times, increased reliability, and other service improvements and operating efficiencies," and "that CN will remain financially strong after consummation of the transaction[] and … have the financial resources to maintain the integrated CN/WC system in top condition"); Decision No. 89, *CSX Corp. and CSX Transp., Inc. and Norfolk Southern Corp. and Norfolk Southern Ry. Co., et al.—Control and Operating Leases/Agreements—Conrail Inc. and Consolidated Rail Corp.*, STB Docket No. FD 33388, 3 S.T.B. 196, 248–49 (1998) ("*CSX/NS-Conrail*") (recognizing public benefits of more effective competition with trucks, "new and efficient single-line service," "improved service and reduced transit times," over a million truck diversions annually, and "substantial new investments in improving rail infrastructure" of over $1.1 billion "in new rail property and equipment," "reduce[d] … cost[s] of providing transportation by about $1 billion per year," "lower rates," and "improved financial ratios"); *Norfolk Southern Corp.—Control—Norfolk & Western Railway Co. and Southern Railway Co.*, ICC Docket No. FD 29430 (Sub-No. 1), 366 I.C.C. 173, 193–96 (1982) ("carefully distinguish[ing] between public and private benefits" and recognizing "cost reductions," "service improvements," "rate reductions or deferral of rate increases," "faster or more reliable service," and "the railroad industry … becom[ing] stronger, more competitive, and more responsive to the shipping public" as examples of public benefits, in contrast to mere "benefits for the applicants," such as "profits," "raising rates," "reduc[ing] competition," or mere "transfer[s] [of] revenues … without significantly affecting efficiency").

[14] *See* 49 U.S.C. §§ 11324(c),11344(c); *UP-SP*, 1 S.T.B. at 367 (discussing the breadth of the Board's "'broad conditioning power and [] continuing oversight'" of mergers) (quoting *McLean Trucking Co. v. United States*, 321 U.S. 67, 87–88 (1944)); *Grainbelt Corp. v. STB*, 109 F.3d 794, 796 (D.C. Cir. 1997) ("The Commission . . . has broad authority to impose protective conditions to govern

explained that it has "broad power under 49 U.S.C. § 11344(c) to impose appropriate conditions on our approval of railroad consolidations, including those that might be useful in ameliorating potential anticompetitive effects," and that its "overriding concern in the imposition of conditions is the public interest."[15] The Board has not hesitated to deny applications and impose significant conditions where it was concerned about whether public benefits outweighed potential harms, including under its old rules.[16] Further, the Board has cited the importance of lessons learned from mergers under the old rules, which sometimes resulted in substantial harms to service and significant transitional disruptions, indicating it would carefully evaluate the need to address concerns about service, including by requiring concrete commitments from merging railroads.[17]

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mergers."); *CSX/NS-Conrail,* 3 S.T.B. at 250 ("we have used our broad conditioning authority to *preserve or enhance* service and competitive opportunities" (emphasis added)).

[15] *Norfolk Southern Corp.—Control—Norfolk & Western Railway Co. & Southern Railway Co.*, ICC Finance Docket No. 29430 (Sub-No. 1), 366 I.C.C. 173, 235 (1982).

[16] *See, e.g.*, Decision No. 44, *Union Pacific Corp., et al.—Control and Merger—Southern Pacific Rail Corp., et al.*, STB Docket No. FD 32760 (STB served Aug. 12, 1996) (granting extensive BNSF trackage rights to remedy competitive harm); *Santa Fe Southern Pacific Corp.—Control—Southern Pacific Transportation Co.*, ICC Docket No. FD 30400, 3 I.C.C.2d 926, 935–36 (1987) ("Having had the opportunity to examine the complete package that applicants have presented, we think it continues to pose considerable problems.").

[17] *See, e.g.*, Final Rules, *Major Rail Consolidation Procedures*, STB Docket No. EP 582 (Sub-No. 1) (STB served June 11, 2001), slip op, at 20–21 ("Despite the railroads' very strong financial incentives to avoid post-merger service disruptions, despite substantial planning by applicants in conjunction with this agency and the Federal Railroad Administration (FRA), and despite carefully phased and delayed implementation, the *CSX/NS/CR* transaction resulted in severe service problems that plagued applicants and their customers for a full year or more. Moreover, …

Applicants here bear the burden of demonstrating that their combination is in the public interest,[18] but they have not carried it. CN shows in Part I that the Application contains a host of shortcuts, inconsistencies, and material gaps. Based on the content of the Application (and related workpapers), it is not possible to determine whether the merger is in the public interest.

CN shows in Part II that Applicants have failed to quantify, and have significantly overstated, the benefits of the proposed transaction while omitting its significant risks. Applicants simply assume that the mere existence of a CPKC single-line route via Kansas City will automatically result in public benefits—even without adequate, specified capital investments to support anticipated traffic growth and even if the CPKC single-line route is longer or more circuitous than other (cheaper and faster) competitive options. The only quantified benefit in the Application is the merged railroad's anticipated private profits—which are not a public benefit at all. Neither do Applicants' post-merger traffic diversion and revenue estimates constitute public benefits; and, in any event, Applicants'

The [*UP/SP,] UP/CNW[,]* and *BN/SF* transactions were also accompanied by service disruptions …. Thus, it is natural for the Board to be concerned about future mergers in this connection …."); *id.* at 41 (requiring a concrete Service Assurance Plan for major merger proposals to plan for and swiftly address "any potential adverse service effects during implementation").

[18] 49 CFR § 1180.4(c)(8) ("The application must present a *prima facie case*. Applicants can fail to meet their burden of proof and thus not present a prima facie case either by (i) disclosing facts that, even if construed in their most favorable light, are insufficient to support a finding that the proposal is consistent with the public interest, or by (ii) disclosing facts that affirmatively demonstrate that the proposal is not in the public interest. *See Railroad Consolidation Procedures*, 363 I.C.C. 767 (1980).").

predictions are wildly overstated and entirely unreliable. Applicants have also failed to demonstrate that the merger will give rise to any substantial unquantifiable public benefits (such as more efficient routings, increased capacity, capital investment, or improved service). Even if proven, any such modest benefits would be overshadowed by the significant risks and uncertainty created by Applicants' "essentially meaningless"[19] Operating Plan.

The limited capital investments identified in the Application are demonstrably inadequate to support the predicted traffic growth, which would more than double the number of trains on key line segments and at major terminal areas on the CPKC network (including at locations where CPKC must share capacity with other freight carriers and Amtrak). Shockingly, { Redacted

}}[20]

In Part III.A, CN shows the Application also fails to address the merger's severe risks of competitive and other harms to the public interest. The CP-KCS merger presents a significant horizontal competition issue. KCS currently operates a line ("the Springfield Line") that is parallel to CP's line running between Kansas

[19] Exhibit 2, Verified Statement of Carl Van Dyke ("Van Dyke V.S.") at 5.

[20] Exhibit 7, Excerpts from Transcript of February 18, 2022 Deposition of Raymond A. Elphick and John F. Orr ("Elphick/Orr Dep."), at 71–74, 93–97, 152–155.

City and Chicago. The Board recognized in *CN-IC* that the Springfield Line's connection to CN was a viable competitive route, but it has been less used in recent years. Despite KCS's recent pre-merger statements that this line could be a "Kansas City Speedway" competing for north-south traffic with routes like the CP line,[21] the Application abandons this plan, and instead anticipates no increased investment in the Springfield Line.

An unconditioned merger would permanently eliminate the Springfield Line as a competitive alternative, instead favoring the parallel CP line. The Board should condition approval of the merger on divestiture of the Springfield Line so that CN can preserve and upgrade the route and turn it into a high speed, efficient route—competing for traffic not only between Kansas City and Chicago, but beyond to Detroit and Eastern Canada. This condition can be imposed without impeding a combined CPKC in any way. CN proposes to grant back to KCS haulage rights that will enable KCS to access customers on the Springfield Line. Thus, every customer on the Springfield Line would retain access to KCS, while gaining access to CN, and would benefit from CN's investments in the line. To protect the public interest, merger approval should be conditioned on this targeted divestiture.[22]

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[21] *See, e.g.*, Exhibit 14, June 3, 2021 CN-KCS Presentation Slides, Bernstein's 37th Annual Strategic Decisions Conference ("Bernstein Slides"), at 5 (touting the "Kansas City Speedway – connecting CN's Midwest foothold and the KC region").

[22] Today, CN is separately filing a responsive application seeking divestiture in STB Docket No. FD 36500 (Sub-Nos. 1–4).

Moreover, the merger will reduce routing choices through gateways, by diminishing KCS's existing incentives to interchange traffic with other railroads on commercially reasonable terms. Pre-merger, KCS served as an important neutral interchange partner, providing limited single-line service, and thus had a strong incentive to cooperate neutrally with all connecting railroads to jointly serve shippers that neither could serve individually. Post-merger, KCS will have an incentive to maximize traffic that is exchanged with CP. Applicants' vague promises to keep gateways open provide an insufficient safeguard against this potential loss of competition. Instead, as explained in Parts III.B and IV, merger approval should be conditioned on their concrete commitment to prompt, neutral arbitration of commercially reasonable rates and the provision of service on non-discriminatory terms.

In Part III.B, CN shows that the merger also presents significant risks to the rail network as a whole. Despite Applicants' earlier assurances, the Application does not provide "all the information [the Board] needs to satisfy itself that Applicants have carefully planned for the integration of these railroads and will implement measures to monitor and adjust service levels during the integration process so that shippers' service levels are safeguarded . . ."[23] In fact, the opposite is true. Applicants' witness admitted that the "Service Assurance Group" that he vaguely referenced in his verified statement does not exist, and that Applicants have no plans for public reporting of metrics, Board monitoring, or any of the other

[23] Applicants' Reply to Objections to KCS Waiver, at 19.

key elements of a Service Assurance Plan. The Board should insist on fulfillment of this promise, through provision of a Service Assurance Plan or its equivalent, as a condition of approving the merger, as well as imposing at least five years of post-merger monitoring.

Moreover, as detailed in Part III.C, the Application substantially overstates the financial benefits the merged company will achieve.[24] When the predicted revenue growth fails to materialize, the merged company will have a strong incentive to cut costs, raise prices for shippers, discriminate against interline partners, degrade service, defer investment and maintenance, and spin off assets—exacerbating the risks of harm described above. Respectfully, the Board needs to put safeguards in place through robust conditions that will guard against these harms to the public interest.

For all these reasons, Applicants have not carried their burden of demonstrating that the merger is in the public interest, and it is essential that the Board, at the very least, impose conditions sufficient to mitigate the harms the merger would cause. Specifically, as set forth in Part IV, CN requests that the Board require divestiture of the Springfield Line to CN, require a concrete gateway commitment including neutral arbitration of disputed rates, require Applicants to fulfill their promise to provide the equivalent of a Service Assurance Plan, and impose a monitoring period for a minimum of five years. Both divestiture and access

[24] *See generally*, Exhibit 4, Verified Statement of Mark E. Zmijewski ("Zmijewski V.S."), at Section III.

to gateways on fair terms are independently important to prevent the merger from causing competitive harm—the former mitigates a specific competitive concern regarding parallel routes between Kansas City and Chicago and routes beyond to Detroit and Eastern Canada, while the latter does so for all situations where a formerly neutral KCS would be motivated to force customers to use CP-KCS single-line routes by refusing to participate in competitive joint-line routes on commercially reasonable terms. If the merger goes forward, these conditions are essential to addressing the competitive concerns it raises. The Service Assurance Plan (or its equivalent) and post-merger monitoring are necessary to prevent one of the most troubling consequences of mergers under the old rules, where disruption and degradation of service followed the less demanding examination of a merger's benefits and harms. As demonstrated below, such concerns are plainly present here.

Accompanying these comments are several verified statements in support.[25] First, Exhibit 1 is the Verified Statement of David Hunt. Mr. Hunt is a Vice-President of the global consulting firm of Oliver Wyman and has been a consultant in the transportation sector for more than 35 years. His statement analyzes the Application's post-merger traffic diversion projections and demonstrates that they are based on flawed methodologies, unsupported assumptions, and error-ridden calculations, and thus are wholly unreliable.

Exhibit 2 is the Verified Statement of Carl Van Dyke. Mr. Van Dyke is a senior advisor and partner emeritus at Oliver Wyman and has been a consultant in

[25] The workpapers will be made available to parties upon request.

the transportation sector for more than 40 years. As the developer of the MultiRail modeling software for analyzing rail operations, operating expenses, and associated investment requirements, he shows that Applicants' Operating Plan is based on invalid inputs, significant omissions, and numerous errors such that it is wholly unreliable and fails to comply with the Board's requirements.

Exhibit 3 is the Verified Statement of Hugh Randall. Mr. Randall is a senior advisor and partner emeritus at Oliver Wyman and has been a consultant in the transportation sector for over 30 years. His statement shows that Applicants' capital investment plan is inadequate and their operating expense estimates are clearly erroneous and unreliable.

Exhibit 4 is the Verified Statement of Mark E. Zmijewski. Professor Zmijewski is a professor emeritus at The University of Chicago Booth School of Business and Senior Consultant to Charles River Associates, specializing in accounting, valuation, and securities analysis. His statement analyzes the financial effects of CP's acquisition of KCS using the same analyses CP used to criticize CN's proposed acquisition of KCS and concludes that CP's financial risks—including high debt leverage, historically low ROIC, and likely incentives to behave anti-competitively when Applicants' over-optimistic financial projections fail to materialize—are the very same risks CP asserted made the proposed CN-KCS merger contrary to the public interest. Professor Zmijewski also reviews Applicants' claimed merger benefits in light of FTC guidelines and concludes that most of them would not be considered as cognizable or verifiable benefits.

I. THE APPLICATION IS RIDDLED WITH ERRORS, INCONSISTENCIES, AND FLAWED ASSUMPTIONS THAT CANNOT PROVIDE A BASIS FOR THE BOARD TO FIND THAT THE MERGER IS CONSISTENT WITH THE PUBLIC INTEREST.

Before the Board can even consider the "public interest" question in this proceeding, it must first understand the transaction Applicants are proposing and how the proposed merger will be implemented. But Applicants have submitted an Application that is so riddled with errors, omissions, inconsistencies, and unrealistic assumptions that the Board simply cannot rely on it in performing the public interest assessment required by 49 U.S.C. § 11323 *et seq.* and the Board's merger regulations.

As explained by CN witness Carl Van Dyke—the developer of the MultiRail modeling software for analyzing rail traffic and operations, operating expenses, and associated investment requirements—the first prerequisite for a sound operating plan for a proposed merger is a *traffic study* that, among other things, accurately predicts the volume of traffic that will be carried by the merger railroad.[26] These traffic diversion figures drive the development of the *operating plan.*[27] The projected traffic diversions also determine the merger's predicted revenues, which, along with the operating statistics derived from the operating plan, provide the necessary inputs to the *financial plan* (*i.e.,* revenues, capital spending, and operating expenses).[28]

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[26] Van Dyke V.S. at 10

[27] *Id.*

[28] *Id.* at 7.

"Any failure to use reasonable inputs and/or generate accurate outputs at any step [of this process] cascades through the process and renders the subsequent calculations invalid."[29] This is precisely what is offered in the Application—a error-ridden foundation that generates meaningless projections.

A. Applicants' Projected Traffic Diversions and Revenue Projections Are Grossly Exaggerated and Invalid.

Fundamental to an analysis of whether the proposed merger is in the public interest are diversion studies and related revenue projections. These are critical building blocks to assessing, for example, the extent to which the merger will generate procompetitive benefits, take trucks off the road, and allow the merging parties to handle their increased debt load. As Mr. Hunt explains, Applicants' diversion studies and related revenue projections are based on flawed methodologies, unsupported assumptions, and erroneous calculations that render the results of the study invalid.[30] These errors are not minor—Applicants' traffic-related revenue projections appear to be overstated by more than 100 percent.[31] As Mr. Hunt demonstrates, rather than the more than $1 billion of traffic-related revenue Applicants project, the likely figure is on the order of $500 million.[32]

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[29] *Id.*

[30] Exhibit 1, Verified Statement of David T. Hunt ("Hunt V.S.") at 3.

[31] *Id.* at 3–4.

[32] *Id.* at 6, Exhibit 3-2.

This overstatement is the result of several fundamental methodological errors committed by Applicants. First, Applicants grossly overstate expected rail-to-rail diversions and, as a result, the revenues they will earn post-merger.

Applicants' rail-to-rail diversions are based on the simplistic and highly implausible assumption that the length of a route is unrelated to that route's ability to gain a share of the available traffic.[33] But the relationship between route length and market share is a well-established concept in transportation modeling (as well as intuitive—the shortest route between an origin and destination can be expected to capture the greatest market share where cost is a function of distance).[34] Instead of applying this accepted principle, Applicants' experts mechanically assigned diversion percentages to traffic movements regardless of the relative distance of the incumbent rail route and the proposed CPKC route.[35] This is particularly problematic because the majority of the CPKC single-line routes that will be created by the merger are substantially longer than the already-existing route options available to shippers.[36] In fact, new CPKC single-line routes will be, on average, 217 miles longer than the routes over which the diverted traffic actually moves today.[37] Given that the routes to which Applicants predict traffic would be diverted are significantly longer than the routes over which that traffic moves today, Applicants'

[33] *Id.* at 8.

[34] *Id.*

[35] *Id.* at 8–13.

[36] *Id.* at 13–14.

[37] *Id.* at 14.

claim that 216,675 carloads and containers will be diverted to CPKC is simply not credible.[38]

To compound this clearly invalid assumption, Applicants' traffic experts applied overstated revenue amounts for many diverted carloads that are much higher than the average per carload revenue for those movements shown in the STB Public Waybill sample, in some cases by over 60 percent.[39] This overstatement of revenue per diverted carload is neither explained nor justified.[40] In other words, Applicants implausibly project that CPKC will collect more revenue from shippers on diverted traffic than those shippers pay today, and will do so by diverting the shipments to new CPKC routes that are substantially more circuitous than the existing joint-line route! As a result of these, and other, errors, Applicants have overstated the rail-to-rail diversions by at least $133 million.[41]

But this massive overstatement is just the tip of the iceberg. Applicants also proffer "supplemental" diversion estimates from company witnesses, which add an additional $411 million of projected revenues gains (approximately 40 percent of the total incremental revenue gains) over and above the diversions found by their expert traffic witnesses (Richard Brown, Nathaniel S. Zebrowski,

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[38] *Id.*

[39] *Id.* at 7 & n.9.

[40] *Id.*

[41] *Id.* at 7.

and Bengt Muten).[42] These "additional opportunities" include traffic that Applicants' experts did not include in their analysis of the same commodities, movements that clearly are not merger-related (because CP or KCS already participate in those movements today), and even traffic that does not currently exist.[43] CN witness Mr. Hunt estimates that these phantom opportunities account for as much as $388 million of the $411 million in projected "supplemental" revenues posited by Applicants' company witnesses.[44] For example, the claim by CP witnesses Jonathan Wahba and Mike Naatz that the merger would allow new shipments of "DRUbit" from a facility at Hardisty, AB, ignores that CP and KCS had already signed a contract to serve such shipments in 2019—long before merger discussions began.[45] Redacted

[42] *See generally*, Application, Vol. 2, Verified Statement of Richard W. Brown and Nathaniel S. Zebrowski ("Brown & Zebroswki V.S.") and Verified Statement of Bengt Mutén.

[43] Hunt V.S. at 24–35.

[44] *Id*. This does not include a currency conversion error that further overstates revenues on shipments with a currency conversion by 78%. *Id.* at 23–24.

[45] *See* Exhibit 11, December 3, 2019 Gibson Energy Press Release ("Gibson Energy Press Release"), at 1 (announcing "an agreement to construct and operate a diluent recovery unit (DRU) near Hardisty, Alberta, Canada … to process 50,000 barrels per day of inlet bitumen blend through the DRU to be shipped by Canadian Pacific … and Kansas City Southern Railway Company … to the U.S. Gulf Coast"); *id.* at 3 (KCS stating the agreement was "a great opportunity to grow our business in the Gulf Coast area and develop our Port Arthur asset").

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}} Applicants have disclosed in their SEC filings that they had reached remarkably different views of the potential synergies of the merger before entering the transaction. Specifically, at the KCS special Board meeting held on September 15, 2021, the KCS Board of Directors considered two separate synergies analyses: a CP synergies analysis showing annualized EBITDA synergies for the combined company of approximately $990 million ($810 million from revenue synergies and $180 million from operating and expense synergies); and a KCS management synergies analysis showing EBITDA synergies of approximately $377 million ($222 million from revenue synergies and $155 million from operating and expense synergies).[47] The enormous gap between the CP analysis and the KCS analysis casts considerable doubt on the

[46] *See* Ottensmeyer Dep. at 88:11–90:13 (stating that the Dec. 3, 2019, Gibson Energy Press Release described "a new service, moving DRUbit from western Canada to the U.S. Gulf Coast, specifically Port Arthur, Texas" with "a Canadian Pacific origin, interchanged at Kansas City, and … from Kansas City to Port Arthur," and responding, "Correct," when asked if the new service was "well before any merger talks"); *id.* at 90:3–13 (responding, "Correct" to the statement that "CP and KCS didn't need a merger to develop this particular piece of interline business").

[47] Exhibit 15, Excerpts from Canadian Pacific Railway Limited Form F-4 Registration Statement, filed with the Securities and Exchange Commission on October 1, 2021, at pp. 64–65, 97.

accuracy of Applicants' merger synergies analysis—particularly when the Application appears to have adopted the CP analysis and discarded the KCS one.

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[48] {{Redacted

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[49] {{Redacted

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[50] Exhibit 13, Excerpts from February 4, 2021 KCS Board of Directors Meeting Materials, at KCSR-HC-00014589 through KCSR-HC-00014591.

[51] *Id.* at KCSR-HC-00014591

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B. Applicants' Operating Plan Is "Essentially Meaningless."

As Mr. Van Dyke attests from his experience, "a rigorous operations plan is a key element of a reliable merger application."[53] In particular, the operating plan must be based on a "series of logical, interrelated steps," each of which must be sound to ensure that later steps are not skewed.[54] Applicants' operating planning process, however, "fails at nearly every level … [and] [t]he result is a set of modeling outputs that were so unreliable that *Applicants themselves disregarded their own operating plan outputs, including train-miles and GTMs – both of which are critical drivers of operating costs*."[55] The outputs of Applicants' Operating Plan do not align with their financial and environmental evidence and cannot be reconciled with one another. The result is incoherence.

Applicants' approach to developing their Operating Plan is both conceptually flawed and patently unreasonable. Applicants proposed to use 2019 as the "Base Year" for the Application. In its Decision accepting the Application, the Board

[52] *Id.* at KCSR-HC-0014593 through KCSR-HC-0014601.

[53] Van Dyke V.S. at 7.

[54] *Id.* at 7.

[55] *Id.* at 12–13 (internal footnote omitted) (emphasis in original).

adopted 2019 as the Base Year for this proceeding.[56] However, Applicants did not develop a Base Year Operating Plan that accurately reflected the 2019 traffic or operations of CP or KCS. Instead, Applicants developed a MultiRail operating model based on a series of disparate data sources from different years.

For example, rather than using carload data for the year 2019,[57] Applicants input to MultiRail a traffic file containing carload traffic that moved on CP and/or KCS during a single month in a different year, October 2020.[58] For unit train traffic, Applicants used a single month (October 2019) for CP and a different 30-day period (which is not identified in the workpapers) for KCS. Neither the Application nor the underlying workpapers offer any evidence to support the notion that these disparate traffic sources accurately portray the traffic volumes and commodity mix that moved on CP and KCS, respectively, during the (supposed) 2019 Base Year.

Even more strangely, Applicants elected not to use the blocking and train service plans that were in effect on CP and KCS during the actual Base Year (2019)

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[56] Amended Notice of Intent to File Application for Approval of Transaction Subject to 49 U.S.C. §§ 11323-25, *Canadian Pacific Railway Ltd.—Control—Kansas City Southern, et al,*, STB Docket No. FD 36500, at 3 (filed Sept. 15, 2021) ("Applicants will use the year 2019 as the base year for purposes of the impact analyses to be included with the Application (which remains the last full year unaffected by the COVID pandemic for which data are available"); Decision No. 11, *Canadian Pacific Railway Ltd., et al.—Control—Kansas City Southern, et al,*, STB Docket No. FD 36500 (STB served Nov. 23, 2021).

[57] Full year CP and KCS traffic data for 2019 was available to Applicants. *See* CPKC WP-HC-Traffic File – Methodology, at 3 ("FTI supplied CPRS with multiple years of data, *but CPRS chose to use October 2020 for a base month*") (emphasis added).

[58] Elphick/Orr Dep. at 157:13 – 157:21.

in building an initial set of trains in the MultiRail model. Instead, Applicants constructed a Base Year (2019) blocking and train service plan that reflected the carriers' operations *as of the 1st Quarter of 2021*. Applicants' explanation for doing so—that Q1 2021 data were used to avoid attributing to the merger efficiencies already achieved by Applicants between 2019 and Q1 2021[59]—is beside the point. A series of inputs involving traffic, blocking plans and trains from three different time periods, by definition, cannot produce an accurate estimate of Applicants' actual Base Year (2019) operating plan.

Applicants further undermined the validity of their Operating Plan outputs for both the pre- and post-merger cases by removing trains that had traffic assigned to them by MultiRail from the counts of trains per day by subdivision and the subdivision traffic densities (tonnages). Specifically, Applicants applied a "rule" that removed from the train counts and line densities any train that did not traverse at least 25 percent of the stations on a subdivision. This rendered the trains per day and tonnages by subdivision incomplete and had a cascading effect on the calculation of key operating statistics, including train-miles (which in theory should be used to estimate operating expenses).[60]

While it is customary to use a full year of traffic data, *Applicants took a similar, mere one-month sample approach to rail yard activity and carloads,*

[59] *See* Application, Vol. 2, Exhibit 13 (Operating Plan), at 27.

[60] *See* Van Dyke V.S. at 24–25.

including the number of hazardous cars on their lines in the Base Year.[61] Applicants submitted this flawed information as the foundation of their Application, as well as in response to the requests from the Board's Office of Environmental Analysis.[62]

These and other significant errors when processing traffic data used to develop the Operating Plan resulted in "invalid traffic" that "distorted the Applicants' development of the Base Year blocking and routing plan, train plan, and the operating metrics, rendering the operating plan invalid and unusable."[63] The Operating Plan does not produce reliable estimates of traffic density, train counts, or yards where growth is expected such that "Applicants have provided essentially meaningless responses" to the Board's requirements.[64] Ultimately, Applicants'

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[61] *See, e.g.,* Application, Vol. 2 Operating Plan, Appendix B, Changes in Yard Volumes ("Base Traffic: October 2020FTIBase, 28 days" and "Alternate Traffic: October 2020FTIBase."). The Board requires density charts be submitted for the "latest available full calendar year" for precisely this purpose. *See* 49 C.F.R. § 1180.8(b)(5).

[62] Applicants' response to the Board's Office of Environmental Analysis did not reveal the use of a one-month snapshot from October 2020 for carload and intermodal traffic in the gross tons, rail yard activity, and [trains per day and carloads.] Letter from Applicants to Danielle Gosselin, FD 36500, at 2 (October 28, 2021) (In Response to Request A, Applicants indicated their transaction-related growth analyses "set 2019—the last pre-pandemic year—as a starting point" and indicating that they provided the "2019 baseline traffic" in tables); *id.* at 6 (In Response to Request F, "Like the other tables CP and KCS are providing, these tables show 2019 traffic…."). Applicants' December 20 response to the Board's Office of Environmental Affairs again reiterated their erroneous claim that their first response included actual historic numbers form 2019: "As it did in response to Information Request No. 1, CP is providing three data sets: actual numbers from 2019 (the last pre-pandemic year)…." Letter from Applicants to Danielle Gosselin, FD 36500, at 2 (Dec. 20, 2021).

[63] Van Dyke V.S. at 3.

[64] *Id.* at 5.

Operating Plan "fails to meet basic Board requirements" and is a "deeply flawed proposal that cannot be relied upon in evaluating the impact of the proposed merger on CP-KCS operations, the operations of other railroads, or other stakeholder, such as shippers and communities."[65]

The numerous flaws in Applicants' Operating Plan generated additional errors throughout the Application. For example, *Applicants did not use their Operating Plan to calculate their purported operating metrics or expenses*. In particular, the post-merger table of operating plan metrics in Applicants' Exhibit 13[66] is not based on the MultiRail Operating Plan but, rather, on a "System Model" that does not align with the Operating Plan.[67] And while the Operating Plan accounted for organic growth, the System Model does not (thereby significantly understating Year 3 operating metrics). Nor do the Operating Plan metrics align with Applicants' financial projections, which are based strictly on new business growth. Likewise, Applicants' environmental filing relies on values that are inconsistent with those in the Operating Plan. In other words, Applicants' System Model, operating plan, financial projections, and environmental filings—which all should be in harmony and reflect consistent inputs—paint multiple contradictory pictures, and there is no way of knowing which is correct.

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[65] Van Dyke V.S. at 2.

[66] *See* Application, Vol. 2 at 287, Table 2.

[67] *See* Elphick/Orr Dep. at 180:17–183:3.

These disconnects are not minor. For example, the Operating Plan produces an annual increase in train-miles of approximately {{Redacted }} whereas Applicants' costing process appears to be based on an increase of approximately { Red }} train-miles. Likewise, while the Operating Plan contemplates an { Redacted }}, the costing process uses an { Redacted }}. Applicants' decision not to develop operating metrics based on Applicants' Operating Plan (as has been done in prior merger cases) means that Applicants' operating and capital expense calculations (which should be based on accurate operating metrics) are understated and wholly "unreliable."[68]

C. Applicants' Financial Plan Is Inadequate and Understates Operating Costs by More Than $2.0 Billion.

A robust and accurate capital investment plan is necessary for the Board to determine the financial impact of the merger and the ability of the merging parties to handle their projected traffic. As Mr. Randall explains, Applicants identify specific projects for only 8 percent of the $5.7 billion they plan to spend in Years 1–3 and otherwise fail to identify the nature or location of other capital projects—much less their estimated cost and timing—which makes "it impossible for interested parties (or the Board) to assess the adequacy of Applicants' capital spending plans."[69]

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[68] Van Dyke V.S. at 6.

[69] Exhibit 3, Verified Statement of Hugh Randall ("Randall V.S."), at 7.

In any event, Applicants' projected capital spending appears to be woefully inadequate. Pre-merger, CP and KCS collectively averaged capital expenditures of $1.9 billion annually, which equaled 24.2 percent of revenue between 2014 and 2019, and in no year were their (combined) capital expenditures less than 21.0 percent of (combined) revenues. Post-merger, Applicants plan to continue spending the same $1.9 billion per year, or 20.6 percent of revenue, in Year 1, 20 percent in Year 2, and 19.6 percent in Year 3 on capital projects.[70] At the same time, Applicants are projecting that CPKC will transport 40 percent more traffic (in GTMs) by the end of Year 3 (19.8 percent resulting from merger-related growth and 21 percent from organic growth). As Mr. Randall notes, "[i]t is simply not credible that Applicants can adequately address the merged railroad's capital needs by spending no more per year than they spend before the merger, while accommodating significantly higher traffic growth."[71]

Importantly, Applicants have failed to provide for capital projects that clearly would be required to accommodate post-merger traffic volumes. Mr. Randall and his team at Oliver Wyman assessed the CPKC network in light of projected traffic increases and found that "significant train delays and service disruptions are likely without additional capital spending" to ensure line-of-road, yard capacity, key bridges, and locomotive fleets can handle the traffic.[72]

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[70] *Id.* at 8–9.

[71] *Id.*

[72] *Id.* at 10.

This is not surprising given the lack of attention Applicants paid to this critical issue. Applicants' operating witness, Mr. Elphick, {{Redacted

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With regard to operating expenses, Applicants "have failed to prove that they have adequately estimated operating expenses and have used a deeply flawed and inaccurate approach to cost analysis and financial projections."[75] In particular, Applicants' operating expense estimate is based entirely on a table of incremental

[73] *See, e.g.*, Elphick/Orr Dep. at 55:10-56:24, 79:21-81:4, 124:5-20, 250:14-251:23 Redacted

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[74] *See id.* at 124–28.

[75] Randall V.S. at 23.

operating expenses that has no relation to the Operating Plan and is not supported by work papers or other evidence.[76] Mr. Randall estimates that Applicants have understated their projected operating expenses for the first three years by no less than $2.0 billion and (based on CP's and KCS's U.S. actual experience) by as much as $2.47 billion.[77] This represents a "an understatement of the merged railroad's operating expenses of approximately 10.7 to 12.9 percent of total operating expenses for those years."[78]

Finally, Applicants overstate productivity savings. Doing so has the effect of allowing Applicants to claim they will have greater cash flow available to fund capital improvements and pay off the massive debt CP is incurring to acquire KCS. Reality is far less rosy and casts significant doubt on whether Applicants will be able to provide adequate levels of service.

Applicants make the obviously incorrect assumption that the vast majority of the projected productivity savings will be realized during the first year of merged operations. *Applicants assume that $93.5 million, or 80.8 percent, of the total projected $115.7 million savings in operating expenses will be achieved in Year 1.* For transportation, fuel-related, and locomotive leasing/depreciation cost savings, Applicants assume that fully 96.5 percent will be realized in Year 1.[79] It is highly

[76] *Id.* at 23–24.

[77] *Id.* at 23.

[78] *Id.*

[79] *Id.* at 24–25; *see* Oliver Wyman Opex worksheet for calculation.

unlikely that Applicants would be able to implement all of the operating changes required to generate virtually all of the achievable operating expense savings in the first post-merger year, especially when considering that CP and KCS cannot begin the merging of their networks until Day 1 of the approved merger.

Based on their seriously flawed operating expense estimation process, Applicants posit they will incur only $306.3 million in increased operating expenses to transport 510,315 incremental carloads, while those carloads will generate $1,021.9 million in additional revenues.[80] This equates to a 70 percent flow-through of revenue to operating income, or a 30 percent operating ratio—*something no Class I railroad in North America has ever achieved on either baseload or incremental traffic.*[81] As Mr. Randall explains, "while Applicants submitted the veneer of an operating expense development process (including a purported MultiRail analysis of post-merger operations), the operating expenses reflected in the Application are nothing more than assumptions that are unsupported by documentation or analysis."[82]

[80] Randall V.S. at 24.

[81] *Id.* at 31.

[82] *Id.* at 24.

II. APPLICANTS' ASSERTED BENEFITS ARE VASTLY OVERSTATED & UNSUPPORTED.

The core question entrusted to the Board in a Class I merger proceeding is whether the proposed merger is "consistent with the public interest."[83] This standard requires more than a mere showing that the proposed merger will result in private profits, traffic diversions, or even new single-line service. Rather, the application must demonstrate that verifiable and quantifiable benefits would flow *to the public* from the proposed merger, and that those *public* benefits would outweigh "any harm to competition, essential service(s), labor, and the environment that cannot be mitigated by conditions."[84] Applicants have failed to meet this standard.

A. Traffic Diversions and Private Profits Are Not Public Benefits.

Applicants have failed to prove the proposed merger will be in the public interest by quantifying its claimed public benefits.[85] The Application's alleged "quantified public benefits" is merely a balance sheet of hoped-for private earnings.[86] Providing an estimate of increased CP-KCS profits does not satisfy Applicants' burden of proof: The agency has long made clear that private earnings are not public benefits: "financial benefits for the consolidating carriers that are

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[83] Decision No. 37, *Canadian National Ry. Co., et al.—Control—Illinois Central Corp., et al.*, STB Docket No. FD 33556 (STB served May 25, 1999) ("*CN-IC*"), slip op. at 19 ("'[t]he Act's single and essential standard of approval is that the [Board] find the [transaction] to be "consistent with the public interest."').

[84] *Id.*

[85] *See id.*

[86] Application, Vol. 1 at 10; *id.*, Vol. 1 at 74 ("Summary of Benefits" exhibit).

purely transfers from competing carriers" are "private benefits [that] have not been considered in our analysis of the public benefits of the consolidation."[87]

In this proceeding, the demonstrated and quantifiable benefits to the shipping public supported by the Application are exactly *zero*. Providing financial gains to CP-KCS shareholders does not further the public interest. Applicants, who have the burden of proof to establish quantifiable public benefits in their Application, have thus failed to meet their burden.[88] The Board should not approve a major merger application that fails to prove any quantifiable public benefits, particularly in light of the current Administration's competition policy goals and positions.[89]

Likewise, Applicants' projected traffic diversions do not constitute public benefits. Shippers do not benefit from shifting traffic to different routes or different carriers absent some showing that those diversions will produce lower rates, better service, shorter routes, or the like—none of which Applicants have proven. In any event, as discussed above, Applicants' projected traffic diversions are grossly exaggerated and cannot be relied upon by the Board.

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[87] *Union Pac. Corp., et al.—Control—Missouri-Kansas-Texas R.R. Co., et al.*, ICC Finance Docket No. 30800, 1988 WL 226818, at *5 (decided May 13, 1988); *see also* Decision No. 37, *Canadian National Ry. Co., et al.—Control—Illinois Central Corp., et al.*, STB Finance Docket No. 33556 (STB served May 25, 1999), slip op. at 18, n. 62 (noting that the "total annual net revenue gain of $90.3 million[] must be viewed as a private benefit (not a public benefit) of the CN/IC control transaction").

[88] 49 CFR § 1180.4(c)(8).

[89] *See, e.g.*, *Promoting Competition in the American Economy*, E.O. 14036, 86 Fed. Reg. 36987 (Jul. 9, 2021), *available at* https://www.govinfo.gov/content/pkg/FR-2021-07-14/pdf/2021-15069.pdf.

B. Applicants' Assumed Public Benefits Are Unsupported and Overshadowed by the Significant Risks of the Proposed Merger.

If the errors, exaggerations, and unsubstantiated claims in the Application are set aside, the potential *public* benefits that remain from the proposed transaction do not amount to much. While CP and KCS may be able to capture some modest traffic diversions (if there are no serious service problems), the Application offers few substantial and identifiable capital improvements to enhance the national rail network or benefit shippers, limited environmental benefits, no planned innovations to improve the customer experience, and no evidence that rates would fall or service would improve.

Importantly, the majority of CPKC single-line routes to which Applicants propose to divert traffic are substantially longer than the incumbent routing options. Specifically, as CP-KCS witnesses Brown and Zebrowski acknowledge, *the new CPKC single-line route would be, on average, 217 miles longer than the routes over which the diverted traffic actually moves today*.[90] Replacing a more efficient, less costly interline route with a longer, more circuitous single-line route does not benefit shippers. Moreover, Applicants have not committed to any rate reductions for shippers who agree to utilize CPKC's less efficient routes. Indeed, Applicants assume a 333 R/VC ratio on traffic they convert from other railroads.[91]

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[90] Brown & Zebrowski V.S. at 132, Table 6.

[91] Application, Vol. 1 at 74. CP-KCS assert that the merger will result in a $1.02 billion "Revenue Increase from Traffic Gains" (primarily from alleged diversions from other railroads), but that their "Cost of Handling Added Traffic" would be only

Neither would a combined CP-KCS improve service, particularly in light of the more circuitous CPKC routes. In addition, as discussed above, Applicants' inadequate capital investment plan—far from improving service—actually poses a serious risk even to maintaining current service levels. With the longer routes and minimal levels of investment Applicants have planned, shippers cannot expect increased capacity, faster transit times, lower rates, or innovative service offerings.

Applicants have shown little interest in developing truck-to-rail diversion opportunities. They estimate that the merger would take only 64,000 trucks per year off the road. By contract, CN's Responsive Application will divert more than 80,000 annual truck shipments to the Springfield Line alone. Applicants' seeming indifference to removing trucks from America's highways is a loss to shippers, local communities, and the Administration's environmental goals. In addition, Applicants have failed to protect—and will be incentivized to discourage—interline opportunities, which would increase competition and offer more routing options to the benefit of shippers.

In short, Applicants have merely asserted—but have not proven—that significant public benefits would flow from the proposed transaction. Repeating the mantra of "single-line service" is not evidence. And even assuming some portion of the projected traffic diversions will materialize, any potential benefits to shippers

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$306 million. *Id.* Applicants are thus assuming that they would realize an average revenue-to-variable-cost ratio metric ("R/VC") of 333% on diversion traffic.

would be, at best, modest and would be far outweighed by the significant risks to the public interest that this proposed transaction poses, discussed next.

III. THE APPLICATION DOWNPLAYS THE SERIOUS PUBLIC INTEREST RISKS OF THE PROPOSED MERGER.

A. The Net Competition Benefits of the Proposed Transaction Are Negative Unless Remedial Conditions are Proposed.

Applicants repeatedly assert that their merger threatens no competitive harm whatsoever. That is untrue for multiple reasons. First, Applicants simply ignore the competition harm caused by their proposed consolidation of parallel lines and their plan to forego investment in KCS's Springfield Line. Second, the vague gateway commitment in the Application is plainly insufficient to protect against vertical foreclosure concerns. If the Board approves the proposed transaction, it should at a minimum, impose robust conditions to protect competition, including divestiture of the Springfield Line to CN and a clear and enforceable gateway commitment. The need to impose such conditions here is supported by CP's historical conduct. KCS used to offer a competitive alternative to Iowa and Minnesota based on agreements with CP—agreements that CP refused to renew, thus eliminating that competitive option only three years before proposing to acquire KCS. The Board should view CP's alleged "commitment" to preserving robust competition in light of its actual past actions.

1. A combined CP-KCS is not a "pure" end-to-end merger and raises significant horizontal competition concerns.

In opposing the proposed CN-KCS merger, CP proffered the verified statement of Dr. W. Robert Majure, who broadly asserted that a merger between

railroads with parallel routes creates a horizontal threat to competition.[92] In his expert opinion, railroads that terminate or originate traffic within the same BEA are competitors.[93] For example, Dr. Majure treated CN's and KCS's lines in Mississippi as competitive even though they were many miles apart.[94] Indeed, Dr. Majure's analysis treated CN's and KCS's main north-south lines as competing even though they were separated by the Mississippi River.[95] Dr. Majure's analysis did not consider truck or barge competition to be of any relevance, focusing exclusively on loss of "rail choice."[96] Apparently convinced by CP's advocacy, the Board

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[92] Canadian Pacific's Reply to CN and KCS Joint Motion for Approval of Voting Trust, *Canadian National Railway Company, et al.—Control—Kansas City Southern, et al.,* STB Docket No. 36514 ("Canadian Pacific Reply") (filed June 28, 2021),Verified Statement of W. Robert Majure ("Majure V.S."), ¶¶ 49–50; *see also id.* ¶¶ 46–48; *id.* at 38–41.

[93] Majure V.S. ¶¶ 42–53.

[94] Applicants' Reply to Comments on Proposed Voting Trust Agreement, *Canadian National Railway Company, et al.—Control—Kansas City Southern, et al*., STB Docket No. 36514 (filed July 6, 2021), Reply Verified Statement of William J. Rennicke ("Rennicke Reply V.S."), at 40–41 (discussing Dr. Majure's competition analysis). The DOJ also raised concerns about mergers involving parallel lines, even when they do not serve the same origin-destination pairs. Comment of the U.S. Dep't of Justice, *Canadian National Railway Company et al.—Control—Kansas City Southern Railway Company, et al.*, STB Docket No. 36514, at 2 (filed May 14, 2021); *see also* Comment of the U.S. Dep't of Justice, *CSX Corporation and CSX Transportation, Inc., et al—Control and Merger—Pam Am Systems, Inc, et al*. STB Docket No. FD 36472, at 3 (filed Aug. 26, 2021).

[95] *Compare* Majure V.S. ¶ 48 & Ex. 4, *with* Rennicke Reply V.S. at 16, 32–33, 37–42.

[96] *Compare* Majure V.S. ¶¶ 5, 46, *with* Rennicke Reply V.S. at 22–23.

concluded that CN and KCS "operate parallel lines through the central portion of the United States…."[97]

Applicants now try to sweep CP's prior positions under the rug. They appear to hope that if they repeatedly assert their merger is a "pure" "end-to-end" combination, that will make it so.[98] Rhetoric, however, is not a substitute for facts. The CP-KCS merger raises a significant horizontal competitive concern that must be addressed by the Board.

As CN had demonstrated, the Springfield Line is part of a direct competitive alternative to CP's route between Kansas City and Chicago, and beyond to Detroit and Eastern Canada.[99]

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[97] *Canadian National Railway Co., et al.—Control—Kanas City Southern, et al.*, STB Docket No. FD 36514, at 28 (STB served Aug. 31, 2021).

[98] Application, Vol. I, at 20; *id.*, Creel V.S. ¶ 28. This hide-the-ball tactic stands in direct contrast to CN's treatment of horizontal competition issues in its proposed merger with KCS. There, CN expressly acknowledged the parallel KCS line between Baton Rouge and New Orleans, Louisiana and committed to divest the line on terms that would ensure no reduction in competition for shippers in that corridor. Joint Motion for Approval of Voting Trust Agreement, *Canadian National Railway Company—Control—Kansas City Southern*, STB Docket No. FD 36514 (filed May 26, 2021),Verified Statement of Jean-Jacques Ruest, at 3–5,; *id.*, Verified Statement of William J. Rennicke, at 4, 7, 10.

[99] Description of Anticipated Responsive Application, *Canadian Pacific Railway Limited, et al.—Control—Kansas City Southern, et al.*, STB Docket No. 36500 ("Notice of Responsive Application") (filed Jan. 12, 2022).

The Parallel CP and KCS Routes

This route can be used to move freight in competition with CP's parallel line, and shippers have in the past moved freight between Kansas City and Chicago using this line.[100] More recently, KCS expressed interest in, and touted the benefits of, investing to increase track speeds on this line to create a "Kansas City Speedway."[101]

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[100] *See, e.g.*, Decision No. 37, *Canadian National Railway Company, et al.—Control—Illinois Central Corporation, et al.*, STB Finance Docket No. 33556, 4 S.T.B. 122, 175 (1999) ("*CN-IC*") (recognizing that KCS and Illinois Central (now CN) were interchanging "three trains per week" via the Springfield interchange point at Cockrell).

[101] *See, e.g.*, Kansas City Southern, *Combination of CN & Kansas City Southern: Creating the Premier Railway of the 21st Century*, at 8–9 (July 2021), *available at* https://www.sec.gov/Archives/edgar/data/0000054480/000005448021000202/kcsinvestorpresentation .htm (stating that "Kansas City Speedway" would be a "new competitive route between KC, Detroit & Chicago").

Yet Applicants propose *no* incremental investment in the Springfield Line.[102] A combined CP-KCS will have little incentive to invest in the Springfield Line or to partner with CN to create the Kansas City Speedway or to invest in improvements on the line, because such pro-competitive actions would be inconsistent with their plan to concentrate traffic on CP's parallel route to Chicago.

As DOJ has explained in this proceeding[103] and elsewhere,[104] a combined CP-KCS will have an incentive to resist efficient interchanges with rival railroads that could divert traffic from CP's network. The Application confirms that concern, as the parties apparently plan to allow the KCS Springfield Line effectively to wither on the vine in favor of CP's parallel route. This not only prevents its use as a competitive option for through traffic, but also harms local customers on the line who will see no incremental investment and likely deteriorating rail service.

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[102] Notice of Responsive Application at 3–4 (citing Application, Vol. 1 at 41) (showing no planned capital investment on Springfield Line).

[103] *See* Comment of the U.S. Dep't of Justice, *Canadian Pacific Railway Limited et al.—Control—Kansas City Southern Railway Company, et al.*, STB Docket No. FD 36500, at 4 (filed Apr. 12, 2021 (observing that the pending merger would cause "KCS [to] make decisions regarding new track construction and old track closure with an eye toward interchanging KCS traffic with CP in the future. Such decisions may be at the expense of interchanges with other railroads, even though these other interchanges may be better for KCS's customers and KCS itself").

[104] *See* Comment of the U.S. Dep't of Justice, *CSX Corporation and CSX Transportation, Inc., et al.—Control and Merger—Pan Am Systems, Inc., et al.*, STB Docket No. 36472, at 3 (filed Aug. 26, 2021) (noting that if CSX were to acquire a stake in a line parallel to its own it could "undermine [its rivals] notwithstanding the joint venture by sabotaging this service and expecting to recapture traffic on its independent line").

Applicants appear to suggest that there is no competitive issue because CN's lines do not physically connect with KCS's at Springfield.[105] Applicants are wrong. In fact, CN's subsidiary, Illinois Central, has unrestricted trackage rights over UP to connect with KCS at Springfield, as recognized by the STB in its decision in the *CN-IC* merger.[106]

Further, and dispositively, Dr. Majure, Applicants' economist, acknowledges that { Redacted

}}[107] The fact that this traffic today is moved jointly by KCS in cooperation with a railroad other than CP contradicts Applicants' assertion that the Springfield Line is not "parallel" to CP's line.[108] Indeed, it directly raises the concern that the merger will eliminate KCS's existing incentives to facilitate the

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[105] Applicants' Reply to Canadian National's Description of Anticipated Responsive Application, *Canadian Pacific Railway Limited, et al.,—Control—Kansas City Southern, et al.*, STB Docket No. FD 36500, at 6 (filed Jan. 28, 2022).

[106] *CN-IC*, 4 S.T.B. at 190–99 (describing various trackage rights agreements relevant to KCS/IC Springfield interchange).

[107] Buried towards the end of his statement, Dr. Majure { Redacted

} *Id.*

[108] Applicants' Reply to Canadian National's Description of Anticipated Responsive Application, Canadian Pacific Railway Limited, et al.—Control—Kansas City Southern, et al., STB Docket No. FD 36500, at 6 (filed Jan. 28, 2022).

interchange of traffic with other railroads because it risks diverting traffic from CP after the merger.[109]

To be sure, the traffic volumes that currently move between Kansas City and Chicago over the Springfield Line are below the levels that are currently moved by CP over its parallel line.[110] But that does not mean that shippers today are not able to leverage the Springfield Line as a competitive threat when negotiating with CP, as Dr. Majure previously acknowledged.[111]

Moreover, even if there were *no* traffic being moved between Kansas City and Chicago today over the Springfield Line, there would still be a significant competitive concern. As noted, KCS has touted the potential for this line to be upgraded to create a Kansas City Speedway.[112] As described in CN's Notice of

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[109] In making this suggestion, Applicants are again quarreling with their own economist. Dr. Majure { Redacted }} Majure V.S. ¶ 54. And yet, KCS does not serve the Upper Midwest or Canada, which makes clear that corridor competition under Dr. Majure's argument includes interline routes.

[110] *Cf.* Majure V.S. ¶ 70.

[111] Majure V.S. ¶¶ 18–19, 38 (describing { Redacted }).

[112] *See, e.g.*, Bernstein Slides, at 5 (touting the "Kansas City Speedway – connecting CN's Midwest foothold and the KC region"); Kansas City Southern,, *Combination of CN & Kansas City Southern: Creating the Premier Railway of the 21st Century*, at 8–9 (July 2021), *available at* https://www.sec.gov/Archives/edgar/data/0000054480/000005448021000202/kcsinvestorpresentation .htm (stating the "Kansas City Speedway" would be a "new competitive route between KC, Detroit & Chicago").

Responsive Application, such a Speedway would provide enormous public interest benefits—preserving and renewing the route and doing more to benefit customers, including creating a more attractive option for moving freight between Kansas City and Chicago and then beyond to Michigan and Eastern Canada.[113] It would provide a far superior alternative to CP's more circuitous route and, CN projects, remove more than 80,000 trucks off the road annually.[114] The antitrust agencies have repeatedly recognized that significant competitive concerns arise where, as here, an acquiring company will have reduced incentive to deploy the acquired assets efficiently because of the concern that doing so will cannibalize the acquiring company's existing sales.[115]

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[113] *See generally,* Notice of Responsive Application.

[114] Application and Exhibits, *Canadian Pacific Railway, et. al.—Control—Kansas City Southern, et al.*, STB Docket No. FD 36500 (Sub-Nos. 1, 2, 3, 4) (filed Feb. 28, 2022) ("CN Responsive Application"), Verified Statement of David T. Hunt, at 8.

[115] *See* U.S. DEP'T OF JUST., ANTITRUST DIV., MERGER REMEDIES MANUAL 6–9 (Sept. 2020); Press Release, U.S. Dep't of Just, Antitrust Div., Just. Department Sues to Block Visa's Proposed Acquisition of Plaid (Nov. 5, 2020), https://www.justice.gov/opa/pr/justice-department-sues-block-visas-proposed-acquisition-plaid (asserting, *inter alia*, that Visa's acquisition of Plaid was likely to prevent Plaid from competing with it in the future); *United States v. Bazaarvoice, Inc.*¸ No. 13-cv-0013-WHO, 2014 WL 203966 (N.D. Cal. Jan. 8, 2014), https://www.justice.gov/atr/case-document/file/488846/download (similar); *cf.* Press Release, Fed. Trade Comm'n, FTC Challenges Illumina's Proposed Acquisition of Cancer Detection Test Maker Grail (Mar. 30, 2021) (similar), https://www.ftc.gov/news-events/press-releases/2021/03/ftc-challenges-illuminas-proposed-acquisition-cancer-detection.

2. CP's acquisition of KCS will fundamentally undermine KCS's existing incentives to interchange traffic with other railroads on commercially reasonable terms

The proposed merger will also reduce KCS's existing incentives to interchange traffic with other railroads on commercially reasonable terms, creating a significant threat to future rail competition. Today, KCS provides very little "single-line" service. According to STB data, approximately 87 percent of the traffic KCS carries is handled in partnership with another railroad.[116] Pre-merger KCS is, in essence, a neutral connecting carrier with strong incentives to work cooperatively with other railroads to exchange traffic on reasonable terms so that KCS and its partners can jointly serve shippers that individually neither could serve.

The proposed transaction will fundamentally change those existing incentives. Post-merger, Applicants will have a strong incentive to favor CP-KCS routings, to the detriment of other efficient routes in which other railroads participate with either KCS or CP today. KCS will seek to concentrate that traffic on the combined firm's routes, which serves many of the same geographic areas in the Midwest and Canada as CN. Working with CN, in contrast, would threaten to divert traffic from CP, reducing the revenues the combined company earns.[117] CP-

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[116] *See* STB 2019 Commodity Statistics Report for KCS, *available at* https://www.stb.gov/wp-content/uploads/files/econdata/QCS/KCS/2019/QCS-KCS-2019.xlsx (showing 13 percent of KCS traffic are local moves where KCS serves both the origin and destination—164,967 cars of local KCS movements out of 1,263,808 total movements).

[117] When CP-KCS serve a customer entirely over their own facilities, they keep all of the revenues earned. When KCS jointly serves a customer with another railroad such as CN, then those revenues are divided between KCS and the partner railroad.

KCS, for example, may not have an incentive to maintain service levels at efficient interchanges with other railroads or to quote competitive rates for movements that require participation of other railroads.

This agency has repeatedly recognized that an "end-to-end" rail combination, while generally efficient, can nevertheless raise significant vertical competition concerns: "[In an end-to-end merger], the consolidated system may profit by limiting the 'downstream' competition [from connecting carriers] and routing traffic over its own lines from origin to destination.… This vertical foreclosure effect will occur, if at all, at the gateways served commonly by the consolidating carriers."[118] DOJ has likewise recognized the potential for vertical competitive harm from end-to-end

[118] *Lamoille Valley R.R. Co. v. ICC*, 711 F.2d 295, 319 (D.C. Cir. 1983) (quoting *Union Pac. Corp.—Control—Mo. Pac. Corp.*, 366 I.C.C. 462, 529 (1982)); *see also* Decision No. 44, *Union Pac. Corp., et al.—Control & Merger—Southern Pac. R.R. Co., et al.*, 1 S.T.B. 233, 365 (1996) (recognizing that "[v]ertical effects [may] occur where the merging parties connect end-to-end"); *Union Pac. Corp., et al.—Control—Missouri Pacific Corp. and Missouri Pacific Railroad Co.*, 366 I.C.C. 462, 514 (1982) ("A vertical effect can occur if one of the consolidating carriers formerly interchanged traffic with both its consolidation partner and other carriers in providing joint line services over a particular gateway. The transaction then may result in the foreclosure of the nonincluded carrier from competing in the markets it formerly served."); *Norfolk S. Corp.—Control—Norfolk & W. Ry. Co., et al.*, 366 I.C.C. 173, 216 (1982) ("An end-to-end consolidation … may allow the system to divert traffic from remaining competitors and hence foreclose their opportunity to compete in the marketplace. … Such diversions can have anticompetitive effects."); *Guilford Transp. Indus., Inc.—Control—Bost. & Me. Corp.*, 366 I.C.C. 294, 341 (1982) ("We have previously found that end-to-end rail consolidations can directly reduce competitive alternatives … for shippers located at common points on the consolidating systems").

transactions—indeed, it has raised this concern with respect to the CP-KCS merger itself.[119]

Of particular concern is that post-merger KCS will have reduced incentive to interchange traffic with CN at Jackson, Mississippi—an exchange that illustrates the points made above. As KCS has previously recognized, there is a significant commercial opportunity to connect origins and destinations in Mexico and Texas on its network with destinations in the upper Midwest and Canada on CN's network.[120] The interchange at Jackson is a critical link for CN and its customers to reach origins and destinations in Mexico and Texas. After the merger, however, a combined CP-KCS will be concerned that interchanging at Jackson with CN and other railroads will divert traffic away from the legacy CP network, which connects with KCS at Kansas City, and through that route, services large parts of Canada and the Midwest. The following maps illustrate this point.

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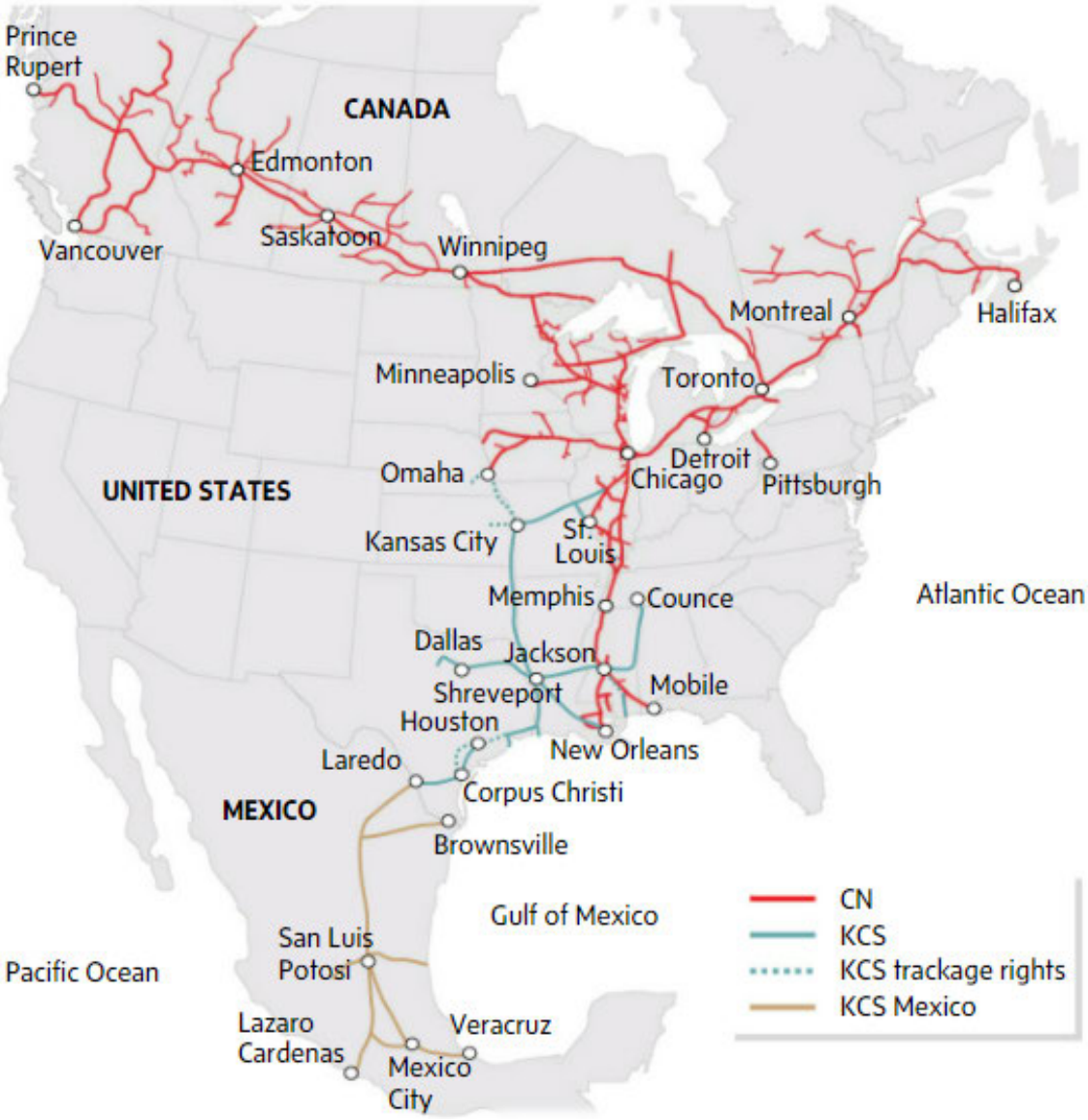
[119] Comment of the U.S. Dep't of Justice, Canadian Pacific Railway Limited et al.-Control-Kansas City Southern Railway Company, et al., STB Docket No. 36500, at 4 (filed Apr. 12, 2021) (after the merger, KCS will make operational and investment decisions with an "eye toward interchanging KCS traffic with CP").

[120] *See, e.g.*, Joint Motion for Approval of Voting Trust Agreement, Canadian National Railway Company, et al.-Control-Kansas City Southern, et al., STB Docket No. FD 36514 (filed May 26, 2021), Verified Statement of Patrick J. Ottensmeyer at 8–9.

CN and KCS Networks Efficiently Connect at Jackson to Serve Traffic Flows between Texas/Mexico and the Upper Midwest/Canada



CP and KCS Will Have an Incentive to Favor CP-KCS Routes between Texas/Mexico and the Upper Midwest/Canada

The Application underscores this concern. In connection with the CN-KCS merger proposal, KCS recognized that the merger would allow shippers to move industrial goods between Texas and Mexico, on the one hand, and Detroit and Ontario, on the other, via Jackson. However, the Application projects a material *decrease* in KCS's interchange traffic with CN and other railroads at Jackson, while traffic on the competing CP-KCS route via Kansas City is expected to increase substantially.[121] Indeed, the core assumption of CP-KCS's claims of volume growth from the merger is that a substantial volume of traffic that CP and KCS currently

[121] *See* Application, Vol. 2 at 305 (showing decrease in cars moving through Jackson yard even under CP-KCS "growth plan").

move in joint-line service with other railroads will instead move on single-line CP-KCS service.[122] Applicant's post-merger strategy is further revealed by the fact that *the Application identifies $276 million in planned capital investment in the proposed CPKC north-south mainline between Sabula Jct., IA, and Beaumont, TX, while no capital investment dollars are earmarked for KCS's Springfield Line.*[123]

This vividly illustrates the danger that a combined CP-KCS will set prices and degrade service to push shippers to their own long-haul routes unless significant enforceable protections are imposed as merger conditions. Applicants' operating plan thus confirms the need for the Board to impose meaningful, enforceable conditions to ensure that gateways remain open on commercially reasonable terms.

Ultimately, and as conceded by Applicants,[124] the issue is what conditions the Board should impose to address these concerns, not whether any conditions should be imposed. Given the foregoing facts, no other position would be tenable. However,

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[122] *See* Applicants' Reply to "Comments" Seeking Rejection of Application Filed October 29,2021, *Canadian Pacific Railway Limited, et al.-Control-Kansas City Southern, et al.*, STB Docket No. 36500, at 3 (filed Nov. 16, 2021) (asserting that CP-KCS single-line service would replace 80,356 UP interline moves, 38,342 BNSF interline moves, 15,439 CSXT interline moves, and 9,540 CN interline movements). To be sure, single-line service can potentially offer shippers substantial benefits and some amount of diversion can be expected from the new CP-KCS single-line service will be able to offer. However, as explained above, Applicants' diversion estimates are overstated because their single-line offerings are frequently inferior to existing, substantially shorter routes and they appear to envision charging commercially unreasonable rates.

[123] *See* Application, Vol. 2, Operating Plan (Exhibit 13) at 85, Table 8.

[124] *See* Application, Vol. 1 at 233.

the vague commitments that Applicants have proffered to date are facially inadequate and would not address the fundamental concern that the merger will eliminate KCS's existing incentive to act as a neutral connecting carrier and work cooperatively with other railroads to serve shippers that KCS cannot today service by itself. CN explains some of the key contours required for an effective gateway commitment in Section IV below.

3. CP's pre-merger actions to foreclose competition from KCS raise serious concerns.

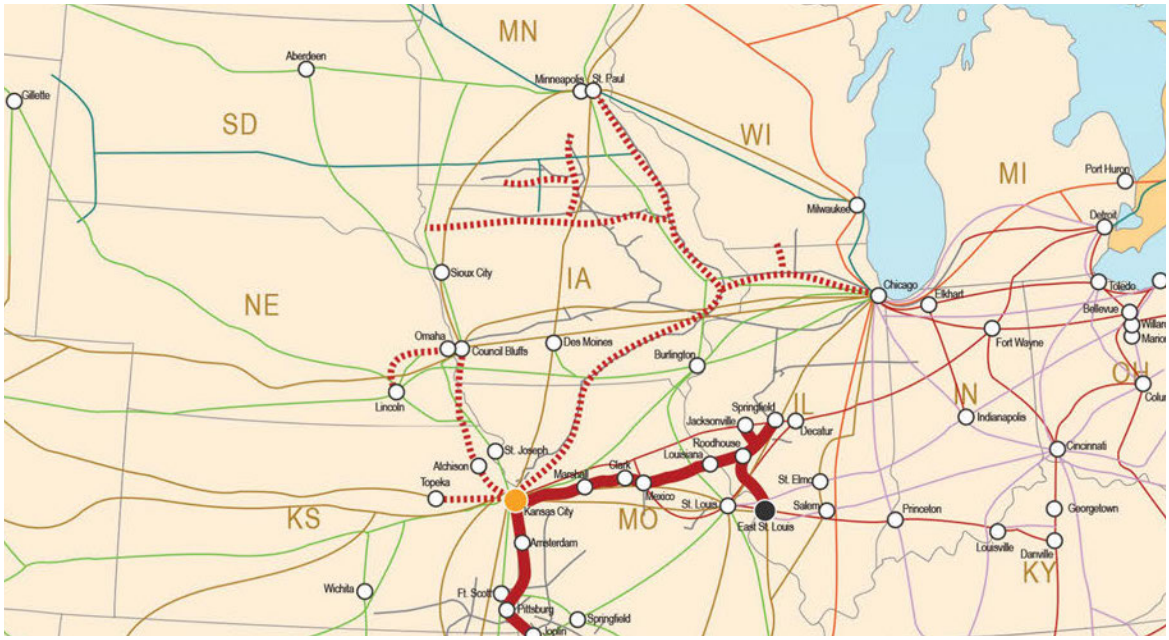
KCS formerly had hundreds of miles of haulage rights over CP lines, which enabled KCS to compete for grain traffic moving from Iowa and Minnesota to destinations on the KCS network, and for chemicals, forest products, and other carload traffic moving between Kansas City and Chicago, based on other agreements with the Dakota, Minnesota and Eastern ("DM&E") and Iowa, Chicago, and Eastern Railway ("IC&E") (collectively, "DME"), entered in 1997.[125] After CP acquired control of DM&E and IC&E, it refused to renew those agreements. As a result, "no customer is jointly served by CP and KCS" today only because CP

[125] Specifically, a "Grain Agreement" that provided KCS with ratemaking authority for the transportation of grain from IC&E-served origins in Iowa and Minnesota to KCS-served destinations in the south-central United States and a "Chicago Agreement" that gave KCS ratemaking authority for rail service over the IC&E route between Kansas City and Chicago for chemicals, forest products, and other carload commodities. *See* Decision No. 11, *Canadian Pacific Railway Company, et al.—Control—Dakota, Minnesota & Eastern Railroad Corp., et al.*, STB Docket No. FD 35081, at 11 (STB served Sept. 30, 2008) ("*CP-DME*"); *see also* Comments of the Kansas City Southern Railway Company and Request for Conditions, *Canadian Pacific Railway Company, et al.—Control—Dakota, Minnesota & Eastern Railway Corp., et al.*, STB Docket No. 35081, at 8–11 filed Mar. 4, 2008).

unilaterally extinguished KCS's access to those customers four years ago, converting customers with access to both KCS and CP into customers solely served by CP.

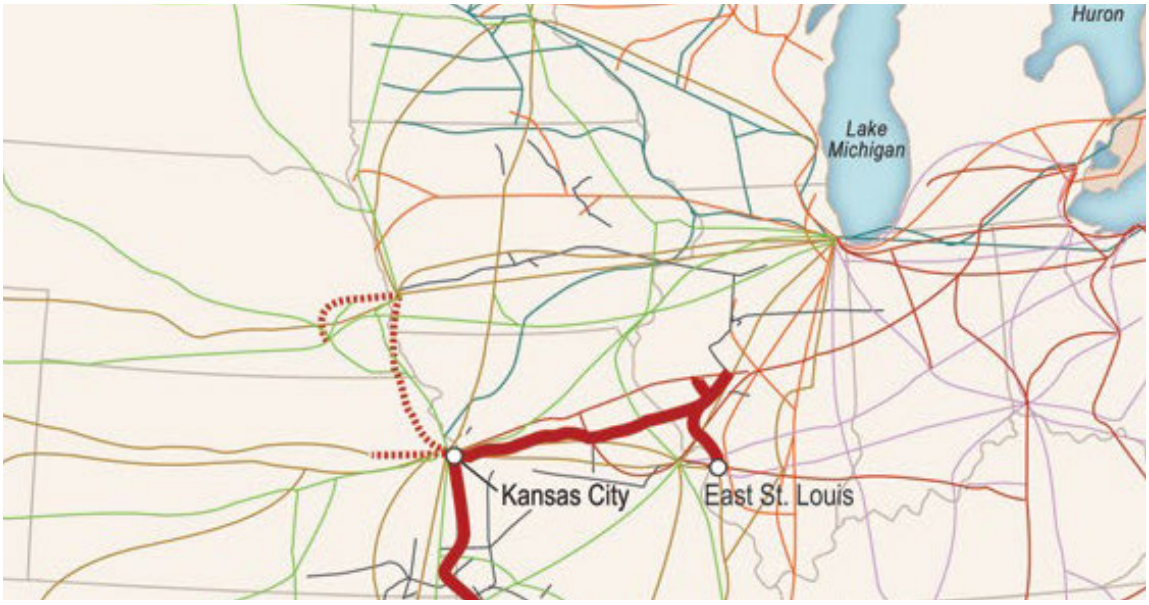
The impact of CP's unilateral action is illustrated by looking at the difference between KCS's system maps in 2017 and 2018. KCS's market reach over CP's lines was markedly reduced after the Grain Agreement expired:

KCS System Map in 2017 (northern portion)[126]



[126] *See* Exhibit 9, Excerpts from 2016 KCS Annual Report. This excerpts the northern portion of the KCS system; the entire map is in Exhibit 9.

KCS System Map in 2018 (northern portion)[127]



CP should not be allowed to claim no competitive harm where the absence of competition results from its own anti-competitive behavior. This history is all the more reason for the Board to ensure strong conditions are in place to prevent CP from using its position to decrease competition on the network.

B. The Application's Inadequate and Unreliable Operating Plan Poses A Serious Risk to the Post-Merger Service of CPKC and Other Rail Carriers.

One of the Board's primary concerns in connection with its review of railroad mergers is their potential for post-consummation service disruptions. When commenters raised objections to CP's and KCS's request that the Board assess their merger under the old rules, they noted that one of the main catalysts for the updated 2001 merger rules was the experience of severe service disruptions that

[127] *See* Exhibit 10, Excerpts from 2017 KCS Annual Report. This excerpts the northern portion of the KCS system; the entire map is enclosed at Exhibit 10.

occurred following several 1990s mergers.[128] For that reason, interested stakeholders asked the Board to apply the new rules so that, among other things, CP and KCS would be required to submit a Service Assurance Plan.

In response, Applicants made a promise to the STB. They pledged that if they were permitted to proceed under the old rules, they would provide an effective equivalent by giving the Board "all the information [the Board] needs to satisfy itself that Applicants have carefully planned for the integration of these railroads and will implement measures to monitor and adjust service levels during the integration process so that shippers' service levels are safeguarded . . ."[129]

Applicants have broken that promise. They did not submit a Service Assurance Plan with the Application, or anything like it. The Application includes only a vague reference to a "Service Assurance Team."[130] However, when asked for documents related to that group in discovery, Applicants responded that there were none. When asked to explain the group in his deposition, CP witness Mr. Brooks admitted that the group had not even been formed yet, and that Applicants had no plans to publicly report on its work, publish any metrics or benchmarks, or develop

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[128] CSX Transportation, Inc. Comments with Respect to Rules Applicable to this Proceeding, *Canadian Pacific Railway Limited, et al.—Control—Kansas City Southern, et al.*, STB Docket No. FD 36500, at 2 (filed Apr. 1, 2021); Comments of the United States Department of Justice, *Canadian Pacific Railway Limited et al.—Control—Kansas City Southern Railway Company, et al.*, STB Docket No. FD 36500, at 8 (filed Apr. 12, 2021).

[129] Applicants' Reply to Objections to KCS Waiver, at 19.

[130] *See* Application, Vol. 1, Verified Statement of John Brooks ¶ 51.

contingency plans for merger-related disruptions.[131] A mere reference to a "Service Assurance Team" that does not currently exist and that apparently would carry out its work in secret plainly does not provide "all the information [the Board] needs to satisfy itself that Applicants have carefully planned for the integration of these railroads . . ."

Indeed, the Operating Plan itself makes clear that Applicants have not carefully planned for post-merger service—or at least that they have not undertaken detailed capacity analyses or developed a detailed capital investment plan that will limit the potential for service disruption. On the contrary, the Application and Operating Plan contain a myriad of inconsistencies and methodological errors that should raise alarms about service disruptions.[132]

First, as discussed above, Applicants' Operating Plan is based on traffic data, a blocking plan, and a train service plan that have not been shown to be truly representative of CP and KCS Base Year (2019) traffic and operations. In addition, Applicants arbitrarily altered the outputs of their MultiRail model (*e.g.*, by removing from their train counts and tonnages any train that did not traverse 25 percent or more of the nodes in a subdivision). These methodological flaws render

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[131] Exhibit 5, Excerpts from Transcript of February 4, 2022 Deposition of John Brooks ("Brooks Dep."), at 210:22–212:18.

[132] *See CSX Corp. and CSX Transp., Inc., Norfolk S. Corp. and Norfolk S. Ry. Co.—Control and Operating Leases/Agreements—Conrail Inc. and Consolidated Rail Corp.*, STB Docket No. FD 33388, 3 S.T.B. 196, 249 (1998) ("We are mindful of the fact that the recent *UP/SP* merger was followed by serious service problems resulting from a variety of factors, a significant one being a rail infrastructure that is inadequate to meet the rapidly increasing demand for rail service ….").

the Operating Plan fatally deficient. This, in turn, means that the Operating Plan cannot reliably support the development of accurate operating statistics (including trains, train miles and GTMs), operating expenses, capital requirements or equipment needs for the merged railroad. These critical components of the Operating Plan must be accurate to assure the Board that service will not be disrupted.

Second, accurate estimates of line density, train counts, and yard activity[133] "are critical to demonstrating that a merged railroad will be able to move projected post-merger traffic over the network without degrading service."[134] Significantly, in their reply to CN's Notice of Responsive Application, *Applicants disavowed their own density data provided in Application Exhibit 14.*[135] Accurate estimates of train counts and line density are essential to identifying line segments where capital investment may be required to maintain fluid train service. Likewise, accurate estimates of yard activity are necessary to identify yards with insufficient capacity to handle the projected post-merger increase in switching work. As demonstrated

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[133] *See* 49 C.F.R. § 1180.8(b)(1) (requiring applicants to provide three specific items in the operating plan for first year in which it will be implemented: (i) traffic density (tonnage) maps or tables for all main and secondary network line segments, (ii) train counts for all main and secondary network line segments, and (iii) a list of all yards anticipated to experience activity growth of 20 percent or more).

[134] Van Dyke Verified Statement at 19.

[135] *See* Applicants' Reply to Canadian National's Description of Anticipated Responsive Application, *Canadian Pacific Railway Ltd., et al.—Control—Kansas City Southern, et al.*, STB Docket No. FD 36500, at 9 n.7 (filed Jan. 28, 2022) (claiming three times that density figures from Exhibit 14 were "figures presented by CN").

above, none of these critical elements of Applicants' Operating Plan is reliable or valid. The traffic density tables and maps contain numerous material errors, for example, omitting unit trains and using unsupported "calibration factors." The projected changes in yard activity portrayed in the Operating Plan are inconsistent with the data in Applicants' environmental filing and significantly underestimate intermodal yard traffic. Contravening Board rules, the Application fails to accurately identify all yards with a projected 20 percent change in activity level (*e.g.*, Port Arthur, Texas).[136] These are not merely "theoretical" failures—inaccurate train counts, density projections, and yard activity estimates can lead to service failures that spread throughout a network.

Third, even assuming that the Operating Plan were valid, the Application is deeply flawed because Applicants chose not to use its outputs to estimate the merged railroad's operating expenses. The GTMs, train-miles, and car-miles generated by an operating plan are customarily used to calculate the merged railroad's operating expenses, equipment needs and capital expenditure requirements. Here, Applicants instead developed a "System Model" that was divorced from the Operating Plan, and they based their operating expense estimates on a spreadsheet of values that was likewise unrelated to the Operating Plan. Like the Operating Plan itself, Applicants' operating expense calculations are unreliable and do not provide a credible basis for the Board to assess the potential for service disruptions.

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[136] Van Dyke V.S. at 24.

Fourth, Applicants' operating expense estimates are based only on "synergy growth" (i.e., the amount of additional traffic that CPKC would gain by diverting shipments from other railroads and trucks) and do not account for the Application's projected "organic growth" (i.e., the amount of additional traffic occurring as a result of general economic and business conditions during Years 1-3). The omission of "organic growth" resulted in massive errors. For example, while the Operating Plan projected an annual increase in train-miles of roughly {{Redacted}} by Year 3, Applicants' operating expense estimates reflect an increase of only {{Redacted}} train-miles per year. Likewise, the Operating Plan projects an increase in GTMs of {{Redacted}}, while operating costs assume an increase of only {{Redacted}} GTMs. The Board can have no assurance that the merged railroad has accurately forecast its operating expenses.

In short, the Application offers no assurance that this major merger will not be disruptive. To the contrary, Applicants' defective and deficient evidence creates ample cause for concern about the potential for serious post-merger services disruption. Moreover, even where the proponents of a merger have submitted realistic and reliable evidence, the Board has, in recent years, imposed a condition providing for post-merger oversight for five years to monitor the actual effects of the merger on rail service. Indeed, the Board has made such oversight a standard condition in major merger proceedings governed by the new merger rules. Under the circumstances present here, and in light of Applicants' unfulfilled promise to

address service assurance in their Application, the Board should impose a five-year oversight period here.

C. Applicants' Unsubstantiated Growth Synergies, Combined with CP's Plan to Not Reduce Earnings, Poses Significant Public Interest Risks.

The proposed CP-KCS merger raises serious financial concerns. Indeed, it flunks the very test that CP has proposed to evaluate the potential financial consequences of a merger of Class I railroads. The combination of the massive debt being assumed by CP with patently unrealistic growth projections will likely leave CP starved for cash. This in turn will inevitably lead to post-merger CP cutting service or leveraging its increased market power to enhance the revenues it needs to service its debt. The merger is thus likely to disserve the public interest, with potentially severe consequences for shippers, interconnecting railroads, and the national economy.

In opposing CN's proposed merger with KCS, CP conducted a financial analysis of the transaction and concluded that:

(1) "CN Will Take on a Very High Level of Debt," "[t]he proposed transaction will CN's leverage to levels that CN has not incurred in the recent past," and CN's debt leverage would be "materially higher than that of any other Class 1 railroad over the last decade;"[137]

(2) After the transaction, CN's rate of return on investment ("ROIC") would fall below its historic and target levels;[138] and

[137] Exhibit 4, Verified Statement of Mark E. Zmijewski ("Zmijewski V.S.") ¶ 20 (quoting Velani V.S. at 6, 8).

[138] *Id.* ¶ 40.

(3) CN had failed to conduct stress testing of its projections using conservative assumptions, demonstrating that CN is "leaving no margin for error," calling into question its ability to repay its debt and retain investor confidence.[139]

Based on this analysis, CP reached the following conclusion:

> CN's targeted rate of return will not be achieved based on the synergies CN forecasts, which will place pressure on CN to boost returns in other ways, such as through cost-cutting, or — more plausibly — reaping the benefits of reduced competition ….[140]

In his attached verified statement, Professor Mark Zmijewski, a Professor at the University of Chicago Booth School of Business, has applied CP's own analysis of the proposed CN-KCS merger to CP's proposed acquisition of KCS.[141]

Straightforward application of CP's financial test shows that:

- "CP is taking on a high level of debt that will substantially increase CP's leverage, and thus, its financial risk;"[142]
- CP's leverage ratios are as high as the CN leverage ratios CP criticized, and higher than its target ratio;[143]
- a credit rating analysis of CP post-acquisition "further corroborate[s] the conclusion of substantially increased financial risk";[144]
- CP's post-transaction ROIC will fall far below its historic and target levels;[145] and

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[139] *Id.* ¶¶ 17, 29.

[140] *Id.* ¶ 5 (quoting Velani V.S. at 11).

[141] To be sure, CN does not agree with all aspects of CP's prior analysis, which CN showed was exaggerated and flawed. But CP cannot now complain about application of its own financial "stress-test" to its proposed acquisition of KCS.

[142] Zmijewski V.S. ¶ 20.

[143] *Id.* ¶ 28.

[144] *Id.* ¶ 20.

[145] *Id.* ¶ 40.

- stress-testing CP's transaction with conservative projections about post-transaction growth and revenues reveals that CP would be subject to the same anti-competitive incentives it predicted for CP.[146]

More specifically, in criticizing CN's leverage in connection with its proposed transaction, CP noted that it would be "materially higher than that of any other Class I railroad over the last decade," highlighting that as of 2020 "the highest leverage amongst other Class I railroads is 3.0 times Adj. Debt/EBITDA, materially lower than the contemplated 4.8 times adjusted debt/EBITDA for CN."[147] That standard is fatal to CP. Applying that very standard, Professor Zmijewski shows CP's "[u]nconsolidated leverage ratios are as high as CN's leverage ratios, and based on both sets of forecasts, CP's leverage ratios are higher than the Target Leverage Ratio of 2.5x."[148] Indeed, Professor Zmijewski demonstrates that CP's $8.2 billion acquisition debt "pushes the leverage ratio above the thresholds associated with investment grade credit rating."[149]

Likewise, again using the same analysis CP did of CN's transaction, Professor Zmijewski has shown that CP's post acquisition ROIC would be substantially lower than CP's historical ROIC and target ROIC of roughly 15%.[150] In its 2021 SEC Form 8K filing, however, CP shows that while it had a ROIC of 16.7 percent in 2020—consistent with its historical ROIC—that number fell dramatically

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[146] *Id.* ¶¶ 36, 38.

[147] *Id.* ¶ 28 (quoting Velani V.S. at 8–9).

[148] *Id.* ¶ 28.

[149] *Id.* ¶ 37.

[150] *Id.* ¶ 40.

to 8.2 percent in 2021 after the KCS acquisition.[151] Even using CP's optimistic forecasts of synergies submitted to the STB, "the expected ROIC in the post-acquisition period ranges between 7.0% and 9.1% and is well below CP's 15% target ROIC even with a full credit of [CP's] Claimed Efficiencies."[152] In this scenario, CP would have to "more than double its unleveraged earnings" to achieve an ROIC close to its 15% target.[153] Critically, moreover, using a more conservative forecast of synergies arising from the merger, "the expected ROIC in the post-acquisition period … falls even lower into the 5.7 to 6.3% range."[154]

Finally, in connection with CN's proposed merger, CP highlighted the importance of stress testing a transaction to determine whether a company can manage its debt if optimistic projections are not realized. Indeed, CP criticized CN for allegedly failing to do so and accused CN of adopting a strategy that "leaves no margin for error."[155] Despite CP's (incorrect) criticism of CN on this point,[156] CP failed to stress test its own proposed acquisition.

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[151] *Id.* ¶ 52.

[152] *Id.* ¶ 56.

[153] *Id.* ¶ 56.

[154] *Id.* ¶ 58.

[155] *Id.* ¶ 29.

[156] *See* Applicants' Reply to Comments on Proposed Voting Trust Agreement, *Canadian National Railway Co., et al.—Control—Kansas City Southern, et al.*, STB Docket No. FD 36514 (filed July 6, 2021), Exhibit 4, Reply Verified Statement of Mark Zmijewski at 15–25 (showing multiple stress tests in extreme financial distress scenarios).

All of the financial risks described above become worse if, as is likely, CP's rosy synergy and growth projections do not come to pass. As described in other sections of these Comments, CP's projections are built on data riddled with errors and illogical assumptions. If CP's claimed revenue gains and operating efficiencies are not realized, then "CP would be $2.2 billion short of the free cash flow that is necessary to de-lever the company by Year 4 to a level consistent with CP's historical leverage."[157] Yet CP's ability to successfully manage the financial risk associated with its transaction depends on CP's ability to de-leverage the company by aggressively repaying its debt.

The post-merger combination of CP's high leverage and low ROIC—and CP's likely inability materially to improve its financial position in the way it forecasts—raise significant public interest concerns under 49 U.S.C. § 11324(b)(5). After asserting that CN could not meet its stated ROIC targets based on the synergies CN projected in connection with its acquisition of KCS, CP asserted that CN "must have based its investment decision on some unstated set of strategic benefits CN expects to realize. The most plausible explanation is that CN's investment is justified by CN's anticipated increase in market power — giving it greater pricing power."[158] That was nonsense—and CN proved its confidence in the projected growth benefits of its then-proposed transaction by committing to a review under the new merger rules with enhanced competitive conditions. But if one accepts that a railroad that

[157] Zmijewski V.S. ¶ 34.

[158] *Id.* ¶ 59.

fails to realize projected merger synergies would be motivated to make up the difference by behaving anti-competitively—these same conclusions "equally apply to, and are equally valid for, CP's acquisition of KCS."[159]

At a minimum, these financial considerations raise serious concerns about the "effect of the proposed transaction on the adequacy of transportation to the public."[160] As CP itself has stated, in the circumstances presented here, CPKC will likely face a cash crunch and seek to boost profits by cutting costs and reducing capital investment, with inevitable, negative consequences for service quality.

IV. CONDITIONS ARE NECESSARY TO ENSURE THE PUBLIC INTEREST IS PROTECTED.

Given the serious deficiencies and inaccuracies of the Application, the Board must impose conditions if it approves the proposed merger to protect the public interest.

A. If the Board Approves the Merger, It Should Order Divestiture of the Springfield Line to CN as a Condition of the Merger

In light of the competitive concerns and threat to the adequacy of post-merger transportation discussed above, the Board should require divestiture to CN's U.S. subsidiary, Illinois Central, of the Springfield Line.[161] Divestiture would (i) ensure that this important asset will be efficiently utilized to preserve the Kansas City to Chicago corridor and to provide an efficient competitive option in the Kansas City to

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[159] *Id.*

[160] 49 U.S.C. § 11324(b)(1).

[161] Notice of Responsive Application at 1.

Chicago corridor, (ii) restore and upgrade the Springfield Line, (iii) improve transportation options and increase rail-to-rail competition, and (iv) take more than 80,000 long-haul trucks off of the nation's highways annually. CN proposes to develop the "Kansas City Speedway" that KCS envisioned prior to its agreement to merge with CP. To this end, CN has committed to invest approximately $250 million to create a high speed, direct route between Kansas City and Chicago.[162] These investments would be used to increase the speed of the entire route to at least 40 mph and to add intermodal and automotive terminal capacity, among other improvements.

This would preserve and foster competition and give rail shippers a far more efficient way of shipping between Kansas City and Chicago, and beyond to Michigan and Eastern Canada. CP's service to these areas is limited by restrictions on its trackage rights and other operational constraints. In contrast to CP, CN would be able to serve intermodal and automotive shippers in Michigan and Ontario over its own tracks, providing shippers with a far more efficient way of reaching Kansas City.

CN projects that this route could annually take more than 80,000 long-haul trucks off the road—more than CP-KCS project for their entire post-merger

[162] *Id.* at 5, 7.

network.[163] This would generate significant environmental benefits in the form of reduced greenhouse gas emissions.

Applicants do not dispute that the Board has authority to order divestiture. The Board has express statutory authority from Congress to order the "divestiture of parallel tracks" as a condition of approving a merger and in furtherance of its authority to ensure a merger serves the public interest.[164]

To be sure, the Board will not "lightly" order divestiture, and any divestiture remedy should be "tailored" to the concerns that have been identified.[165] But CN's proposal satisfies these criteria. CN is seeking only targeted divestiture of the Springfield Line (including ancillary rights to access yard facilities in the Kansas City terminal area). Divestiture here is necessary to ensure that this key asset connecting Kansas City with CN's line to Chicago will remain available to provide efficient and competitive rail service, whereas, absent the requested condition, CP will have little (if any) incentive to deploy the assets efficiently.

Indeed, the antitrust authorities routinely seek divestiture in these circumstances.[166] "Structural remedies are strongly preferred in merger cases

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[163] *See* CN Responsive Application, Verified Statement of David T. Hunt, at 8; Application, Vol. 1 at 23, 310 (asserting that CP-KCS will divert 64,000 trucks to rail annually).

[164] 49 U.S.C. § 11324(c).

[165] Applicants Reply to Responsive Application at 7–8.

[166] *See* U.S. DEP'T OF JUST., ANTITRUST DIV., MERGER REMEDIES MANUAL 6–9 (Sept. 2020); Press Release, U.S. Dep't of Just, Antitrust Div., Just. Department Sues to Block Visa's Proposed Acquisition of Plaid (Nov. 5, 2020), https://www.justice.gov/opa/pr/justice-department-sues-block-visas-proposed-

because they are clean and effective, and they avoid ongoing government entanglement in the market."[167] Divestiture is also needed for CN to make the "Kansas City Speedway" a reality, which will benefit shippers of intermodal and automotive traffic moving between Kansas City, on the one hand, and Detroit and points in Eastern Canada, on the other hand.

Finally, Applicants would not be harmed by this divestiture, except to the extent it would be used to provide meaningful competition to CP's parallel line between Kansas City and Chicago and Detroit.[168] As explained in the Responsive Application in FD 36500 (Sub-No.1), CN would grant KCS haulage rights to serve all customers on the Springfield Line and to interchange with other carriers at interchange points along the Line. No local customer on the Springfield Line would lose a rail option—to the contrary, most of those shippers would gain access to an additional rail alternative.

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acquisition-plaid (asserting, *inter alia*, that Visa's acquisition of Plaid was likely to prevent Plaid from competing with it in the future); *United States v. Bazaarvoice, Inc.*¸ No. 13-cv-0013-WHO, 2014 WL 203966 (N.D. Cal. Jan. 8, 2014), https://www.justice.gov/atr/case-document/file/488846/download (similar); Press Release, Fed. Trade Comm'n, FTC Challenges Illumina's Proposed Acquisition of Cancer Detection Test Maker Grail (Mar. 30, 2021) (similar), https://www.ftc.gov/news-events/press-releases/2021/03/ftc-challenges-illuminas-proposed-acquisition-cancer-detection.

[167] Comments of the U.S. Dep't of Justice, *CSX Corporation and CSX Transportation, Inc., et al.—Control—Pan Am Systems, Inc., et al.*, STB Docket No. FD 36472, at 6 (filed Aug. 26, 2021) ("*CSX-Pan Am*") (citing U.S. DEP'T OF JUST., ANTITRUST DIV., MERGER REMEDIES MANUAL 13 (Sept. 2020)).

[168] *Cf.* Applicants Reply to Responsive Application at 8.

As discussed previously, Applicants apparently do not plan on making the investments necessary to maintain their existing customer base or serve new customers, whereas CN's planned improvements would *increase* the speed at which trains could be operated on the Springfield Line, benefiting all shippers who rely on the line, including those that would choose to ship their freight via CPKC pursuant to the haulage arrangement.[169] CN's planned investment would also increase line capacity, again benefiting all shippers on the line, including those that would choose CPKC haulage service.

B. The Board Should Impose Conditions Needed to Prevent a Combined CP-KCS from Engaging in Foreclosure.

In CN's proposed acquisition of KCS, CN addressed possible "vertical" concerns forthrightly and committed to significant conditions to address them financially. Specifically, CN committed to keep existing gateways open on commercially reasonable terms, not on the basis of maximum regulatory rate-setting methodologies, and to promptly arbitrate disputes before a neutral.[170]

Applicants have conceded that they must provide a remedy to address the vertical concerns raised by the merger, but offered only vague promises: They stated that the combined company will "maintain efficient operations" and "offer commercially reasonable rates and terms."[171] Notably, Applicants did not identify

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[169] *See* CN Responsive Application, Exhibit 13 (Operating Plan).

[170] *See* CN-26/KCS-9, Applicants' Reply to Comments on Proposed Voting Trust Agreement, *CN-KCS* (July 6, 2021), Reply Verified Statement of James Cairns, at 11–12.

[171] *See* Application, Vol. 1 at 233.

what "gateways" are covered by their commitment.[172] Nor did they provide any detail as to how this commitment would be enforced, other than potential Board enforcement on an individual, post-hoc basis, which would be highly inefficient and fail to offer meaningful assurances of competitive joint-line service.[173] Indeed, ultimately revealing the lack of substance to the merging parties' commitment, the Application stated that CPKC will work "to find ways to make these commitments more concrete and readily enforceable."[174]

As explained below, the Board should tighten and strengthen the vague gateway commitments offered by Applicants. In this regard, in their depositions, Applicants' own witnesses effectively conceded the gateway conditions as proposed were not sufficient and that additional protections were appropriate. At the same time, as revealed by the deposition testimony, Applicants appear to intend to enforce an "affected traffic" restriction on the availability of the gateway condition that was not disclosed in the Application. The Board should make clear that Applicants cannot adopt this new restriction. Finally, consistent with gateway conditions that CN offered in connection with its proposed acquisition of CP, the

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[172] Subsequent developments increase the need for skepticism of CP-KCS's "trust us" approach. In discovery responses, CP and KCS named only seven locations that would be covered by their gateway commitment: Chicago, St Paul, Jackson, Shreveport, Laredo, Robstown, and Kansas City). *See* Applicants' Responses to CN's First Discovery Requests at 70. That list omits numerous gateways where CN exchanges traffic with CN or KCS, including gateways at the Canadian border for cross-border traffic (Vancouver; Superior, Wisconsin; Noyes, MN); East Dubuque, Illinois; Superior, WI; Baton Rouge, Louisiana; and Hattiesburg, Mississippi.

[173] *See* Application, Vol. 1 at 233.

[174] *Id*.

Board should adopt binding arbitration as the means to resolve disputes over whether Applicants are offering commercially reasonable terms.

1. Although CN believes the gateway conditions proposed by Applicants remain a second-best remedy with respect to the vertical concerns it has identified,[175] at a minimum, the Board must clarify and strengthen the vague commitments proposed by Applicants. Indeed, CP itself has in the past argued that vague assurances that merging parties will agree to keep gateways open on "commercially reasonable" terms are insufficient to protect competition and that clear and enforceable terms are necessary.[176]

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[175] As discussed above, CN's principal concern is how the merger will change KCS's incentives with respect to working with CN to serve customers in Mexico. Requiring CPKC to grant CN haulage rights between Jackson and Laredo, Texas would be a superior solution to the gateway conditions Applicants have proposed here. A haulage condition would largely eliminate CPKC's ability to block CN from competing because CN would be able to independently price traffic to Laredo, paying a fixed fee to CPKC to haul traffic on CN's account. However, CN understands a key portion of the line between Jackson and New Orleans (the so-called "Meridian Speedway") is jointly owned and operated by NS and KCS. CN further understands the contractual arrangement between NS and KCS may restrict KCS's ability to grant haulage rights, and thus NS would likely contend that the Board cannot order KCS to grant haulage rights to CN. Because of this contractual restriction, CN is not now seeking a haulage condition. Of course, if the Board concludes haulage is the only condition that can fully ameliorate the competitive concerns raised by the CP-KCS merger, it could condition the merger on CPKC securing the necessary rights to provide haulage to CN. At a minimum, however, if the Board approves the merger subject to gateway conditions, the Board should make clear that it will permit parties to seek haulage in the future if the Applicants do not in fact provide commercially reasonable rates and services as they have committed to do.

[176] Brooks Dep., Ex. 5 at 2 (CP comments).

Notably, in his deposition testimony, CP's Chief Marketing Officer, John Brooks, "clarified" the gateway commitments in important respect. The Board should hold Applicants to these representations.

- On behalf of Applicants, Mr. Brooks clarified that a "gateway" means "the interchange point that would link two carriers." He agreed that "any location where two railroads interchange or link together" is a "gateway."[177]

- Mr. Brooks effectively abandoned the Applicant's position that a rate would be "commercially reasonable" merely because it was below the maximum lawful rate that would be permitted by the Board.[178] Instead, Mr. Brooks agreed that to be "commercially reasonable" the rate must be one that would give the customer a "choice" and that a "high gateway rate" that would "force traffic to [Applicants'] single-line routes" "would not be acceptable."[179] Mr. Brooks also acknowledged that this "commercially reasonable" rate commitment applies both to a shipper's request for "interline rates" as well as a competing carrier's request for a "commercially reasonable divisions."[180]

- Mr. Brooks acknowledged Applicants' commitment also extended to non-rate terms. Just as Applicants could foreclose competition by charging high joint rates to shippers that want to reach CP-KCS's rivals, they could also do so by degrading the quality of the interchange with those

[177] Brooks Dep. at 21:23–22:2.

[178] Brooks Dep. at 82:11–14, 103:23–104:2. While Applicants acknowledged that "interline options via these gateways must be commercially viable" to provide meaningful competition to its own service, the Application itself merely stated that they were committing to offering a "Rule 11" rate—that is, a rate between the gateway and a shipper location that could theoretically be challenged before the Board. *See* Application, Vol. 1 at 233.

[179] Brooks Dep. at 210:12–21.

[180] *Id.* at 94:22–95:5, 96:21–97:7.

rivals.[181] Thus, Mr. Brooks acknowledged that Applicants needed "to provide the best quality service we can provide to the interchange."[182]

The need to hold Applicants to Mr. Brooks' clarifications is reinforced by the testimony of Dr. Majure. CP's expert economist, Dr. Majure, admitted that his conclusion that the transaction would not result in anticompetitive foreclosure at locations like Laredo was entirely predicated on the general applicability and the efficacy of the types of conditions imposed by the STB in the *KCS/Tex-Mex/TFM* decision—that is, Dr. Majure did not offer any opinion that the transaction was unlikely to result in harm to competition absent these conditions being universally applied to the combined CP-KCS.[183] And, as the Board knows, these conditions include the right of connecting carriers to challenge a rate, and service commitments to mitigate the possibility of non-price foreclosure.[184]

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[181] *See, e.g.*, *CSX Corp.—Control—Am. Com. Lines, Inc.*, 2 I.C.C.2d 490, 515 (1984) ("In our competitive analysis, we will consider whether the proposed transaction would create or enhance the ability of CSX and ACBL to maintain rates above competitive levels, or to reduce or eliminate nonprice competition, in the relevant transportation markets."); *see also* U.S. Dep't of Justice & Fed. Trade Comm'n, Vertical Merger Guidelines 4 (June 30, 2020) (noting that foreclosure can occur, *inter alia*, by lowering product quality) (withdrawn by FTC on other grounds).

[182] Brooks Dep. at 209:16–210:3; *see also id.* at 209:6–11 (agreeing that with respect to "the quality of interchange service at a gateway" that Applicants' "intent would be to preserve the service there").

[183] Exhibit 6, Excerpts from Transcript of February 7, 2022 Deposition of W. Robert Majure, Ph.D., at 92:7–94:13.

[184] *See* NITL-3, Comments and Statement of Support on behalf of the National Industrial Transportation League, *Kansas City Southern—Control—Kansas City Southern Ry. Co. et al.*, STB Finance Docket No. 34342 (filed Aug. 4 2003) (attached as Exhibit 1 to the Verified Statement of John Brooks). These conditions include an arbitration requirement, as discussed further below.

2. On the other hand, discovery revealed that CP-KCS intend to engraft a limitation on their gateway commitment that was nowhere mentioned in their Application. In his deposition testimony, Mr. Brooks stated for the first time that Applicants' gateway condition only applied to "affected" movements. The thrust of this limitation appears to be that Applicants will only agree to provide commercially reasonable interline rates or division for movements where a combined CPKC would, *for the first time*, be able to provide competing single-line service (or at least a longer portion of the movement that it previously could).[185]

As a matter of economics, foreclosure concerns are not raised solely where a competitor seeks to move traffic between the same origin and destination as a new CP-KCS single-line movement. As the Board has recognized, geographic competition means that movements between different origins and destinations can still compete with each other. Geographic competition exists when a shipper can "obtain[] the same product from a different source, or by shipping the same product to a different destination . . ."[186] DOJ raised this very concern with regard to the CP-KCS merger.[187] Thus, Applicants would still potentially have incentive to

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[185] *See* Brooks Dep. at 89:13–19. Mr. Brooks, however, was unable to articulate a clear standard for what constitutes "affected traffic" that would be entitled to the gateway protection commitment *See id.* at 94:3–7, 123:15–126:9, 126:15–129:25.

[186] *See* Decision, *Market Dominance Determinations—Product and Geographic Competition*, STB Docket No. EP 627, at 1 (STB served Dec. 21, 1998); *see also* Decision, *Major Rail Consolidation Procedures,* STB Docket No. EP 582 (Sub-NO. 1), 2001 WL 648944, at *11 (STB served June 11, 2001).

[187] Comment of the U.S. Dep't of Justice, *Canadian Pac. Ry. Ltd., et al. – Control – Kansas City S. Ry Co., et al.*, STB Finance Docket No. FD 36500 (filed April 12,

refuse to interchange traffic with rivals even via routes where they do not themselves provide single line service, but where that route may be attractive as an alternative to a shipper that they do serve.

In addition, it is not clear whether Applicants' limitation would apply only where the exact same origin-destination is served by a combined CP-KCS. So, for example, it is unclear whether Applicants would provide commercially reasonable access at Kansas City where a rival is seeking to provide interline service from New Orleans to Minneapolis—a route that CP-KCS could provide as single-line service—but where the rival's customer in Minneapolis is not currently a CP customer or able to access CP's facilities in Chicago.

For these reasons, the Board should reject Applicants' attempted after-the-fact limitation on its gateway commitment. It would eliminate competitive protections in instances where Applicants may still have incentive to foreclose competition and invite countless disputes as to whether a particular route qualified.

3. Notwithstanding the foregoing, key aspects of how Applicants' gateway commitments would actually be implemented remain unclear. Applicants acknowledge that "CP isn't promising to agree with shippers on a more concrete standard for what it means for a rate to be commercially reasonable."[188] Rather, as

2021), at 9 ("[R]ailroads can also compete through 'source competition'—that is, the ability of shippers to choose between railroads that can carry their goods to (or receive goods from) different endpoints.").

[188] Brooks Dep. at 100:2–5.

Mr. Brooks conceded, Applicants are "just saying [they will] talk [with shippers] and try to develop some sort of standard."[189]

CN agrees with Applicants in so far as they are saying it would be difficult—if not impossible—to prescribe *ex ante* a rate formula that would ensure a particular rate in connection with a particular movement for a particular route is commercially reasonable. Whether a particular rate or division provides a commercially viable alternative to CP-KCS will depend on a host of factors, such as the length of the move, the nature of the freight, the extent of intermodal, geographic and source competition, and the point of interchange. As Applicants acknowledge, given these factors, there will undoubtedly be "good faith" disagreement as to whether a particular interline rate or division offered by CP-KCS is, in fact, "commercially reasonable."[190]

It is essential that such disputes be resolved promptly and efficiently. Otherwise, CP-KCS could potentially preclude competition simply by threatening to force resolution of any dispute by litigation before the Board. The potential costs involved in such litigation would deter shippers and carriers alike from invoking their rights and the inherent delay would likely render even favorable decisions of little value because the commercial opportunity will have vanished. At a minimum, Applicants should be required to commit to prompt arbitration of all disputes over

[189] *Id.* at 100:6–19.

[190] *Id.* at 102:7–103:2.

commercially reasonable rates, similar to the commitment in the NITL settlement agreement that was incorporated into the *Tex Mex* conditions.[191]

C. Applicants Should Be Required to Provide A Service Assurance Plan or Its Equivalent.

In light of the errors, inconsistencies, and illogic embedded in Applicants' Operating Plan, which cascade into the Application's projected operating expenses and investment planning, service disruptions are a serious concern. Applicants received approval to proceed under the old rules after expressly committing to provide the Board with adequate information to ensure that the merger would not result in service disruptions. Yet the Application provides no such assurance and gives rise to serious concerns. In this setting, the Board should require Applicants to provide a Service Assurance Plan or its equivalent. Merger applicants under the old rules have provided such plans,[192] and it is clearly appropriate to require such a plan here.

The Board should also impose an oversight period of at least five years. The Board has done so in past mergers, and Applicants would be required to do so

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[191] National Industrial Transportation League (NITL) Letter Filing, STB Docket No. FD 34342 (filed Aug. 5, 2003), Attached Agreement, at 3 § 6.

[192] *See, e.g.*, Decision No. 10, *Canadian National Railway Company, et al.—Control—Wisconsin Central Transportation Corporation, et al.*, STB Docket No. FD 34000, at 20 (STB served Sept. 7, 2001) ("[E]ven with a *minor* transaction, there is a need to assure the Board that service is not compromised, particularly during the implementation of the transaction. With this in mind, applicants have provided a Service Assurance Plan … to assure the Board and affected shippers that all aspects of the implementation planning process have been fully considered." (emphasis added)).

under the new rules.[193] The oversight period should include required reporting on whether merger benefits have been achieved, compliance with conditions, and any merger-related harms. The Board should retain jurisdiction to impose additional conditions as needed and to entertain additional conditions requests from parties. The deficiencies in this Application and operating plan require no less.

CONCLUSION

For the reasons stated in these Comments, Applicants have failed to carry their burden to show that this merger is in the public interest. At the very least, the conditions requested, including the divestiture of the Springfield Line to CN, should be imposed to prevent the harms to public interest that the merger threatens.

[193] *See* Final Rules, *Major Rail Consolidation Procedures*, STB Docket No. EP 582 (Sub-No. 1), at 10 (STB served June 11, 2001); *CSX/NS-Conrail,* 3 S.T.B. at 217 ("we are establishing oversight for 5 years so that we may assess the progress of implementation of the CSX/NS/CR transaction and the workings of the various conditions we have imposed").

Respectfully submitted,

Sean Finn
Olivier Chouc
CN
935 de La Gauchetière Street West,
16th Floor
Montreal, QC H3B 2M9
CANADA

Kathryn J. Gainey
CN
601 Pennsylvania Ave, NW
Suite 500, North Building
Washington, DC 20004
Kathryn.gainey@cn.ca

/s/ Raymond A. Atkins
Raymond A. Atkins
Terence M. Hynes
Matthew J. Warren
Sidley Austin LLP
1501 K Street, N.W.
Washington, DC 20005
(202) 736-8000
ratkins@sidley.com

Counsel for Canadian National Railway Company, Grand Trunk Corporation, and CN's Rail Operating Subsidiaries

Dated: February 28, 2022

CERTIFICATE OF SERVICE

I hereby certify that on this 28th day of February 2022, a copy of the foregoing Comments on Application and Request for Conditions was served by first class mail or email on the service list for Finance Docket No. 36500.

/s/ Matthew J. Warren
Matthew J. Warren

Exhibit 1

Verified Statement of David Hunt

BEFORE THE
SURFACE TRANSPORTATION BOARD

STB FINANCE DOCKET NO. 36500

CANADIAN PACIFIC RAILWAY LIMITED; CANADIAN PACIFIC RAILWAY COMPANY; SOO LINE RAILROAD COMPANY; CENTRAL MAINE & QUEBEC RAILWAY US INC.; DAKOTA, MINNESOTA & EASTERN RAILROAD CORPORATION; AND DELAWARE & HUDSON RAILWAY COMPANY, INC. – CONTROL – KANSAS CITY SOUTHERN, THE KANSAS CITY SOUTHERN RAILWAY COMPANY, GATEWAY EASTERN RAILWAY COMPANY, AND THE TEXAS MEXICAN RAILWAY COMPANY

CN'S COMMENTS ON APPLICATION AND REQUEST FOR CONDITIONS

Verified Statement of David T. Hunt

February 28, 2022

PUBLIC VERSION

Contents

1. Qualifications....1

2. Assignment and Summary of Findings....2

3. Applicants' Incremental Traffic and Revenues of $1.02 Billion Are Overstated by $520 Million and Are Inaccurate....4

4. Applicants' Rail-to-Rail Diversion Estimates Are Not Based on a Credible Methodology and Are Overstated by More Than $133 Million....7

4.1 The simplistic modeling methodology employed by witnesses Brown and Zebrowski ignores the effect of route circuity and diverts traffic from customers over longer CPKC routes....8

4.2 Revenue for post-merger diverted traffic is overstated by $47.4 million due to errors assuming CPKC revenues after the merger exceed the rates currently charged to customers....14

4.3 Diversion estimates include arbitrary and unsubstantiated additions for grain and lumber traffic that overstate revenue by $86 million....20

4.4 Applicants made a currency conversion error of Canadian dollars to US dollars that further inflated the revenues likely to be achieved from diverted traffic....22

5. Certain Additional Claimed Incremental Revenues of $386.7 Million Are Unsubstantiated or Unrelated to the Merger....24

5.1 Nearly $158.1 million (40 percent) of the revenue from additional traffic opportunities posited by witnesses Wahba and Naatz is attributable to traffic gains that are unrelated to the merger....25

5.2 Additional diversion revenue opportunities of $107 million involve impractical, circuitous, and complicated routes....27

5.3 Witnesses Wahba and Naatz claim approximately $122 million in diversions that were apparently "missed" by Applicants' diversion experts in LPG, grain, and perishable commodities....32

Appendix A. Resume of David Hunt....37

1. Qualifications

My name is David T. Hunt. I am a Vice President with Oliver Wyman, a global general management consulting firm with more than 60 offices in 31 countries. My office address is 1 University Square, Suite 100, Princeton, NJ 08540.

Oliver Wyman is a leading general management consulting firm. We maintain one of the largest practices in the world dedicated to the transportation and logistics sectors. Oliver Wyman's transportation clients include national and regional governments on six continents, as well as many of the world's largest users of rail services, railroads, motor carriers, leasing companies, and industrial and consumer manufacturing firms.

I have been a consultant in the transportation sector for more than 35 years. I joined Oliver Wyman in 2008, specializing in strategic planning, regulatory issues, and operations for freight railroads and other freight transportation providers. Prior to joining Oliver Wyman, I was a consultant at Cambridge Systematics, Wilbur Smith Associates, and ALK Associates. While at ALK from 1983 through 2000, I provided services to clients in connection with all of the Class I railroad mergers that occurred during that time period. I also was responsible for the annual calibration of and updates to ALK's Advanced Traffic Diversion Model that was used in ICC and STB merger proceedings. I hold a bachelor's degree in civil engineering from West Virginia University and a master's degree in civil engineering and operations research from Princeton University. My resume is included in Appendix A.

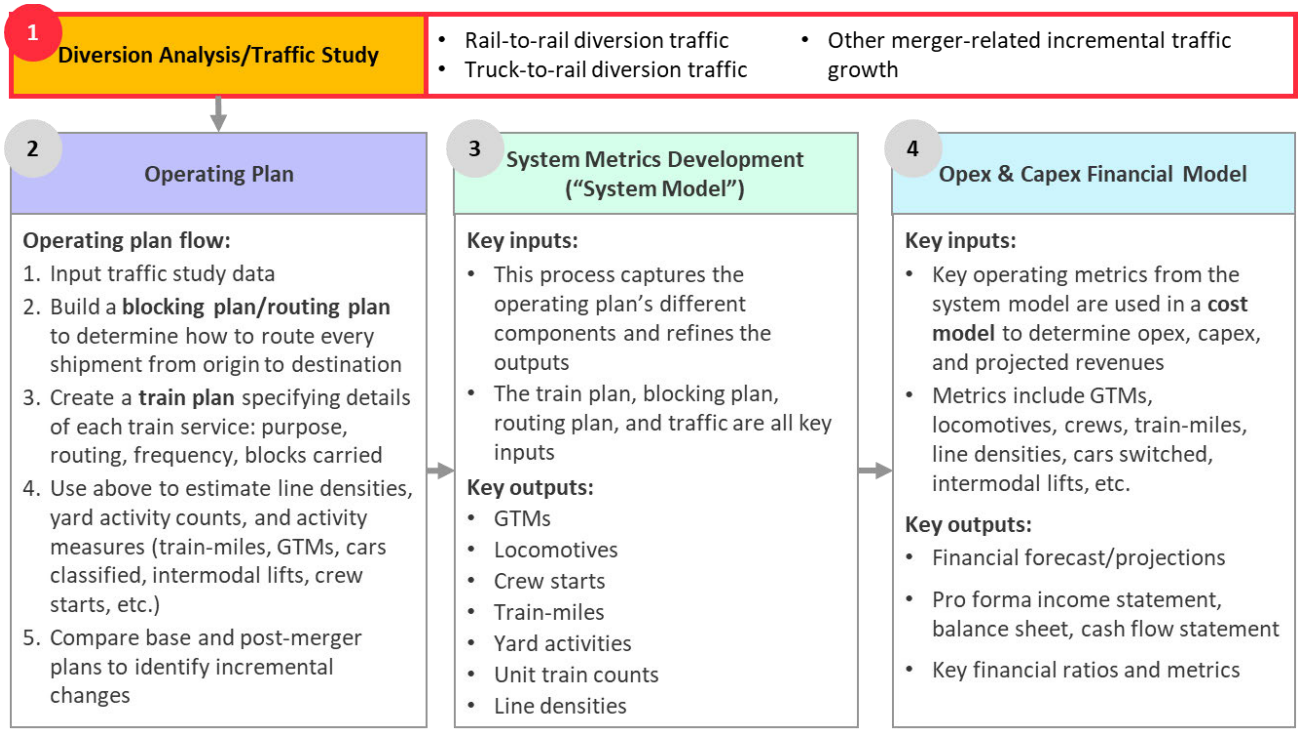
2. Assignment and Summary of Findings

I have been asked to review and comment on Applicants' testimony regarding the traffic diversions and associated revenues that are likely to be achieved by the merged CPKC as a result of the proposed transaction. Specifically, my testimony focuses on the traffic and revenue synergies from rail-to-rail diversions projected by witnesses Richard W. Brown and Nathan S. Zebrowski, the truck diversions posited by witness Mutén, and the additional traffic and revenue sources identified by witnesses Jonathan Wahba and Michael J. Naatz (in their corresponding Verified Statements and work papers to the Application).

As shown in Exhibit 2-1, complete and accurate traffic and revenue data is the fundamental building block of the major merger application required by Board regulations.[1] Accurate operating plans, operating statistics, and financial exhibits must be predicated on reliable traffic projections. As shown below, Applicants' traffic diversion estimates (and associated revenues) are vastly overstated. Exhibit 2-1 illustrates the relationship between traffic projections and other elements of a merger application.

[1] The required content applicable to the CP/KCS major merger application is set forth at 49 CFR 1180.7 through 49 CFR 1180.11 (2000).

Exhibit 2-1: Elements of a reliable merger plan: the operating plan and financial model are dependent on the accuracy of Applicants' traffic projections[2]



The Application claims that the proposed merger will generate $1,021.9 million in incremental revenue[3] from rail-to-rail diversions, truck-to rail diversions, and (what Applicants characterize as) "growth initiatives."[4] The Applicants' traffic diversion studies, however, are based on flawed methodologies, unsupported assumptions, and erroneous calculations that render their traffic and revenue estimates invalid. Indeed, *Applicants' merger-related revenue projections appear to be overstated by more than $520.2 million. When corrected, Applicants' adjusted merger-related revenue projection is $501.8 million. The overstatement is more than*

[2] Exhibit 2-1 depicts the logical connection between traffic, operating, and financial elements of the application explicitly cited in the Canadian National-Illinois Central and Norfolk Southern-Conrail merger proceedings. *See* Finance Docket No. 33556, Railroad Control Application, Surface Transportation Board, July 1998 (CN-IC merger) and Finance Docket No. 33388, Railroad Control Application, Surface Transportation Board, June 1997 (Conrail merger). Oliver Wyman has been unable to find a clear connection between Applicants' traffic studies, operating plan, and financial model in the Canadian Pacific-Kansas City Southern Application or work papers.
[3] Application Vol. 1, p. 141. All revenue figures in this report are in 2019 US dollars.
[4] FD 36500 – Work Paper – HC – Growth Initiative Calculations.xlsx.

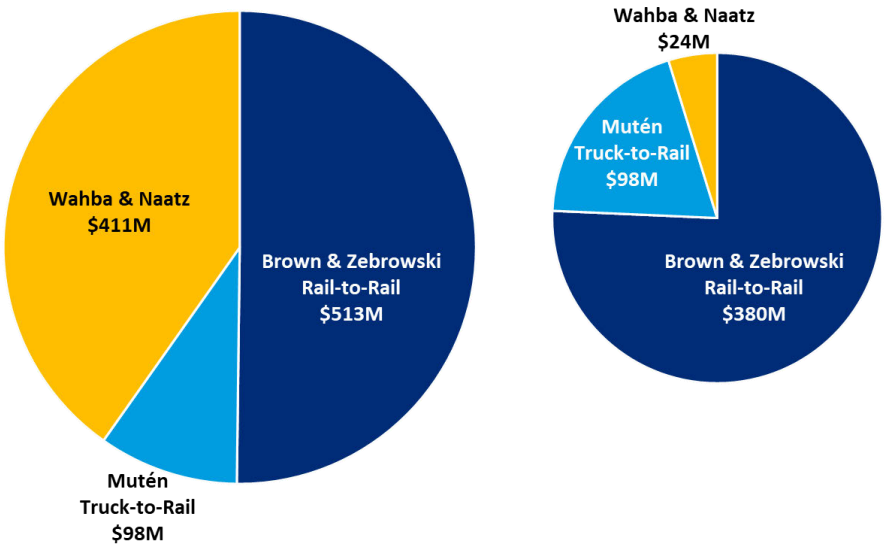
100 percent; i.e., the revenue gains claimed by Applicants are more than double the plausible incremental revenues that could be supported based on the traffic data provided in the Application and supporting work papers.

3. Applicants' Incremental Traffic and Revenues of $1.02 Billion Are Overstated by $520 Million and Are Inaccurate

Exhibit 3-1 identifies the amount of incremental revenue that Applicants' traffic witnesses claim the CPKC system will gain by Year 3 by diverting traffic from other railroads and motor carriers and from certain new business opportunities, and the amount of such incremental revenue that is realistic based on my testimony.

Exhibit 3-1: Applicants' projected incremental revenue gains from the proposed merger (left chart) and corrected totals (right chart)[5]

In 2019 US dollars



[5] Verified Statement of Richard W. Brown and Nathan S. Zebrowski, Application Vol. 2, p. 166, Table 28; Verified Statement of Bengt Mutén, Application Vol. 2, pp. 223-224; FD 36500 - Work Paper - HC - Growth Initiative Calculations.xlsx.

Reliable traffic volume and revenue estimates are critical to virtually every other element of the Application. A feasible operating plan must be based on an accurate count of cars and trains moving along the network. The incremental increase in traffic volume likewise informs decisions regarding the capital investment required to handle that traffic safely and efficiently. Accurate train data is essential to measuring the environmental impacts of the proposed transaction. From a financial perspective, the reliability of incremental traffic and revenue estimates determines the accuracy of Applicants' expense projections and pro forma financial exhibits.

The incremental traffic and revenue estimates presented by Applicants' traffic witnesses are inaccurate and vastly overstated, for a variety of reasons. In particular, I find that:

- The rail-to-rail traffic diversions projected by witnesses Brown and Zebrowski are based on critical conceptual flaws and significant calculation errors that result in a substantial overstatement of the incremental revenue likely to be achieved as a result of the merger. Witnesses Brown and Zebrowski apply fixed diversion percentages of 25, 50, or even 75 percent that are unsupported by any credible rationale. The Brown and Zebrowski traffic study also contains substantial calculation and conceptual errors. Finally, witnesses Brown and Zebrowski inflated their diversions of grain and forest products traffic with a random, unsupported five percent "market share increase."[6] The result of these flaws in the Brown and Zebrowski analysis is an overstatement of rail-to-rail traffic diversion revenues attributable to the proposed merger of at least $133 million.
- Applicants took the unusual step of "supplementing" the diversion estimates sponsored by their expert traffic witnesses (Brown, Zebrowski, and Mutén) with a verified statement by CP witness Wahba and KCS witness Naatz, who purport to identify "additional revenue opportunities" for the merged CPKC system. These additional traffic volumes and revenues – *which account for $411 million or 40 percent of the total incremental revenue gains set forth in the Application* – are based on unrealistic

[6] Brown and Zebrowski V.S., Application Vol. 2, ¶42 and ¶81.

assumptions and unsupported claims, including attributing to the merger *traffic movements in which CP and/or KCS already participate today* and other traffic gains that were excluded by Applicants' expert traffic witnesses. Those assumptions, inconsistencies, and conceptual errors invalidate as much as $387 million (out of the total of $411 million) in additional revenue opportunities posited by witnesses Wahba and Naatz.

In all, I estimate the $1,021.9 million in new revenue estimated by the Applicants' diversion witnesses should be reduced to at most $501.8 million in legitimate, plausible merger-related revenue gains. Corrections required to produce more realistic post-merger incremental revenue gains are shown in Exhibit 3-2.

Exhibit 3-2: Applicants' diversion estimates adjusted for incorrect assumptions, inconsistencies, and conceptual errors[7]

$ millions

Category		Adjusted Total
Applicants' Estimated New Revenue - Total	$ 1,021.9	
Brown & Zebrowski Overstatement of Revenue Due to Error	$ (47.4)	$ 974.5
Brown & Zebrowski Grain and Lumber Arbitrary 5% Gain	$ (86.0)	$ 888.5
Wahba & Naatz Crude Oil Movement Announced in 2019, Prior to Merger	$ (158.1)	$ 730.4
Wahba & Naatz Lazaro Cardenas Intermodal Unlikely Due to High Circuity	$ (107.0)	$ 623.4
Wahba & Naatz "Missed" by Other Experts - Grain	$ (36.7)	$ 586.7
Wahba & Naatz "Missed" by Other Experts - LPG	$ (30.5)	$ 556.2
Wahba & Naatz "Missed" by Other Experts – Perishables	$ (54.4)	$ 501.8
CPKC Revenue Adjusted for Mistakes, Overreach, and Poor Assumptions		**$ 501.8**
Revenue Overstatement		**$ 520.2**
Percent Revenue Overstated		**104%**

For the Applicants' diversion estimates to be achievable, shippers would have to agree to use longer rail routes and pay higher rates. The Applicants acknowledge that *the average route for rail-to-rail diversions on CPKC is 217 miles longer than the average route on current rail*

[7] Oliver Wyman work paper Corrected Revenue Summary.xlsx.

carriers.[8] Increased route length leads to increased shipment times, which impacts rail customers through the need for larger fleets to move the same traffic. Furthermore, as I demonstrate in Section 4.2, there are numerous cases where the incremental revenue assigned to CPKC greatly exceeds the revenue received by the existing carrier, in some cases by over 60 percent.[9]

4. Applicants' Rail-to-Rail Diversion Estimates Are Not Based on a Credible Methodology and Are Overstated by More Than $133 Million

Applicants' estimated rail-to-rail traffic diversion revenues are conceptually and arithmetically wrong. Revenues are significantly overstated for the following reasons:

- Witnesses Brown and Zebrowski use a simplistic rule-based modeling methodology that ignores the impact of route circuity on how divertible traffic is likely to be. This conceptual error undermines the validity of Applicants' operating plan, capital investment evidence, and assessment of environmental impacts.
- The methodology used by witnesses Brown and Zebrowski to allocate revenue to diverted traffic leads to an implausible result: According to their calculations, CPKC's post-merger revenues from diverted traffic shipments will, in many instances, substantially exceed the revenue currently earned by the railroads hauling that traffic today. This leads to at least a $47.4 million overstatement of revenue.
- Brown and Zebrowski's traffic diversion model applies simplistic rules that are not supported by data or other credible evidence. Moreover, their projected diversions include unjustified additions of traffic outside the model. Despite modeling specific origin-destination based grain and forest product shipments that could divert to CPKC, Brown and Zebrowski add to their totals an additional 5 percent market share increase

[8] Brown and Zebrowski V.S., Application Vol. 2, p. 132, Table 6.
[9] FD 36500 – Work Paper – HC – 8 - Diversion Identification.xlsx, Calculations tab, Row ID=6422. CN received {{ }} for a shipment from Jackson, MS to Chicago, IL. CPKC was given {{ }} in incremental revenue for this projected diversion, in constant 2019 dollars. This is an increase of 62 percent.

for these products, which they distribute equally across multiple locations.[10] These flaws result in an $86 million overstatement of revenue.

- An error in converting Canadian dollars to US dollars further inflates some of the revenues associated with diverted traffic.

I estimate that, collectively, these fundamental flaws in witnesses Brown and Zebrowski's analysis generate an overstatement of achievable revenue for the merged railroad from rail-to-rail diversions of more than *$133 million or 26 percent of the total of $513 million in rail-to-rail diversions projected by those witnesses*.

4.1 The simplistic modeling methodology employed by witnesses Brown and Zebrowski ignores the effect of route circuity and diverts traffic from customers over longer CPKC routes

The relationship between route length and route choice is a well-established concept in transportation modeling.[11] This idea is both simple and intuitive: the least-cost route between an origin and a destination is likely to capture the greatest share of traffic, where cost is a function of distance.[12] The traffic diversion models used in prior Class I railroad merger cases have consistently recognized this principle. Indeed, Applicants' own witness, Bengt Mutén, testifies that "distance between end points" was found by his former colleagues at Reebie Associates to be one of "the primary drivers of intermodal market share."[13] CP witness Mutén's truck-to-rail diversion model includes two parameters based on route distance: overall truck distance and the difference between truck and rail distances.[14]

[10] Brown and Zebrowski V.S., Application Vol. 2, ¶42 and ¶81.
[11] Route choice models use cost or travel time, both of which are a function of distance. *See, e.g.,* Chapter 7.2 "Route Choice," in Transportation Demand Analysis, Adib Kanafani, McGraw-Hill Book Company, New York, NY, 1983.
[12] The Board's Uniform Rail Costing System (URCS) lists distance as one of the mandatory parameters used in the railroad costing process. "Railroad Cost Program," Surface Transportation Board, User's Manual, December 2011, p. 1.
[13] Mutén V.S., pp. 17-18, ¶46.
[14] Mutén V.S., pp. 17-18, ¶46.

From a rail customer perspective, switching traffic from a shorter to a longer route can lead to increased transit times and higher transportation costs. If customers use private railcars, increased transit times require the purchase or lease of additional cars to move the same quantity of traffic, since the cycle time (origin to destination and back to origin) for each car will increase. Longer transit times also lead to increased inventory costs, since a shipment in transit is not available for productive use. Finally, switching to longer-distance routes increases the variable costs of a shipment, and these increased costs must be absorbed either by the railroad or the customer.

It appears that witnesses Brown and Zebrowski initially recognized the importance of distance in rail market share. They conducted a statistical analysis comparing the relationship between rail carriers' length-of-haul and their historical market share. But the results of their analysis – which purported to find "a weak correlation between the relative shares of traffic among the available routing options and the movement mileage for those options"[15] – are utterly inconsistent with both prior traffic diversion modeling and witness Mutén's truck-to-rail diversion analysis.

Using their flawed analysis as justification, witnesses Brown and Zebrowski set aside customary traffic diversion modeling principles and instead applied a set of fixed percentage-based diversion rules that are not supported by data. In an attempt to dismiss the competitive advantage enjoyed by a carrier whose route is shorter than that of a potential new entrant, witnesses Brown and Zebrowski arbitrarily assumed that any time CPKC will compete head-to-head with another railroad for single-line service, CPKC will divert a 25 percent share of traffic

[15] Brown and Zebrowski V.S., Application Vol. 2, p. 131; Mutén V.S., pp. 17-18, ¶46; FD 32549, Mark Hornung, V.S., ALK Associates.

regardless of the competing carriers' respective lengths of haul,.[16] They assigned this same arbitrary diversion percentage rule to each traffic lane involving a single-line competitor they studied, regardless of distance, asserting (without explanation or analysis of particular movements) that their percentages are "reasonable and conservative."[17]

To demonstrate the fallacy of their assumption, consider the example in Exhibit 4-1. It shows that witnesses Brown and Zebrowski assigned the same 25 percent traffic diversion share regardless of whether the new CPKC single-line service route would be shorter than the existing route – such as New Orleans, LA to Superior, WI – or drastically longer, such as New Orleans to Elkhart, IN. It is simply not credible to believe that CPKC could divert the same percentage of traffic in these two lanes; nor do witnesses Brown and Zebrowski support their conclusion with any logical or established traffic analysis. The fact that Brown and Zebrowski mechanically attribute the same diversion percentage to these vastly different scenarios highlights the degree to which their approach is flawed.

[16] Brown and Zebrowski V.S., Application Vol. 2, p. 132, Table 6 and p. 183, ¶16.
[17] Brown and Zebrowski V.S., Application Vol. 2, p. 183, ¶16.

Exhibit 4-1: Witnesses Brown and Zebrowski use the same diversion percentage, regardless of whether CPKC has a shorter route or much longer route[18]

Origin	Destination	Current RR	Current RR Miles	CPKC Miles	Difference in Miles	Assigned Diversion Percentage
New Orleans, LA	Superior, WI	BNSF	2023	1675	-348	25%
New Orleans, LA	Elkhart, IN	NS	1075[19]	1476	+401	25%
Chicago, IL	San Angelo, TX	BNSF	1274[20]	1499	+225	25%

In total, witnesses Brown and Zebrowski diverted a total of 66,845 cars and containers that now move in single-line service at a constant rate of 25 percent, regardless of the difference in length of haul between the incumbent carrier's single-line route and the proposed CPKC route.[21] It is important to note that, for these movements, the creation of a new CPKC single-line route would not, in itself, confer any advantage on the merged carrier, since an incumbent railroad already offers single-line service.

Even if Applicants' assumed diversion of 25 percent for lanes with existing single-line service were correct on average (which is impossible to determine, since it is not based on any data), this rule still generates serious downstream problems. For example, in Exhibit 4-1, if 25 percent were a realistic average, then CPKC would, in all likelihood, gain more than 25 percent of the traffic moving from New Orleans to Superior and less than 25 percent of the shipments from New Orleans to Elkhart. But witnesses Brown and Zebrowski mechanically diverted *exactly* 25 percent of both movements. The third example in Exhibit 4-1, from Chicago, IL to

[18] FD 36500 – Work Paper – HC – 8 - Diversion Identification.xlsx, Calculations tab, Row ID (column A) 14638, 14709, and 13350. Current RR Miles from column AB and CP/KCS miles from column BI. Diversion percentage from column BZ.
[19] FD 36500 – Work Paper – HC – 8 - Diversion Identification.xlsx, Calculations tab, Row ID (column A) 14709 states the distance is 581 miles; however, this appears to be an error, so the PC*Miler|Rail ver. 27 distance of 1,075 miles was used.
[20] FD 36500 – Work Paper – HC – 8 - Diversion Identification.xlsx, Calculations tab, Row ID (column A) 13350 states the distance is 1,104 miles; however, this appears to be an error, so the PC*Miler|Rail ver. 27 distance of 1,274 miles was used.
[21] FD 36500 – Work Paper – HC – 8 - Diversion Identification.xlsx. The 66,845 value was calculated by filtering Status to "Final" (column BJ) and New Percent to "25%" (column BZ) and then summing the Diversion Units (column CA).

San Angelo, TX, also receives the same 25 percent diversion, despite the CPKC route being 225 miles longer than the existing BNSF route.

This discrepancy impacts the operating plan, assessment of environmental impacts, capital investment evidence, and assumptions about impacts of the proposed merger on other railroads. Applying such a broad and unsupported diversion assumption has consequences for multiple components of the Application, including:

- **Operating plan**: Witnesses Brown and Zebrowski's indiscriminate diversion of 25 percent of the traffic in each diverted lane, rather than accounting for the real-world differences between scenarios like those in Exhibit 4-1, results in an overstatement of post-merger traffic volume in some lanes and an understatement of post-merger traffic volume in other lanes. This, in turn, means that the operating plan fails to assign the correct number of railcars and trains to the correct rail lines and yards. For the example in Exhibit 4-1, a realistic operating plan would need to provide for handling less traffic heading northeast to Elkhart and more traffic heading northwest to Superior from New Orleans.
- **Assessment of environmental impacts**: Spreading diverted traffic equally across rail lines dilutes the impact on routes where CPKC truly has an advantage in length-of-haul that might lead to diversion percentages above the arbitrary 25 percent value used by witnesses Brown and Zebrowski. Conversely, the use of a constant diversion percentage will lead to overstatement of volume increases on lines where CPKC has a distance disadvantage. Applicants' approach of applying a constant diversion percentage generates unreliable information on traffic volume increases by route, which is a primary input to the environmental assessment.
- **Capital investment evidence**: By potentially understating railcar and train counts on routes where CPKC could realistically achieve above-average diversion percentages due to length-of-haul advantages, the capital investment evidence may not properly reflect the infrastructure necessary to support the number of trains on those lines and in those yards.

- **Impact of merger on other railroads**: In the example in Exhibit 4-1, BNSF might experience more diversions than estimated by witnesses Brown and Zebrowski and NS less diversions. The true impact of the merger on other railroads, including on railroads' line capacity, operating plans, and capital plans, cannot be determined without an assessment of traffic diversions that includes length-of-haul impacts as part of diversion modeling.

The flaws in witnesses Brown and Zebrowski's mechanical approach likewise impacts their other estimated diversions. Witnesses Brown and Zebrowski estimate rail-to-rail diversions based on flat percentages of 25, 50, or 75, based on five "rules" that are summarized in Exhibit 4-2. But witnesses Brown and Zebrowski do not consider length-of-haul differences when applying these rules and percentages, and they offer no data, analysis, or other evidence to support such inflexible percentage-based diversion assumptions.[22]

Exhibit 4-2: Witnesses Brown and Zebrowski diversion percentages[23]

Traffic Type	Diversion Percentage/ Market Share
1. New CPKC Single-Line Moves Replacing Other Railroads' Interline Moves	50%
2. New CPKC Single-Line Moves Replacing Other Railroads' Single-Line Moves	25%
3. CP or KCS Interline Moves Converted to CPKC Single-Line Move Closed by CPKC	75%
4. Other CP or KCS Interline Moves Converted to CPKC Single-Line Move	50%
5. Remove Bridge Carrier on CPKC Route	75%

While differences in length-of-haul are important in any analysis of potential traffic diversions, they are of particular relevance in this case, because many of the CPKC single-line routes that will be created by the merger will be substantially longer than incumbent routing options. For example, in the New Orleans, LA to Elkhart, IN example contained in Exhibit 4-1, witnesses *Brown and Zebrowski divert railcars to a CPKC route that is 400 miles longer than*

[22] Brown and Zebrowski V.S., Application Vol. 2, p. 183, ¶16.
[23] Brown and Zebrowski V.S., Application Vol. 2, p. 134, Table 7.

the existing NS route. The CPKC route must move a shipment northwest on KCS from New Orleans to Kansas City and then head east from Kansas City to Elkhart on CP, whereas the NS route can move a shipment directly northeast from New Orleans to Elkhart. Witnesses Brown and Zebrowski were clearly aware of this fact – their testimony includes a table showing the average incremental circuity of the merged CPKC routes, summarized below in Exhibit 4-3.[24] As Exhibit 4-3 shows, *new CPKC single-line routes will be, on average, 217 miles longer than the routes over which potentially divertible traffic actually moves today*. Yet, Brown and Zebrowski apparently concluded that such substantial route-distance disadvantages would not affect CPKC's ability to divert traffic from carriers with more efficient routes.

Exhibit 4-3: Overall average mileage characteristics for traffic eligible to be diverted[25]

Length-of-Haul	Current Railroad	CPKC	Difference
Average miles	1,853	2,070	+217

Given that many of the CPKC routes to which witnesses Brown and Zebrowski diverted traffic are substantially longer than the routes over which that traffic moves today,[26] Brown and Zebrowski's estimate that 216,675 carloads and containers will be diverted to the CPKC network, regardless of circuity differences, is simply not credible.

4.2 Revenue for post-merger diverted traffic is overstated by $47.4 million due to errors assuming CPKC revenues after the merger exceed the rates currently charged to customers

The revenue gain for CPKC from diverted traffic should logically reflect the approximate revenue that would be lost by the railroads that currently haul that traffic. Indeed, witnesses Brown and Zebrowski "considered it appropriate to assume that CP/KCS would be *required to*

[24] Brown and Zebrowski V.S., Application Vol. 2, p. 132.
[25] Brown and Zebrowski V.S., Application Vol. 2, p. 132, Table 6.
[26] Brown and Zebrowski V.S., Application Vol. 2, p. 159.

offer rate reductions averaging five percent in order to attract traffic away from existing single-line service."[27] Yet the incremental revenue per diverted carload claimed by witnesses Brown and Zebrowski in many cases exceeds the rates currently charged by the incumbent carrier (in constant 2019 dollars). If Brown and Zebrowski's revenue estimates are accurate, it is hard to see how Applicants can claim that diverting this traffic will be beneficial to shippers, who (according to Brown and Zebrowski's revenue assumptions) would be charged significantly more than the current "going rate" to move those shipments over longer, more circuitous routes.[28]

Witnesses Brown and Zebrowski use the Board's Carload Waybill Sample to calculate the average revenue for a rail shipment for comparable available traffic.[29] The revenues were calculated for:

- **End-to-end movements** from the ultimate shipment origin to the ultimate shipment destination.
- **Segment movements** from the new CP or KCS on-point to the new CP or KCS off-point.

It is logical to expect that the revenue for a segment of a rail shipment would be *less* than the revenue for the entire rail shipment. Yet, in cases where the segment revenue exceeds the end-to-end revenue, *witnesses Brown and Zebrowski establish the illogical rule that "if the estimated end-to-end revenue amount was lower than the estimated segment revenue amount, we used the segment estimate*."[30] In other words, witnesses Brown and Zebrowski always selected the higher revenue.

[27] Brown and Zebrowski V.S., p. 21, ¶32 (emphasis added).
[28] Witnesses Brown and Zebrowski show that, on average, CPKC routes are 217 miles longer than the existing route and 323 miles longer than the shortest route in the market. Brown and Zebrowski V.S., Application Vol. 2, p. 132, Table 6.
[29] Brown and Zebrowski V.S., Application Vol. 2, p. 185, Appendix C, ¶2, Comparable traffic included origin and destination region, AAR car type, commodity, and car ownership.
[30] Brown and Zebrowski V.S., Application Vol. 2, p. 186, Appendix C, ¶5.

To illustrate the error, Exhibit 4-4 shows the movement of a carload of **{ }** from Bayou Pierre, LA to Chicago, IL that witnesses Brown and Zebrowski diverted from a KCS-CN interline route to CPKC. The pre-merger route for this shipment involves the KCS line from Bayou Pierre, LA to Jackson, MS, which generates {{ }} in revenue per carload for KCS. The shipment then interchanges to CN at Jackson, MS, generating {{ }} in revenue per carload for CN for the move between Jackson, MS and Chicago, IL. Cumulatively, the current revenue per carload on this movement is {{ }}.

Witnesses Brown and Zebrowski predict that after the merger, this traffic will be diverted to a CPKC single-line route, traveling from Bayou Pierre to Kansas City, MO on KCS lines, and then from Kansas City to Chicago on CP lines. The claimed incremental revenue on this movement is {{ }} per carload, which is {{ }} higher than the current rate for the entire KCS-CN route via Jackson. Witnesses Brown and Zebrowski further compound this higher rate by failing to subtract the {{ }} that KCS already receives for the movement from Bayou Pierre to Jackson. The error is that {{ }} is not incremental revenue, since the {{ }} already received by KCS is not removed.[31]

Exhibit 4-4: Example of the revenue error by witnesses Brown and Zebrowski[32]{{

[31] Witnesses Brown and Zebrowski average the revenue for each individual diversion with revenues for similar diversions and apply the averages in FD 36500 – Work Paper – HC – 8 – Diversion Identification, Results tab. Overstating the revenue for individual diversions leads to an overstatement of the averages, and therefore an overstatement of the total revenue.
[32] FD 36500 – Work Paper – HC – 8 - Diversion Identification.xlsx, Calculations tab, Row ID=6422. Map from PC*Miler|Rail, ver. 27.

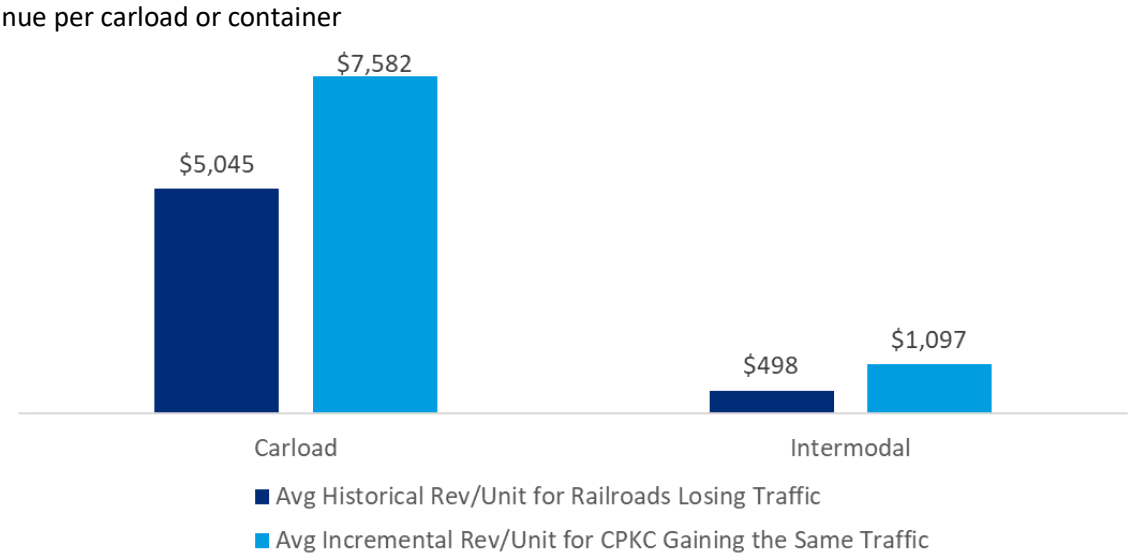
}}

The source of the overstatement of revenue can be traced back to the illogical rule to use the segment revenue if it exceeds the end-to-end revenue. The {{ }} in incremental revenue used by witnesses Brown and Zebrowski in the Bayou Pierre – Chicago example is actually the segment revenue from Jackson, MS to Chicago, IL, as calculated from the Board's Carload Waybill Sample. This segment revenue exceeded the end-to-end revenue from Bayou Pierre to Chicago, therefore witnesses Brown and Zebrowski selected the higher value, based on their rule. Because they considered it a segment rather than an end-to-end move, the existing KCS segment revenue from Bayou Pierre to Jackson was not subtracted.

To correct this example, I used the end-to-end revenue for Bayou Pierre to Chicago calculated by witnesses Brown and Zebrowski from the Board's Carload Waybill Sample and then subtracted the existing KCS revenue from Bayou Pierre to Jackson. So, instead of the {{ }} incremental revenue claimed by witnesses Brown and Zebrowski, my calculation using their values shows an end-to-end revenue of {{ }} minus the existing KCS revenue of {{ }}, to yield an incremental revenue to CPKC of {{ }}, which is {{ }} percent less than the current CN revenue of {{ }}.

Bayou Pierre to Chicago is not an isolated case. Witnesses Brown and Zebrowski select the higher segment revenue when it exceeds the end-to-end revenue for 52,927 of the 201,707 diverted railcars and containers (26.2 percent).[33] This results in incremental revenue added to CPKC that greatly exceeds the revenue lost by the current railroad, as shown in Exhibit 4-5.

Exhibit 4-5: Witnesses Brown and Zebrowski assign significantly more revenue to CPKC than was lost by the current carrier[34]



For carload traffic, the average revenue per car for the non-CP/KCS portion of the move lost by the current carrier is $5,045, while the incremental revenue added by witnesses Brown and Zebrowski as a benefit of the merger is $7,582. For intermodal traffic, the average revenue per container for the non-CP/KCS portion of the move lost by the current carrier is $498, while the incremental revenue added by witnesses Brown and Zebrowski as a benefit of the merger is $1,097.

[33] FD 36500 – Work Paper – HC – 8 - Diversion Identification.xlsx, Calculations tab. "CWS Segment > End to End Flag" (column CF) is 1. The 201,707 is the number of diverted cars and containers, excluding the 14,968 additional grain and forest products diversions (*see* Brown and Zebrowski V.S., Application Vol. 2, p. 159, Table 26).
[34] FD 36500 – Work Paper – HC – 8 - Diversion Identification.xlsx, Calculations tab, Filters were Non-CP/KCS Revenue/Car > 0 (col AD), Route Filter Flag = 0 (col BY), Diversion Units > 0 (col CA), and CWS Segment > End to End Flag = 1 (col CF). For Non-CP/KCS Revenue/Car, all records with a zero or negative value were excluded from the exhibit.

Applicants' experts appear to assume that customers after the merger will choose CPKC as a rail carrier even if distances are longer and rates are higher than those of the current rail movement. Absent competitive foreclosure by CPKC, this is not a logical assumption. Furthermore, witnesses Brown and Zebrowski's flawed use of the higher revenues (when the segment revenue exceeds the total revenue for the movement) falls disproportionately on shippers in Illinois and Michigan. Illinois originates or terminates 29 percent of the carloads and containers where witnesses Brown and Zebrowski selected the higher revenue, while Michigan originates or terminates 14 percent of the diverted carloads and containers.[35]

By applying the simple correction used in the Bayou Pierre – Chicago example to the diverted traffic in witnesses Brown and Zebrowski's Diversion Identification spreadsheet, I estimate that witnesses Brown and Zebrowski have overstated revenues by at least $47.4 million due to this error. My correction was to use the end-to-end revenue minus the existing CP-KCS revenue, rather than repeating the error made by witnesses Brown and Zebrowski of taking the higher segment revenue and not subtracting existing CP-KCS revenue to eliminate double counting.

However, this simple correction does not fully capture the magnitude of the error. For example, in an intermodal move from Chicago, IL to Laredo, TX, BNSF originates the traffic and interchanges with KCS for furtherance to Mexico. The historical data in witnesses Brown and Zebrowski's work papers show a revenue of {{ }} for KCS and {{ }} for BNSF, for a total revenue/container of {{ }}. The incremental CPKC revenue assigned by witnesses Brown and Zebrowski for this move is {{ }}, and when added to the existing KCS revenue, brings the total to {{ }}, which is { } percent above the historical 2019 revenue. I applied the

[35] FD 36500 – Work Paper – HC – 8 - Diversion Identification.xlsx, Calculations tab.

correction of subtracting the historical KCS revenue from the estimate by witnesses Brown and Zebrowski for end-to-end revenue, yielding an incremental revenue of {{ }} and a total revenue of {{ }}, which is still { } percent above the existing historical revenue.[36]

The challenge to determining the full magnitude of the error by witnesses Brown and Zebrowski is the poor data quality in their work papers for the historical revenue received by the non-CP/KCS carrier. In many cases, their work paper assigns revenue of zero, or even negative revenue, to the third-party railroad. For example, on a movement from Toluca, EM to Cottage Grove, MN, the revenue shown for the BNSF portion of the move is {{ }}.[37] This move was diverted to a CPKC route and assigned an incremental revenue of {{ }} for the CPKC diversion of the BNSF segment.[38]

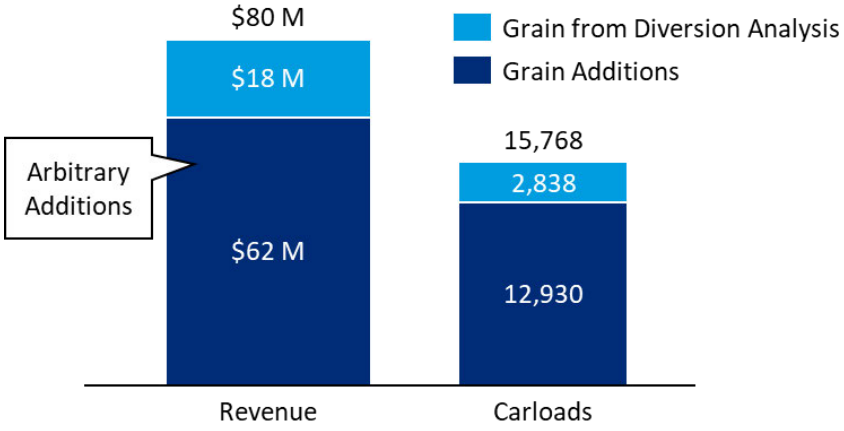
4.3 Diversion estimates include arbitrary and unsubstantiated additions for grain and lumber traffic that overstate revenue by $86 million

After applying an across-the-board percentage-based diversion approach to movement-specific rail-to-rail traffic diversion judgments, witnesses Brown and Zebrowski arbitrarily increased their post-merger diversion estimate by adding another $86 million in incremental revenue from grain and lumber traffic.

Specifically, they assumed that merger synergies would enable the merged CPKC system to capture a five percent increase in market share for cereal grain exports to Mexico (Exhibit 4-6).[39]

[36] FD 36500 – Work Paper – HC – 8 - Diversion Identification.xlsx, Calculations tab, Row ID = 2693.
[37] FD 36500 – Work Paper – HC – 8 - Diversion Identification.xlsx, Calculations tab, Row ID = 11979, column AD.
[38] FD 36500 – Work Paper – HC – 8 - Diversion Identification.xlsx, Calculations tab, Row ID 11979, column CL.
[39] Brown and Zebrowski, V.S., Application Vol. 2, ¶42.

Exhibit 4-6: Witnesses Brown and Zebrowski grain diversion breakdown[40]



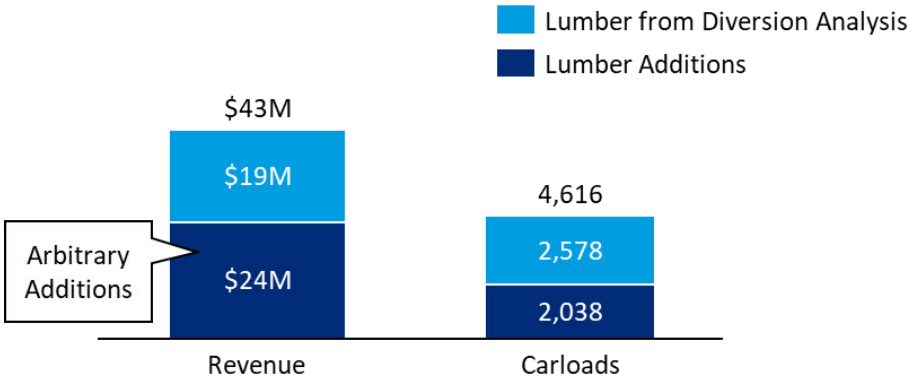
This (unexplained) assumption, *which increases total revenues from diverted grain shipments in the Brown and Zebrowski diversion model by more than 340 percent*, does not appear to be based on any movement-specific analysis. Indeed, witnesses Brown and Zebrowski do not even identify the specific origins and destinations between which these shipments would move. Rather, they simply assume that "For purposes of developing operating outputs for use in the Operating Plan, we estimate that these carloads would be distributed proportionally across the CP-served grain-supply regions that would be newly accessible via single-line routes."[41] There is no justification or evidentiary support for either this arbitrary increase in CPKC's post-merger grain traffic – which accounts for nearly 17 percent of all projected rail-to-rail traffic diversion revenues – or for the random distribution of this traffic across the grain producing regions that CP serves.

Witnesses Brown and Zebrowski likewise assume an arbitrary five percent market share increase on Canadian lumber exports to Dallas. They then apply a 15 percent growth rate to this market share gain to account for growth between 2019 and 2021 (Exhibit 4-7), despite all other

[40] FD 36500 – Work Paper – HC – 8 - Diversion Identification.xlsx, Results tab.
[41] Brown and Zebrowski V.S., p. 26, ¶42.

traffic in their study being based on Base Year 2019 volumes.[42] Witnesses Brown and Zebrowski provide no analysis or calculations to support these market share and growth assumptions. In total, these adjustments account for 2,038 additional carloads, or *56 percent of all incremental revenue from lumber diversions*.[43]

Exhibit 4-7: Witnesses Brown and Zebrowski lumber diversion overstatement[44]



Given the complete lack of analytical support for these "additional opportunities" (not to mention the methodological inconsistency of arbitrarily adding traffic and revenue that was not identified by Applicants' traffic diversion model in the first place), these incremental traffic and revenue gains should be excluded from any realistic evaluation of the rail-to-rail traffic likely to be captured by the merged CPKC system.

4.4 Applicants made a currency conversion error of Canadian dollars to US dollars that further inflated the revenues likely to be achieved from diverted traffic

In addition to the methodological errors and inconsistencies discussed above, witnesses Brown and Zebrowski made a significant calculation error that further inflated their revenue projections. A portion of the Canada traffic in the rail-to-rail diversion model contains a currency

[42] Brown and Zebrowski V.S., Application Vol. 2, p. 156, Table 23.
[43] FD 36500 – Work Paper – HC – 8 - Diversion Identification.xlsx, Results tab, Forest Products (Line 16) and Grain (Line 18).
[44] FD 36500 – Work Paper – HC – 8 - Diversion Identification.xlsx, Results tab.

conversion error that resulted in an overstatement of revenue. The average exchange rate in 2019 was 0.754 US dollars for one Canadian dollar.[45] Witnesses Brown and Zebrowski rounded this to 0.75. Their SQL code, shown below, states that if Currency = 'C' for Canadian, then divide the Tot_Rev by 0.75 and reassign the value to Tot_Rev.[46]

Set [Tot_Rev] = case when Currency = 'C' then [Tot_Rev]/.75

The problem is that *witnesses Brown and Zebrowski should have multiplied rather than divided*. One Canadian dollar *divided by* 0.75 incorrectly converts to 1.33 US dollars, not the correct value of 0.75 US dollars. This miscalculation inflated the revenues on shipments with a currency conversion by 78 percent. This error is illustrated in Exhibit 4-8, where witnesses Brown and Zebrowski calculate the incremental revenue for a movement as {{ }}, when the correct revenue in US dollars should be {{ }}.

Exhibit 4-8: Example of Brown and Zebrowski overstated revenue due to CAD to USD currency error[47]

Origin	Orig. RR	Destination	Dest. RR	Commodity	Incremental Revenue/Car	Corrected Revenue/Car
Saskatoon, SK	CP	Longview, TX	UP	{{ }}	{{ }}	{{ }}

The precise impact of this error on Applicants' overall incremental traffic revenue estimate is difficult to determine, because the error occurs at the data extraction step, prior to the estimation of diversions. To calculate the impact of the error would require a full rerunning of Brown and Zebrowski's SQL code and recreating their diversions.[48]

[45] The US Internal Revenue Service lists the average exchange rate in 2019 as 1.327 Canadian dollars for 1 US dollar, or 0.754 US dollars per Canadian dollar.
[46] Line shown is from FD 36500 – Work Paper – HC – 1 - Traffic Consolidation.sql, Line 584, shown in Oliver Wyman work paper HC- Currency Conversion Error.txt.
[47] FD 36500 – Work Paper – HC – 8 - Diversion Identification, tab Calculations, Row ID 922. Incremental revenue per car is from cell CL 927. Corrected Revenue/Car = ($11,012*0.75)*0.75 = $6,194.
[48] The error is contained in FD 36500 – Work Paper – HC – 1 - Traffic Consolidation.sql, lines 582 through 587.

5. Certain Additional Claimed Incremental Revenues of $386.7 Million Are Unsubstantiated or Unrelated to the Merger

Applicants took the unusual step of "supplementing" the traffic diversion studies conducted by their expert traffic witnesses with a verified statement sponsored by company witnesses Wahba and Naatz, who purport to identify a number of "additional revenue opportunities" for the merged CPKC system. Witnesses Wahba and Naatz claim that those opportunities will generate an additional $411 million in annual revenue for the merged CPKC. *This represents fully 40 percent of the total incremental revenue from traffic diversions identified in the Application*.

This incremental traffic and revenue is questionable in terms of why it was not identified in the diversion analyses presented by Applicants' experts. In addition, the supplemental traffic and revenue gains sponsored by witnesses Wahba and Naatz suffer from several conceptual and methodological errors that render their conclusions invalid. The vast majority of this claimed additional incremental revenue should be excluded from any realistic assessment of the traffic and revenue impact of the proposed CPKC merger for the following reasons, which are discussed in detail below:

- Nearly 40 percent of the revenue from additional traffic opportunities posited by witnesses Wahba and Naatz is attributable to traffic gains that are unrelated to the merger.
- Several supposed revenue opportunities involve impractical, circuitous, and complicated routes.
- Applicants' expert traffic witnesses did not divert the traffic identified by witnesses Wahba and Naatz.

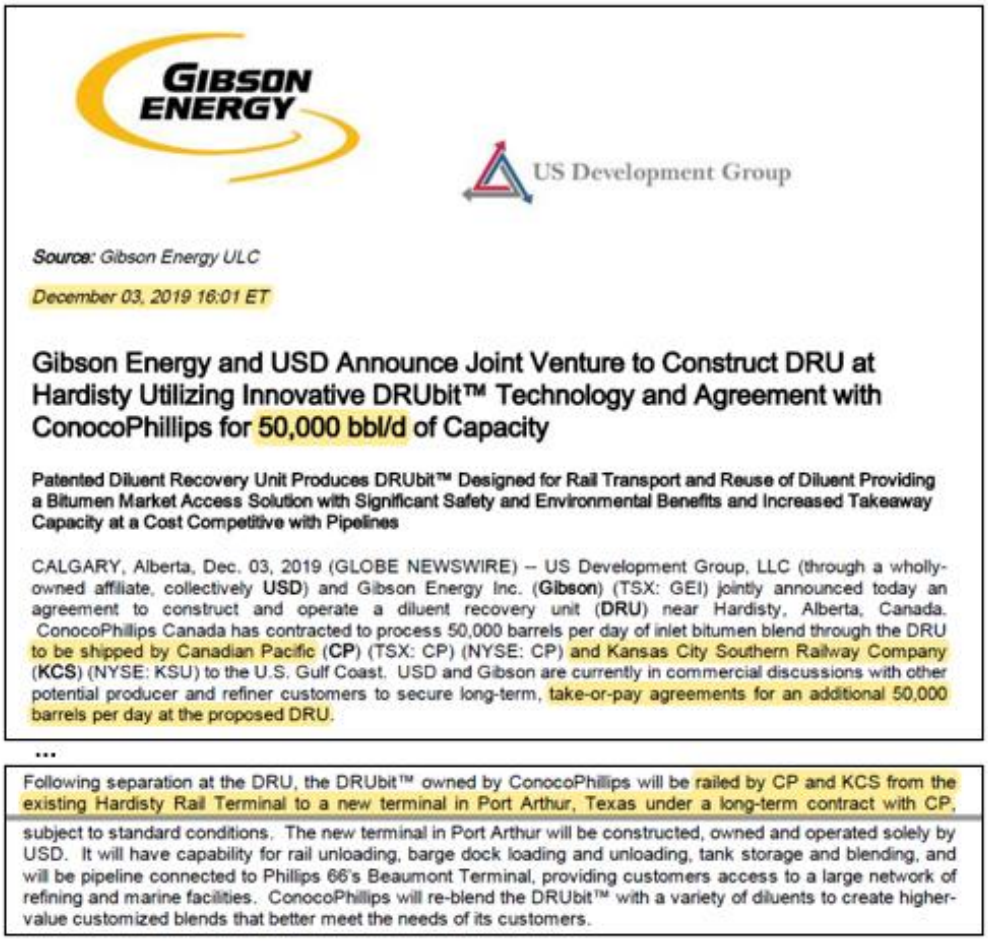
I estimate that in total, these assumptions, inconsistencies, and conceptual errors result in an overstatement of as much as $387 million (out of a total of $411 million) of the additional revenue opportunities posited by witnesses Wahba and Naatz.

5.1 Nearly $158.1 million (40 percent) of the revenue from additional traffic opportunities posited by witnesses Wahba and Naatz is attributable to traffic gains that are unrelated to the merger

The single largest "opportunity" cited by witnesses Wahba and Naatz (accounting for $158.1 million in incremental revenue) is a crude oil movement from Hardisty, AB to Port Arthur, TX.[49] However, as the press release reproduced as Exhibit 5-1 clearly indicates, that traffic opportunity pre-dates the merger. The plan for the new movement was made public by the shipper, Gibson Energy, *in December 2019*. According to witnesses Wahba and Naatz, "CP's evaluation of specific traffic growth opportunities thus *began* at the very outset of our pursuit of KCS *in late 2020*" – *nearly a year after the Gibson Energy press release*.[50] Witnesses Wahba and Naatz also state that discussions with customers regarding the additional traffic opportunities in their testimony did not occur until CP and KCS announced their plans in March 2021.[51] If that statement is true, merger-related discussions could not have occurred with Gibson Energy at the time of the 2019 press release.[52]

[49] FD 36500 – Work Paper – HC – Growth Initiative Calculations.xlsx.
[50] Verified Statement of Jonathan Wahba and Michael J. Naatz, ¶6.
[51] Wahba and Naatz V.S., ¶11.
[52] Wahba and Naatz V.S., ¶11.

Exhibit 5-1: Announced joint CP and KCS crude oil move from Hardisty, AB to Port Arthur, TX: December 2019 press release[53]



Source: Gibson Energy ULC

December 03, 2019 16:01 ET

Gibson Energy and USD Announce Joint Venture to Construct DRU at Hardisty Utilizing Innovative DRUbit™ Technology and Agreement with ConocoPhillips for 50,000 bbl/d of Capacity

Patented Diluent Recovery Unit Produces DRUbit™ Designed for Rail Transport and Reuse of Diluent Providing a Bitumen Market Access Solution with Significant Safety and Environmental Benefits and Increased Takeaway Capacity at a Cost Competitive with Pipelines

CALGARY, Alberta, Dec. 03, 2019 (GLOBE NEWSWIRE) -- US Development Group, LLC (through a wholly-owned affiliate, collectively **USD**) and Gibson Energy Inc. (**Gibson**) (TSX: GEI) jointly announced today an agreement to construct and operate a diluent recovery unit (**DRU**) near Hardisty, Alberta, Canada. ConocoPhillips Canada has contracted to process 50,000 barrels per day of inlet bitumen blend through the DRU to be shipped by Canadian Pacific (**CP**) (TSX: CP) (NYSE: CP) and Kansas City Southern Railway Company (**KCS**) (NYSE: KSU) to the U.S. Gulf Coast. USD and Gibson are currently in commercial discussions with other potential producer and refiner customers to secure long-term, take-or-pay agreements for an additional 50,000 barrels per day at the proposed DRU.

...

Following separation at the DRU, the DRUbit™ owned by ConocoPhillips will be railed by CP and KCS from the existing Hardisty Rail Terminal to a new terminal in Port Arthur, Texas under a long-term contract with CP, subject to standard conditions. The new terminal in Port Arthur will be constructed, owned and operated solely by USD. It will have capability for rail unloading, barge dock loading and unloading, tank storage and blending, and will be pipeline connected to Phillips 66's Beaumont Terminal, providing customers access to a large network of refining and marine facilities. ConocoPhillips will re-blend the DRUbit™ with a variety of diluents to create higher-value customized blends that better meet the needs of its customers.

In addition, Gibson Energy announced in December 2021 "the DRU Fully Operational, including shipment of DRUbit™ By Rail™" from the facility in Hardisty, AB to Port Arthur, TX.[54] Canadian Pacific shared that announcement on social media the same day, including a photograph of a CP train departing the Hardisty facility.[55] In short, this rail movement clearly predates the merger.

[53] Press release, Global Energy ULC, December 3, 2019.
[54] "Gibson Energy and US Development Group declare the DRU Fully Operational, including shipment of DRUbit™ By Rail™," PR Newswire, December 14, 2021.
[55] Canadian Pacific, Twitter @CanadianPacific, December 14, 2021.

The Gibson Energy announcement involved an agreement to ship 50,000 barrels per day with a take-or-pay for an additional 50,000 barrels per day, which is equivalent to approximately 50,000 annual tank cars.[56] Witnesses Wahba and Naatz claim that the fully phased in number of units is 51,840 annual tank cars – almost identical to the volume mentioned in the Gibson Energy press release of 2019.[57]

Because this incremental revenue opportunity was announced publicly more than a year before the CP-KCS merger was announced and is operational now, it clearly did not come to pass because of the proposed merger, and therefore cannot properly be considered a result of, or synergy generated by, the merger.

5.2 Additional diversion revenue opportunities of $107 million involve impractical, circuitous, and complicated routes

Certain other revenue opportunities claimed by witnesses Wahba and Naatz are implausible because they fail to account for the reality of global supply chains or the circuity of the longer rail and maritime routes that would make it difficult for CPKC to capture that traffic.

For example, the Application assumes that CPKC will capture incremental traffic and revenue by shifting international container traffic that currently moves via the Port of Los Angeles/Long Beach to destinations such as Chicago, New York, and Toronto to more complex and circuitous water and rail routes via the Port of Lazaro Cardenas (on the Mexican Pacific coast) and KCSM/KCS/CP. Witnesses Wahba and Naatz use a distorted map (reproduced in Exhibit 5-2) in an attempt to show that such a routing would be a viable competitive alternative

[56] A tank car can hold about 560 barrels of heavy crude oil. Wahba and Naatz claim tank cars can haul 20-30 percent more DRUbit, so (365 days x 100kbd/(560 bbl/0.75)) = 48,900 annual tank cars. The API gravity for Canadian heavy crude oil is 9º to 11º (*see* API Gravity, Oil Sands Glossary). A 10º API gravity weights 8.328 lbs./gallon, or 350 lbs./barrel at 42 gallons/barrel (*see* API Gravity (engineeringtoolbox.com)). A 195,900 lbs. net weight limit for a tank car would allow for 560 barrels of heavy crude oil.
[57] FD 36500 – Work Paper – HC – Growth Initiative Calculations.xlsx.

to the shorter routes over which the traffic already moves. This map misrepresents the operational challenge of routing international container traffic bound to US destinations via the Port of Lazaro Cardenas.

To test the Wahba and Naatz hypothesis, I used the industry standard software program PC*Miler|Rail to calculate the distance between the Port of Los Angeles/Long Beach and Chicago via BNSF and the distance between the Port of Lazaro Cardenas and Chicago on a hypothetical CPKC network. As shown in a more accurate map in Exhibit 5-3, the rail route from LA/Long Beach to Chicago is 2,195 miles long, while the rail route via KCSM/KCS/CP from Lazaro Cardenas would be 2,650 miles. The difference is 455 miles, or nearly a 21 percent increase in rail distance, making the route from Lazaro Cardenas slower, less economical, and less environmentally friendly.

Exhibit 5-2: CPKC map of proposed route from Port of Lazaro Cardenas, which distorts differences in distance versus the Port of Los Angeles[58]

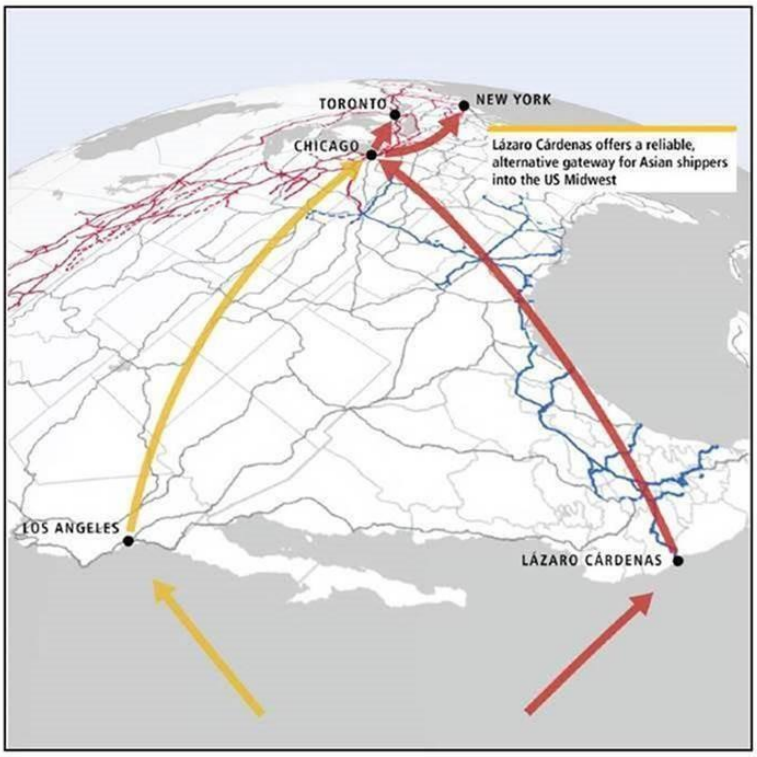
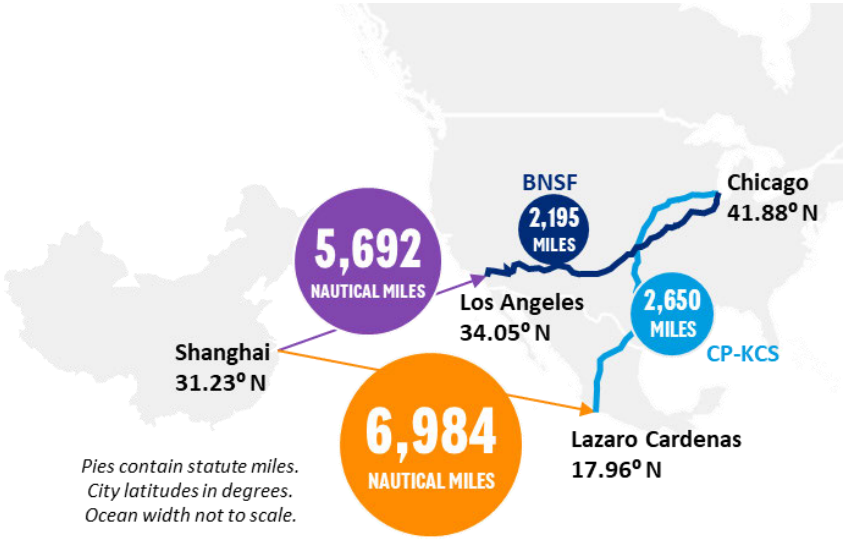


Exhibit 5-3: Oliver Wyman map of proposed route from Lazaro Cardenas, which better shows the 1,300 nautical-mile and 455 rail-mile differences when compared to the Port of Los Angeles[59]



[58] Wahba and Naatz V.S., p. 28, Figure 6. Two trains per day based on Wahba and Naatz claim of 130,000 containers per year.

[59] Shanghai to Los Angeles is 5,692 nautical miles and Shanghai to Lazaro Cardenas is 6,984 nautical miles, based on Portworld.com Distance Calculator from S&P Global Platts. Nautical miles converted to statute miles using 6,080 ft/5,280 ft. A "standard" nautical mile is 6,080 feet versus a statute mile of 5,820 feet, though this is an approximation, since distances vary by latitude (*see* Royal Museums Greenwich).

Witnesses Wahba and Naatz not only obscure the substantial *rail* routing circuity implied by their proposed diversion, they also fail to consider the additional length of the *maritime* route that would be required to divert intermodal traffic originating in East Asia to the Port of Lazaro Cardenas. Using Shanghai (the largest container port in the world[60]) as an example, a ship traveling to Los Angeles/Long Beach would travel approximately 5,692 nautical miles. By comparison, the journey from Shanghai to Lazaro Cardenas would cover 6,984 nautical miles. Thus, a container ship would need to travel an additional 1,292 nautical miles, an increase of 23 percent, to get from Shanghai to Lazaro Cardenas as compared to Los Angeles. This added distance over the ocean further undermines the economics, operational efficiency, and environmental merits of diverting intermodal traffic to Lazaro Cardenas, as posited by Applicants.

The noncompetitive nature of a proposed route involving an additional 1,292 nautical miles plus an additional 455 rail miles is underscored by the fact that *Lazaro Cardenas currently handles almost no traffic destined to any point in the United States*.[61] In any event, CP already has a better option to reach Chicago via the Port of Vancouver, which involves both a shorter rail route and a shorter maritime distance from East Asia than a route via Lazaro Cardenas.

The claimed diversion to Lazaro Cardenas of containers destined for Toronto and New York City posited by the Applicants is even less feasible. To reach Toronto from Lazaro Cardenas, traffic would:

[60] *See* "Shanghai port retains crown as the world's busiest container port," Seatrade Maritime News, January 6, 2021.
[61] CP-KCS waybill data provided by FTI, summarized in Oliver Wyman work paper HC- Lazaro Cardenas – USCanada Traffic.xlsx. Waybill records show **{{ }}** loaded containers from the Port of Lazaro Cardenas to Kendleton, TX and **{{ }}** empty cars between the Port of Lazaro Cardenas to/from the US and Canada in 2019.

- Incur 436 miles of additional rail distance compared to the shorter route from Los Angeles/Long Beach;[62]
- Then travel through some of the most congested rail segments in the nation (including the use of terminal railroads in the Chicago area, as well as several congested crossings);
- Then move via trackage rights on Norfolk Southern to reach the Detroit-Windsor tunnel (which has clearance restrictions for double stack containers), *or*
- Be transferred to CSX for movement (via haulage rights) to Buffalo, NY, where it would be interchanged back to CP for movement to Toronto.[63]

Needless to say, these options are vastly inferior to the available direct routings on either CP or CN from Vancouver, or via UP or BNSF from Los Angeles/Long Beach with an interchange to CN at Chicago.

Routing traffic from Lazaro Cardenas to New York City via CPKC also would be noncompetitive: Intermodal traffic originating on KCSM already has a more direct routing option over the Meridian Speedway to Norfolk Southern, instead of using any portion of the CP network. The route from Lazaro Cardenas to New York via the existing KCS-NS interchange at Meridian, MS is 489 miles shorter than a route from Lazaro Cardenas to New York involving a KCS-CP interchange at Kansas City.[64]

Finally, witnesses Wahba and Naatz quote Mr. Jonathan Sinton, Regional Head of Procurement of A.P. Moller-Maersk, as stating the KCS combination with CP promises to "open

[62] PC*Miler|Rail ver. 27. Distance for Long Beach-BNSF-Chicago-CP-Toronto is 2,722.4 miles, provided the traffic can use NS trackage rights in Michigan and has clearance to use the Detroit Tunnel. Distance for Lazaro Cardenas-KCSM-Laredo-KCS-Kansas City-CP-Toronto is 3,157.9 miles, with same assumptions about trackage rights and tunnel clearance.
[63] One of the two Detroit tunnel tubes in 1993 was enlarged to handle auto racks and international doublestack containers. But the tunnel cannot handle doublestacked domestic containers. So CP's current Montreal-Chicago intermodal trains, which include both international and domestic boxes, run via CSX between Buffalo, NY and Chicago. See: "CP sought to control its own destiny with Detroit tunnel purchase," Trains, October 20, 2020.
[64] PC*Miler|Rail ver. 27. Distance for Lazaro Cardenas-KCSM-Laredo-KCS-Meridian-NS-Oak Island is 3,073.9 miles versus Lazaro Cardenas-KCSM-Laredo-KCS-Kansas City-CP-Chicago-NS-Oak Island which is 3,562.6 miles.

up new options for efficient intermodal rail transportation all the way into America's Heartland."[65] However, witnesses Wahba and Naatz fail to mention Mr. Sinton's very next sentence, where he states, "*We don't expect these options to supplant the current options from ports on the U.S. West Coast*."[66] (Emphasis added.)

Witnesses Wahba and Naatz claim that traffic diverted from the Ports of Los Angeles/Long Beach to the Port of Lazaro Cardenas will generate 130,000 containers, totaling $107 million in annual merger-related revenue for CPKC.[67] They even attribute $21.1 million of the $107 million in merger-related benefits to Lazaro Cardenas – Kansas City diversions and another $22.9 million to Lazaro Cardenas-Dallas diversions, *routes where KCS could provide single-line service on a stand-alone basis today*.[68] The Port of Lazaro Cardenas is simply not a realistic alternative to Los Angeles/Long Beach, given the increased distances and the presence of more competitive alternatives, such as the Port of Vancouver.

5.3 Witnesses Wahba and Naatz claim approximately $122 million in diversions that were apparently "missed" by Applicants' diversion experts in LPG, grain, and perishable commodities

After engaging expert witnesses Brown and Zebrowski to estimate potential rail-to-rail traffic diversions and expert witness Mutén to analyze potential truck-to-rail diversions, Applicants took the unusual step of adding to their estimates of incremental traffic revenues the "additional revenue opportunities" discussed above. But Applicants offer no explanation as to why their outside traffic experts either "missed" such consequential traffic opportunities or failed to include them in their estimates of post-merger CPKC traffic.

[65] Wahba and Naatz V.S., Application Vol. 1, p. 273, ¶64.
[66] Letter from Mr. Jonathan Sinton, Application Vol. 3, p. 153.
[67] FD 36500 – Work Paper – HC – Growth Initiative Calculations.xlsx.
[68] FD 36500 – Work Paper – HC – Growth Initiative Calculations.xlsx.

An estimated $121.7 million in revenue for liquified petroleum gas (LPG), grain, and perishables was added by witnesses Wahba and Naatz, even though Applicants' witnesses Brown, Zebrowski, and Mutén analyzed the potential for diverting shipments of those commodities in their testimony.

LPG ($30.5 million): Witnesses Wahba and Naatz identified existing rail shipments of LPG as likely diversion candidates. This claimed "additional opportunity" accounts for 4,300 carloads of LPG – a volume that is nearly triple the 1,545 carloads that Brown and Zebrowski deemed divertible – and generates an additional $30.5 million in post-merger revenues for the CPKC system.[69] Applicants offer no explanation for, or reconciliation with, Brown and Zebrowski's findings regarding the sources and volumes of divertible LPG traffic. Witnesses Wahba and Naatz vaguely mention a possible CPKC investment in a new LPG origin facility, but that investment is not reflected in Applicants' capital expense evidence.[70] Moreover, 2,600 carloads of the LPG traffic that Wahba and Naatz identified move between Saskatchewan and Mexico. However, Applicants' own work papers indicate that there were only {{ }} total carloads of LPG traffic between Saskatchewan and Mexico in the Base Year[71] – which means that witnesses *Wahba and Naatz are claiming traffic that does not currently exist.* By comparison, *Applicants' outside traffic experts found only seven carloads of LPG between these locations to be divertible*.[72]

[69] FD 36500 – Work Paper – HC – Growth Initiative Calculations.xlsx; Brown and Zebrowski V.S., Application Vol. 2, p. 154, Table 21.
[70] Verified Statement of Elphick and Orr, Application Vol. 2, pp. 81-91, provides capital expenditures for track, yards, and terminals. There is no mention of any LPG facility investment for Canada.
[71] FD 36500 – Work Paper – HC – 4 - Traffic Screening.xlsx. On the CPKCS Combined Traffic Tapes tab, filtered column E as "SK," and column N to "MX," and column AD as "L.P.G." Summed column V to obtain {{ }}.
[72] FD 36500 – Work Paper – HC – 8 - Diversion Identification, tab Calculations, Row ID 877 and 878.

Grain ($36.7 million): Witnesses Wahba and Naatz projected an additional $36.7 million in incremental revenue from rail-to-rail grain diversions, consisting of 3,630 carloads of soybeans and 3,000 carloads of DDGs and sweeteners.[73] These diversions are in addition to the volumes of those commodities that Applicants' expert traffic witnesses identified as divertible (3,684 carloads of soybeans and 2,650 carloads of DDGs and sweeteners), effectively doubling the diversion total for each commodity.[74] Applicants offer no explanation for or reconciliation with witnesses Brown and Zebrowski's findings with respect to these grain shipments.

Perishables ($54.4 million): Witnesses Wahba and Naatz also project that CPKC will earn an additional $54.4 million in incremental revenues from perishables truck-to-rail diversions.[75] Specifically, they divert to the CPKC network 24,748 units of perishables in 53-foot refrigerated containers that move by truck from Michoacán/Veracruz, Mexico to Chicago, the Twin Cities, and Kansas City.[76] Applicants' own truck-to-rail diversion expert Mutén concluded that only a much smaller volume of this perishable traffic would be divertible: 374 units, with associated revenues of just $0.6 million.[77] Witness Mutén explained why he did not include the 24,748 units diverted by witnesses Wahba and Naatz: "Most of these volumes flow out of Mexico to intermediate destinations [sic] in border states and later move to the Midwest."[78] Witnesses Wahba's and Naatz's "analysis" of this "additional opportunity" appears to consist of (i) estimating that five million tons of produce moved from Mexico to wholesaler markets in border states, (ii) assuming that CPKC could capture ten percent of such traffic, and (iii) diverting that ten percent from truck to CPKC. Applicants do not explain why these shipments are divertible,

[73] FD 36500 – Work Paper – HC – Growth Initiative Calculations.xlsx.
[74] Brown and Zebrowski V.S., p. 26, Table 11 and p. 28, Table 12.
[75] FD 36500 – Work Paper – HC – Growth Initiative Calculations.xlsx.
[76] FD 36500 – Work Paper – HC – Growth Initiative Calculations.xlsx.
[77] Mutén V.S., p. 22.
[78] Mutén V.S., p. 22.

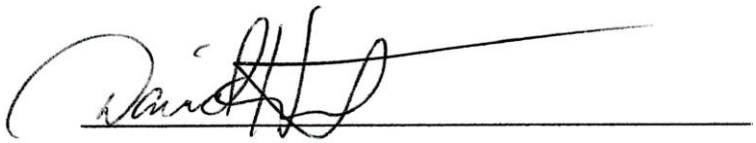
or why witness Mutén (who clearly was aware of the movements) did not judge them to be divertible.

In sum, witnesses Wahba and Naatz "found" an additional $121.7 million in diversion revenue that was not identified by Applicants' diversion experts, with no explanation or facts to support why these additional revenues are credible and should be included in the Application.

VERIFICATION

I, David Hunt, declare under penalty of perjury that the foregoing information is true and correct. Further, I certify that I am qualified and authorized to file this statement.

Executed on this 28th day of February, 2022.



David Hunt

Appendix A. Resume of David Hunt

Mr. Hunt, a Vice President in Oliver Wyman's Transportation & Service practice, has over 30 years of experience in the areas of transportation operations and strategic planning, national and regional transportation policy, and network modeling and operations research. Mr. Hunt focuses on projects involving regulatory and policy analysis, strategic planning, and operational improvements. His projects include:

- Developed a market share model that predicted truck/rail shares and volumes under various scenarios, including autonomous truck technologies and the potential responses by the rail industry.
- Worked with a Class I railroad to explore opportunities and the value of adopting predictive maintenance practices for their railcar fleet.
- Prepared several policy white papers filed with the US Department of Transportation, addressing issues such as positive train control and the use of electronically controlled pneumatic brakes.
- Called as an expert witness in rail capacity modeling as part of an international arbitration case in South America.
- Participated in discussions with the Mexican government that led to a favorable ruling for the rail industry regarding proposed regulatory action to promote competition through expanded interconnection of rail services.
- Managed the design and development of BlueNet, a facility location model used in network design.
- Developed a simulation model that showed the benefits of operating a nationwide railcar pool, the results of which were used in a Surface Transportation Board proceeding to reauthorize the operation of the pool.
- Worked with a rail industry supplier to restructure their support services, incorporating predictive maintenance tools for safer and more reliable operations.

Prior to joining Oliver Wyman, Mr. Hunt was a Senior Associate at Cambridge Systematics. Mr. Hunt also was a Vice President at ALK Associates. Mr. Hunt is active in the Institute for Operations Research and the Management Sciences (INFORMS), where he was the recipient of the 2017 INFORMS President's Award. He currently serves on the INFORMS Board of Directors as Treasurer and is a member of the Transportation Research Board's Railroad Operating Technologies Committee.

Mr. Hunt earned a BS in civil engineering from West Virginia University and a MSE from the Civil Engineering and Operations Research Department at Princeton University.

Exhibit 2

Verified Statement of Carl Van Dyke

BEFORE THE
SURFACE TRANSPORTATION BOARD

STB FINANCE DOCKET NO. 36500

CANADIAN PACIFIC RAILWAY LIMITED; CANADIAN PACIFIC RAILWAY COMPANY; SOO LINE RAILROAD COMPANY; CENTRAL MAINE & QUEBEC RAILWAY US INC.; DAKOTA, MINNESOTA & EASTERN RAILROAD CORPORATION; AND DELAWARE & HUDSON RAILWAY COMPANY, INC. – CONTROL – KANSAS CITY SOUTHERN, THE KANSAS CITY SOUTHERN RAILWAY COMPANY, GATEWAY EASTERN RAILWAY COMPANY, AND THE TEXAS MEXICAN RAILWAY COMPANY

CN'S COMMENTS ON APPLICATION AND REQUEST FOR CONDITIONS

Verified Statement of Carl Van Dyke

February 28, 2022

PUBLIC VERSION

CONTENTS

1. Qualifications....1

2. Assignment and Summary of Findings....2

3. A Rigorous Operations Planning Process is a Key Element of a Reliable Merger Application....7

3.1 The operating plan plays a critical role in the application....7

3.2 Customary method for preparing an operating plan....10

4. Applicants' Operations Planning Process....12

4.1 Applicants have failed to produce reliable base year traffic or operating plan....13

4.2 Applicants' pre- and post-merger traffic file is flawed....15

4.3 Applicants failed to correctly estimate line density, train counts, and yard activity....19

4.4 Applicants largely abandoned their MultiRail operating plan in developing the merged carrier's operating expenses....25

5. Specific Errors in Applicants' Analysis....31

5.1 Traffic density between Sabula, IA, and Airline Junction, Kansas City....33

5.2 Base Year intermodal traffic at Lazaro Cardenas is understated....37

5.3 Application train counts are not reliable....38

5.4 The Application fails to meet the requirement to identify all yards projected to experience more than a 20 percent increase in activity....47

5.5 Originating and terminating railcar volumes are out of balance at many of the locations shown in the Application....48

6. Other Issues That Undermine the Validity of the Application....50

6.1 Detailed review of tonnages for additional line segments....51

6.2 The Applicants' operating plan may violate the constraints of the Michigan and Eastern Canada CSX and NS trackage/haulage rights....57

6.3 Assessment of carload traffic issues....63

Appendix A. Carl Van Dyke Resume....71

1. Qualifications

My name is Carl Van Dyke. I am a Senior Advisor to and a Partner Emeritus of Oliver Wyman, a global general management consulting firm with more than 60 offices in 31 countries. My office address is One University Square Drive, Suite 100, Princeton, NJ 08540.

I have been engaged in the design, development, and application of software tools to model, evaluate, and improve the operations of railroads for more than 40 years. I was a Vice President at ALK Associates, where I led the development of rail planning tools and the initial design and proof-of-concept of the algorithmic blocking system currently used by Norfolk Southern (NS) and Canadian Pacific (CP).

In 1992, I founded and became President of MultiModal Applied Systems. MultiModal developed the MultiRail family of software tools, which have been used in the modern redesign of virtually all major North American railroad operating plans, as well as those of many railroads in Europe, Africa, and Asia. While at MultiModal, I led teams in applying MultiRail to evaluate or develop operating plan designs for the Union Pacific-Southern Pacific, Illinois Central-Canadian National, Norfolk Southern-Conrail, and the proposed Canadian National-BNSF mergers. Both CP and Kansas City Southern (KCS) use MultiRail and are familiar with the software's functionality.

Oliver Wyman acquired MultiModal in 2006 and I became a Partner with the firm until my retirement in 2013. At Oliver Wyman, I continued to advance the use of MultiRail at numerous railroads and led engagements focused on improving railroad operations and the design of new software tools for railroad management.

Currently, I continue to be active in consulting to the industry. Most recently, I assisted two Class I railroads in the design of their next generation operations control systems and helped a

new technology start-up design and build the next generation of software tools for the management of freight rail operations.

I earned a BSE in mechanical engineering from the University of Pennsylvania, and an MS in civil engineering from the Massachusetts Institute of Technology. My full resume is provided in Appendix A.

2. Assignment and Summary of Findings

I have been asked to review the process by which Applicants developed the operating plan for the combined CP, KCS, and Kansas City Southern de Mexico (KCSM) system; the metrics generated through that process; and the process by which those metrics flowed through to the operations costing and capital planning processes.

Based on my review, I conclude that the operating plan presented in the Application fails to meet the Board's basic evidentiary requirements. The result is an incomplete and deeply flawed operating plan that cannot be relied upon in evaluating the impact of the proposed merger on CP-KCS operations, the operations of other railroads, or other stakeholders, such as shippers and communities. This is so for three basic reasons:

- **The operating plan was developed using one-month "samples" from different years, not on the Base Year**. Despite selecting 2019 as the "Base Year" for the Application (including the operating plan), Applicants actually based their operating plan on a mismatched set of data from multiple years. {{XXX}}[1],[2] Applicants provide no evidence that either of the selected one-month traffic samples is representative of any

[1] dwnld_Traffic_KCS.csv, provided as part of the accompanying attachments to Traffic File - Methodology.pdf, indicate the traffic data used is from October 2020; FD 36500 - Work Paper - HC - CP Bulk Cars Per Day By Sub.xlsx, and FD 36500 - Work Paper - HC - KCS KCSM Bulk Train Cars Per Day by Subdivision.xlsx, provided as part of the accompanying attachments to Trains Per Day - Methodology.pdf.
[2] HC - Remote Videotaped Deposition of Raymond A. Elphick and John F. Orr, STB Docket No. FD 36500, Elphick Deposition, pp. 187:17, Feb 18, 2022

full year (much less the Base Year of 2019), nor do they explain why they could not have utilized samples of manifest and intermodal traffic from the same month and year, or for full year 2019. Likewise, Applicants fail to demonstrate that the Q1 2021 train plans on which they relied are representative of Base Year (2019) operations.

Moreover, Applicants made other significant errors when processing the traffic data used to develop the operating plan. Based on my review of the data and the process used by the Applicants, and my experience in developing railroad operating plans, I conclude that using mismatched traffic data and a mismatched train plan distorted the Applicants' development of the Base Year blocking and routing plan, train plan, and the operating metrics, rendering the operating plan invalid and unusable.

- **The flawed operating plan does not produce reliable estimates of traffic density, train counts, or yards expected to experience growth**: It is my understanding that the Application was filed under the Board's "old" merger rules that were in effect in 1982, so the provisions of 49 CFR Part 1111.8(a)(2000) apply with respect to the operating plan. 49 CFR Part 1111.8(a)(1)(2000) requires applicants to provide three specific outputs for the operating plan for the year in which it will be fully implemented: 1) traffic density (tonnage) maps or tables for all main and secondary network line segments,[3] 2) train counts for main and secondary network line segments, and 3) the identity of all yards that are anticipated to experience growth in activity of 20 percent or more.

  Based on my review of the Application, I conclude:

  - The **traffic density** tables and maps contain material errors that render them meaningless and unusable. The exact causes of these errors are unknown, but likely are due to flawed traffic data and a convoluted and error-prone process used for their preparation.
  - The **train counts** are inaccurate because:

[3] 49 CFR Part 1111.8(a)(5)(2000) requires that historic traffic density data for all lines carrying one million gross ton-miles per mile per year or more be presented on a density map.

- The carload and intermodal operating plan is based on flawed traffic data drawn from inconsistent and unrepresentative samples.
- Unit trains are based on a non-representative sample of trains and were incorrectly input in some cases.
- Applicants deliberately chose to exclude any train that did not traverse at least 25 percent of the stations on a subdivision, thereby failing to account for an (unknown) number of local trains that were assigned traffic in Applicants' MultiRail modeling.[4]
- There are inconsistencies between the work papers and the actual values in the Application that leave one uncertain as to the accuracy of the Application.

– The analysis of which **yards** will experience an increase of activity greater than 20 percent is invalid because:
  - The operating plan is based on a flawed analysis of traffic data drawn from inconsistent and unrepresentative samples.
  - Applicants omitted originating/terminating unit train traffic from the MultiRail modeling process, thereby failing to include yard activity values for such traffic.
  - Applicants used the wrong operating plan for the base period in the comparison.
  - Applicants did not include in their calculation of yard activity "block swaps," an integral feature of precision scheduled railroading (PSR), upon which Applicants rely for a significant portion of their cost savings.
  - Not all yards that had significant changes in cars handled were disclosed in the operating plan.
  - Applicants miscounted intermodal cars.
  - In this area, too, there are multiple discrepancies between values in Applicants' work papers and the values in the Application.

Based on my knowledge of the operations planning process, the proper use of the MultiRail software supporting that process, and the material flaws I have described in

[4] Applicants note in FD 36500 – Work Paper – HC – Trains Per Day - Methodology.pdf that "The train must pass by at least 25% of the subdivision's segment stations in order to be counted on it."

the data, I conclude that Applicants have failed to meet the requirements of 49 CFR Part 1111.8(a)(1) and (5)(2000). Applicants have provided essentially meaningless responses to those provisions.

- **Applicants did not use their operating plan to calculate the merged railroad's operating metrics or expenses**: As described in this Verified Statement and in the Verified Statement of Hugh Randall,[5] in a customary operations planning process, metrics such as gross ton-miles (GTMs), train-miles, and cars switched are generated based on the operating plan, and are then used to drive the calculation of the merged railroad's operating expenses, equipment needs (required by 49 CFR Part 1111.8(a)(3)(2000)), and capital expenditures (required by 49 CFR Part 1111.8(a)(4)(2000)). Applicants failed to follow that customary procedure in this case. Instead, it appears that in calculating operating expenses, Applicants ignored the outputs of their MultiRail operations modeling, and instead used outputs generated by a simplistic spreadsheet model (which they call the "System Model" or "Cost Metrics Model"[6]).[7] This System Model is driven largely by estimated changes in GTMs that were not generated by the MultiRail operating plan.

  In fact, Applicants appear to have intentionally decided to develop their operating plan and operating expenses separately. Applicants' post-merger operating plan includes both "synergy growth" traffic from their traffic diversion studies and "organic growth" (growth resulting from general economic conditions unrelated to the proposed merger). On a systemwide basis, Applicants' post organic growth in traffic volumes of {{XXX percent}} increase from the Base Year to post-merger Year 3.[8] However, in calculating the merged CPKC's operating expenses, Applicants considered only "synergy growth traffic of 19.8" and excluded "organic growth" traffic.[9] It is not clear why Applicants

[5] *See* Verified Statement of Hugh Randall.
[6] FD 36500 – Work Paper – HC – System Model - Methodology.pdf, FD 36500 - Work Paper - HC - Cost Metrics Growth Model _ Base year 2019.xlsx.
[7] I state that Applicants "appear" to have calculated the costs based on outputs not generated by the operating model because I could not find anything in the work papers that demonstrated how the incremental operating costs in the financial statements were prepared, or even any linkage to the Applicants' "System Model/Cost Metrics Model."
[8] FD 36500 - Work Paper - HC - Cost Metrics Growth Model _ Base year 2019.xlsx (Reference tab).
[9] Application Vol. 1, p. 442 states that financials do not include any organic growth; Application Vol. 2, p. 286, ¶85 states that the operating plan includes organic growth.

took this inherently contradictory approach. What is clear is that the resulting operating expenses do not account for the cost of handling the {{XXX}} increase in "organic growth" traffic. As a result, their claimed operating expenses bear no relation to their operating plan.

- This disconnect is not insubstantial. For example, the operating plan produces an annual increase in train-miles of approximately {{XXX }}, while the costing process appears to be based on an assumed increase of only approximately {{XXX }} train-miles.[10]
- Similarly, the increase in GTMs based on Applicants' operating plan is {{XXX }}, while the costing process assumed an increase of only 76.3 billion GTMs, *less than half of the GTMs generated by Applicants' traffic studies inclusive of organic growth and by the operating plan*.[11]
- Other operating metrics customarily developed in the course of preparing an operating plan, such as train-miles, train-hours, and crew-starts, were also estimated without reference to the operating plan for purposes of estimating CPKC's post-merger operating expenses.[12]

Applicants' failure to generate a reliable set of operating statistics based on a unified and rigorous operations planning process, and to base their operating and capital expense calculations on such outputs from the operating plan, resulted in fatally flawed operating plan and operating expense evidence. Any conclusions reached by Applicants based on them are plainly unreliable. While Applicants attempt to leave the impression that they conducted a rigorous planning process, at the end of the day they essentially abandoned the outputs of this planning process in favor of a series of ad hoc calculations taken from a simplistic spreadsheet model.[13] The metrics generated by those ad hoc calculations are

[10] *See* HC – Oliver Wyman - Change in Train Miles and GTM from Base Year to Year 3.pdf for analysis and associated data sources.
[11] *See* HC – Oliver Wyman - Change in Train Miles and GTM from Base Year to Year 3.pdf for analysis and associated data sources.
[12] *See* HC – Oliver Wyman - Review of Operating Plan Statistics and Their Sources.pdf.
[13] FD 36500 – Work Paper – HC – System Model - Methodology.pdf, FD 36500 - Work Paper - HC - Cost Metrics Growth Model _ Base year 2019.xlsx, FD 36500 – Work Paper - STB Rail Road Control Application Model – Final.xlsx – Inputs – Revenues + Costs tab.

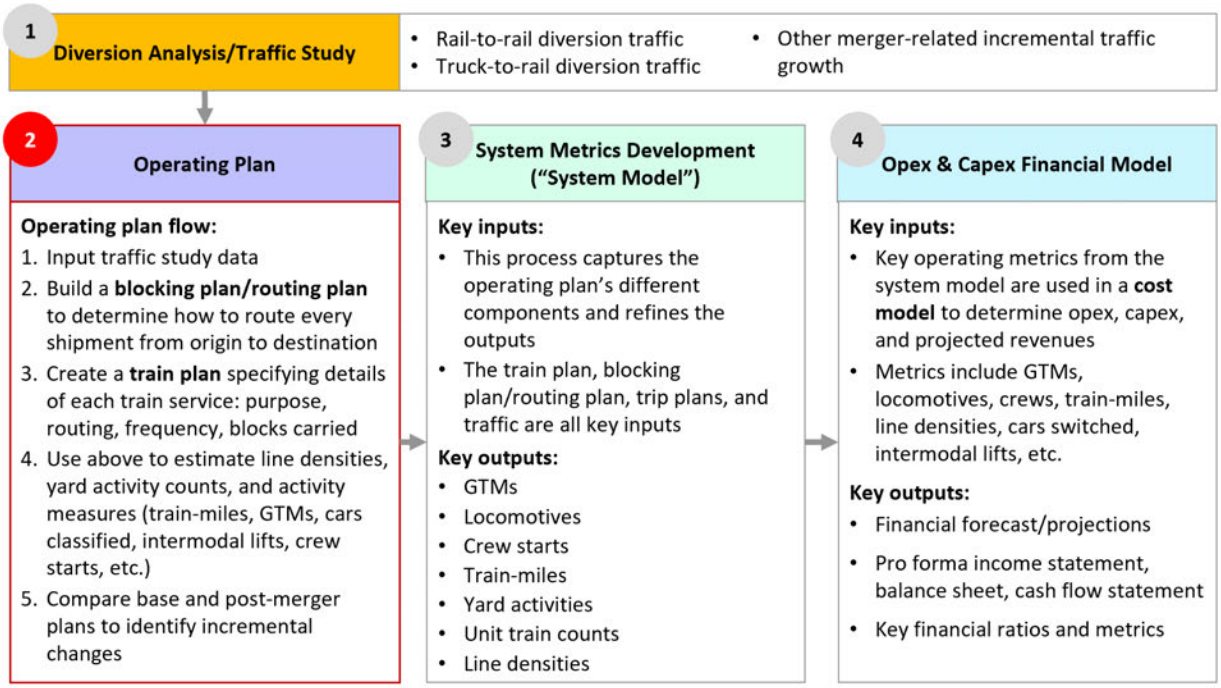
unreliable at best and distort Applicants' operating plan and both operating and capital expense calculations.

3. A Rigorous Operations Planning Process is a Key Element of a Reliable Merger Application

3.1 The operating plan plays a critical role in the application

Based on my direct experience in developing operating plans for prior merger applications, and the applications submitted in connection with those mergers, the Applicants in most recent Class I mergers generally have employed the process depicted in Exhibit 3-1. It is important to understand that this process for developing a merger application consists of a series of logical, interrelated steps: The **diversion analysis/traffic study** provides both revenue input to the financial plan and data concerning the anticipated volumes of carload, intermodal, and bulk commodity traffic that drive the development of an operating plan that is capable of accommodating that traffic. The **operating plan** is then used to generate key operating metrics that are used to calculate the merged carrier's operating and capital expenses. Those outputs, combined with the revenue estimate, drive the **financial plan**. Any failure to use reasonable inputs and/or generate accurate outputs at any step cascades through the process and renders the subsequent calculations invalid.

Exhibit 3-1: Elements of an adequate merger plan: The operating plan and system model provide outputs that drive calculation of operating and capital expenses and the financial plan[14]



The MultiRail software has been used in most recent Class I merger cases to develop the operating plan, including the car blocking and routing plan and train plan for the merged railroad. Based on that operating plan, Multirail generated operating metrics such as GTMs, train-miles, crew starts, and car handlings. Traffic was then carefully developed and tested to ensure that MultiRail would directly produce operating metrics for the base period that were consistent with historical values. For example, both the merger of Canadian National with the Illinois Central Gulf (CN-IC) and the merger of Norfolk Southern with Conrail (NS-CR) followed this process, and this approach is directly cited in their merger applications:

> CN-IC: "The pre-merger traffic flows were first determined, then the commercial and transportation plan teams worked with ALK and Reebie to determine the likely post-merger flows. MultiModal created a computer simulation of the combined rail system on its MultiRail model and the pre- and post-merger traffic was run through that

[14] This is the logic flow explicitly cited in the Canadian National-Illinois Central and Norfolk Southern-Conrail STB merger applications. Oliver Wyman was unable to find a statement indicating an explicit connection between operating plan and financial model in the Canadian Pacific-Kansas City Southern Application.

> simulation to assess train schedules, blocking patterns, and line and yard capacity. When the service design was complete, and the various related integration decisions were made, the MultiModal model produced a variety of operating statistics that were used…to assist the railroads in performing costing, benefits, and financial projections for the combined system. These and other operating statistics were also produced for the environmental and safety teams for their use in putting together environmental data and the Safety Integration Plan."[15]
>
> NS-Conrail: "To prepare the Operating Plan, I received traffic data, including new and diverted business, provided by NS's traffic consultants, and then applied that data to an operational modeling structure created by MultiModal, Inc. Our team then formulated the Plan, assisted by experienced NS operating and service management personnel. Outputs from the Plan were [used]…to estimate cost impacts of the Plan, and…for purposes of preparing the Environmental Report."[16]

In addition to generating the outputs needed for subsequent steps in the planning process, a normal operating plan modeling process supports development of a forward-looking operating plan, which is a specific requirement for the Application,[17] for the following reasons:

- To demonstrate the nature of the service to be provided and any service improvements or other benefits achieved during the first three years after the merger;
- To document the anticipated changes in activity levels for yards and lines, to show that sufficient capacity exists to handle the anticipated increase in traffic volumes (or to inform the capital planning process where investments in the physical plant are needed);
- To document the effects on labor due to changes in operations;
- To document that the merged railroad's locomotive and railcar fleets will be sufficient in light of changes in traffic volumes and operating strategy, and any associated capital requirement needs;
- To understand the changes in various operating metrics such as train-miles, crew-starts, and cars handled, which drive the process of estimating the incremental costs associated with the merger and any associated changes in volumes; and

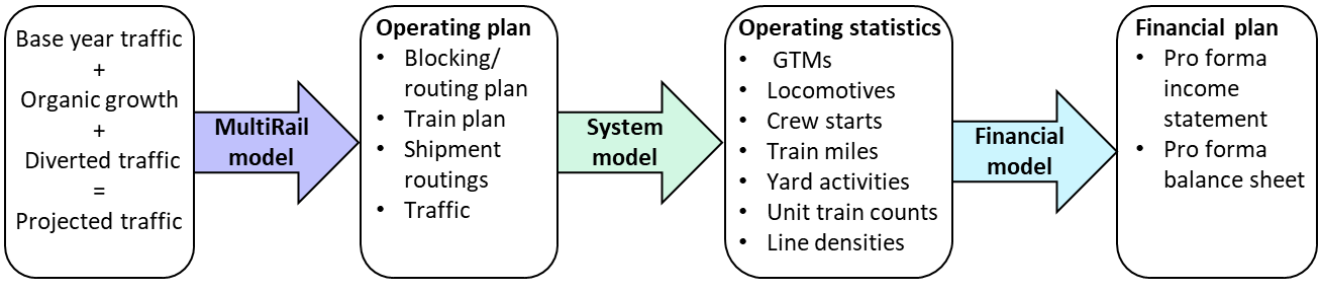
[15] Finance Docket No. 33556, Railroad Control Application, Surface Transportation Board, July 1998, Volume 2, pp. 5-6 (CN-IC merger).
[16] Finance Docket No. 33388, Railroad Control Application, Surface Transportation Board, June 1997, Volume 3B, p. 7 (Conrail merger).
[17] 49 CFR Part 1111 (2000).

- To provide information at a sufficiently granular level of detail on the changes to activity levels for lines and yards to support the assessment of environmental impacts.

3.2 Customary method for preparing an operating plan

The heart of the merger planning process is the development of the operating plan. As shown in Exhibit 3-2, in a customary and logical operating planning process for a merger, applicants utilize operations planning software, such as MultiRail, to flow projected traffic over a model of the merged railroad's network to develop the building blocks of the operating plan. Operating plan results are then processed to generate the operating statistics that are the key drivers of the merged railroad's operating and capital expense projections (i.e., the "System Model").

Exhibit 3-2: Logical operating plan development process



As the creator of the MultiRail software, I am keenly aware that the software relies on accurate traffic projections to produce reliable results. Traffic projections typically are based on a single, representative "base year" and include carload, intermodal, and unit train traffic for that year. Projections of organic growth and diverted traffic are then typically developed on a consistent basis and added to the base year traffic to develop a complete picture of the merged railroad's future traffic.

Typically, in prior recent mergers, applicants would build the network of the merged railroads into MultiRail and first flow **base year traffic** over that network using the applicants' pre-merger blocking and train service plans to verify that the model results are consistent with

actual operating results for the base year. Only then would applicants flow **projected traffic** for the merged railroads over the network, review the impact of this traffic on the operating plan, and adjust the operating plan both to accommodate changes in volumes and to leverage opportunities the merged network might provide. Based on this process, merger applicants can create consistent pre- and post-merger operating plans that include:

- A blocking and traffic routing plan that determines the route that each shipment will follow from its origin to its destination; and
- A train plan that specifies for each train its purpose, routing, service frequency, and the blocks it will carry.

The MultiRail model uses the traffic, blocking and traffic routing plan, and train plan to calculate line densities and yard activity counts. Merger applicants would then typically compare the base year and projected year densities and yard activity counts to identify line segments and yards that require additional investment to handle projected traffic. (Changes in line density also can be used as inputs to the environmental assessment of the merged system.) Once the operating plan is complete, a "system model" is then used to develop the key metrics for the plan, such as GTMs, train-miles, locomotives required, crew starts, and cars switched.

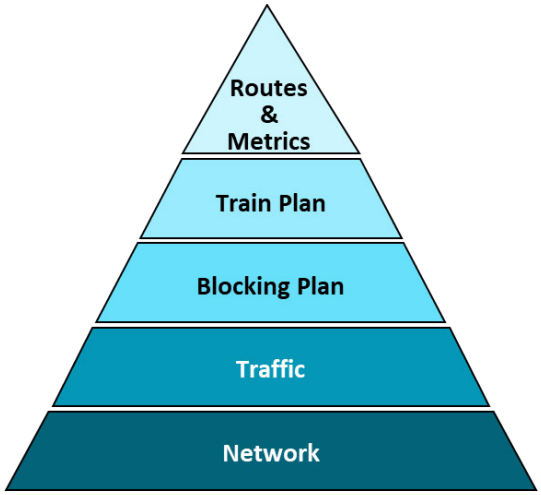
This process is clearly articulated, for example, in the Canadian National-Illinois Central merger application, including the development of the base case, creation of the post-merger case, development and refinement of the blocking plan, and generation of the changes in line volumes and yard activities.[18] That merger application provides explicit enumeration of details such as

[18] Finance Docket No. 33556, Railroad Control Application, Surface Transportation Board, July 1998, Volume 2, Exhibit 13, pp. 126-129.

block swap car volumes versus general switching activities,[19] and the explicit listing of passenger trains versus freight trains.[20]

Railroad operating plan modeling is essentially a "bottom up" process, in which each element of the plan is layered on the prior element, as depicted in Exhibit 3-3. The process begins with the network, followed by the traffic, blocking and routing plan, and train plan. If any foundational layer is flawed or incomplete, then each of the dependent layers are also flawed -- the adage "garbage in, garbage out" quickly comes to mind to describe the operating plan and key metrics based on inaccurate or unreliable inputs.

Exhibit 3-3: The operating plan modeling hierarchy



4. Applicants' Operations Planning Process

Applicants' operations planning process fails at nearly every level of the modeling hierarchy described above. The result is a set of modeling outputs that were so unreliable[21] that

[19] Finance Docket No. 33556, Railroad Control Application, Surface Transportation Board, July 1998, Appendix E to Exhibit 13, starting p. 255.
[20] Finance Docket No. 33556, Railroad Control Application, Surface Transportation Board, July 1998, Appendix F, starting p. 258.
[21] *See* Verified Statement of Hugh Randall for additional detail on operating and capital expense modeling outputs.

Applicants themselves disregarded their own operating plan outputs, including train-miles and GTMs – both of which are critical drivers of operating costs.

Instead, Applicants developed their incremental GTMs using manual calculations, based on the diversion analysis and (unsupported) estimates of car weights and distances traveled.[22] These externally estimated incremental GTMs did not include GTMs generated by Applicants' projected "organic growth" traffic – indeed, they were less than half of the incremental GTMs calculated in the operating plan.[23] Metrics such as incremental train-miles were computed in the Applicants' system model without reference to the operating plan by simply dividing the GTMs by an assumed average train weight value. As a result, the train miles in the Applicant's system model are roughly {{ }} of the incremental train-miles that resulted from the MultiRail operations modeling.[24] Similarly, the line densities from the MultiRail operating plan were significantly modified or "calibrated" to make it appear that the operating plan outputs were consistent with the system model at an aggregate level.[25]

4.1 Applicants have failed to produce reliable base year traffic or operating plan.

Based on my experience, a critical initial step in the operations modeling process for a merger is to create a "pre-merger plan," which involves flowing the merged railroads' base year traffic over the network, and a base period operating plan (once this has been coded into the

[22] FD 36500 - Work Paper - HC - 1.Proposed Final FTI Rail to Rail Diversion Results for Merger Application 10_21_20 Updat_Truck_Rev.
[23] *See* HC – Oliver Wyman - Change in Train Miles and GTM from Base Year to Year 3 Used in Cost Metrics/System Model and HC – Oliver Wyman - MultiRail Estimates – Methodology.pdf for analysis and associated work papers: FD 36500 - Work Paper - HC - Trains Per Day and Gross Ton Miles - 2021.10.22 - Working Copy with Haz Breakdown.xlsx, FD 36500 - Work Paper - HC - Cost Metrics Growth Model _ Base year 2019.xlsx.
[24] *See* HC – Oliver Wyman - Change in Train Miles and GTM from Base Year to Year 3 Used in Cost Metrics/System Model and HC – Oliver Wyman - MultiRail Estimates – Methodology.pdf.
[25] FD 36500 – Work Paper – HC – Gross Ton Miles, Train Miles, Train Weights and MGT – Methodology; FD 36500 - Work Paper - HC - Cost Metrics Growth Model _ Base year 2019; FD 36500 - Work Paper - HC - Trains Per Day and Gross Ton Miles - Working Copy with Haz Breakdown.xlsx.

operations planning software, such as MultiRail), to verify that the model produces realistic operating statistics. Once it is verified that the model is correctly coded, and that the traffic inputs are accurate, the process should produce modeled operating statistics within plus or minus 5 percent of the railroads' actual base year operating statistics. Typical statistics used in this process include car-miles by load/empty and major car type (intermodal, boxcar, covered hopper, etc.), train-miles by major train type (local, intermodal, unit, manifest), and GTMs. Volumes at key locations should also be spot checked. The MultiRail software's diagnostics capabilities also identify issues like highly circuitous moves that reveal areas where the base year plan may have errors. Where the statistics do not match, merger applicants should use the results of the validations to identify and correct problems with the coded network, traffic data, and base operating plan until a satisfactory outcome is achieved.

Based on my review of the Application and associated work papers, there is no evidence that Applicants tested their MultiRail operations planning model to ensure consistency with CP and KCS historic performance/metrics. Further, because unit train traffic was excluded entirely from the Applicants' MultiRail model,[26] any comparisons would have to be done using multiple sources for the statistics such as October 2020 for carload and intermodal traffic, and October 2019 for unit train traffic, and a train plan based on operations during Q1, 2021. The lack of validation is clearly demonstrated by the failure of the Applicants to recognize that their actual October 2020 traffic had almost no intermodal traffic out of Lazaro Cardenas due to labor actions near the port (see Section 5.2 for further details), which would have resulted in a depressed number of intermodal car-miles that should have been obvious in any validation

[26] *See* FD 36500 – Work Paper – HC – Trains Per Day – Methodology.pdf, sections 3.3-3.5. *See* also FD 36500 – Work Paper – HC – Traffic File - Methodology.pdf , Section 1: "Note that Bulk Train Design is completed outside of the MultiRail application…"

process. This is critical, because an accurate, representative base year traffic file – which incorporates all traffic types, including unit trains – is the foundational layer upon which all the other layers in the operations modeling process are dependent. Applicants have not provided parties either the operating plan model or the input files underlying their Application, so the accuracy of the base traffic or operating plan cannot be independently verified. But the fact that Applicants found it necessary to abandon the outputs of their MultiRail modeling and to introduce manual adjustments and "calibrations" suggests that the network, traffic, and base operating plan are incorrect.

4.2 Applicants' pre- and post-merger traffic file is flawed

Once the base period traffic and operating plan have been verified, applicants in the most recent Class I mergers would typically flow projected traffic for the merged railroad over the network to produce the post-merger operating plan.[27] The post-merger plan is typically a variation of the pre-merger plan, taking into account both the changes in traffic volumes that must be accommodated and the opportunities that are likely to arise from the merger. Based on the post-merger operating plan, the Year 3 line density and yard activity data required by 49 CFR Part 1111.8(a)(1) and 1111.8(a)(5)(2000) can be developed. Operating statistics that are critical to developing operating and capital expenses for the merged railroad (such as GTMs, train-miles, train starts, crew starts, and locomotives required) are also generated at this stage. It is critical that the projected traffic data that is the foundation for these calculations is as complete and accurate as possible.

[27] Finance Docket No. 33556, Railroad Control Application, Surface Transportation Board, July 1998; Finance Docket No. 33388, Railroad Control Application, Surface Transportation Board, June 1997.

The traffic data employed by Applicants in conducting their MultiRail modeling is anything but complete and accurate. This is true for many reasons, the most significant issues being as follows:

- **Applicants falsely claim that they were forced to use a representative month because MultiRail can accommodate only 28 days of traffic data.**[28] As the creator of MultiRail, I am uniquely qualified to state that this claim is false. The "days in period" functionality in the MultiRail software allows Applicants to accommodate up to 365 days of data. Furthermore, even if the 28-day limitation were true, it is a relatively easy task to take a full year of traffic and convert it to a set of representative (or "average") values for either a 7- or 28-day period. Applicants do not explain why they chose to rely entirely on a single month of data – with all the issues that creates – when they could have used a full year of data.[29]
- **Applicants chose to use traffic data from October 2020 to represent base year carload and intermodal traffic but used a month from a different year to represent base year unit trains.**[30] For unit trains, Applicants chose to use the actual trains operated during the month of October 2019 as a proxy for unit train operations during the base year (without examining or using the underlying traffic). October 2019 is a full year removed from the month of October 2020 that was used by the Applicants to support all other analytics. Applicants provide no explanation for why they chose a month from a different year than the base year to model their base carload and intermodal traffic volumes, and then and a completely different month/year for unit trains.[31] As noted above, there is nothing in the MultiRail software that would have prevented Applicants

[28] FD 36500 – Work Paper – HC – Traffic File - Methodology.pdf , Section 3. Process Detail notes that "CPRS chose to use October 2020 for a base month as MultiRail only can process 1 month at a time,"

[29] In Canadian Pacific Railway Limited, Et Al. – Control – Kansas City Southern, Et. Al. STB Docket No. FD 36500, Elphick and Orr Dep. 160:15–160:17, Feb. 18, 2022: {
}

[30] dwnld_Traffic_KCS.csv provided as part of the accompanying attachments to Traffic File - Methodology.pdf indicate the traffic data used was from October 2020; FD 36500 - Work Paper - HC - CP Bulk Cars Per Day By Sub.xlsx, and FD 36500 - Work Paper - HC - KCS KCSM Bulk Train Cars Per Day by Subdivision.xlsx provided as part of the accompanying attachments to Trains Per Day - Methodology.pdf.

[31] It is interesting to note that footnote 4 on p. 283 of Application Vol. 2 indicates that the "2019" base year operating plan CPKC chose to create in MultiRail actually reflects the Q1 2021 operating plan (with October 2019 unit trains, and October 2020 intermodal and carload traffic).

from modeling the full base year traffic using the correct year. The choice to use October 2020 for Applicants' base carload and intermodal traffic leads to significant flaws in traffic volumes in aggregate and by lane.[32] This has particularly large impacts for intermodal traffic originating at the Port of Lazaro Cardenas, which was largely closed in October 2020 due to labor issues.[33]

- **Applicants offer no evidence that their modeling of base year unit train traffic is accurate or reliable.**[34] Nothing in the Application explains Applicants' methodology for determining which bulk commodity traffic was unit train traffic, or why it was necessary to exclude unit trains from their MultiRail modeling. Based on my actual experience undertaking numerous efforts to identify unit train traffic in waybill data sets, it can be a challenging task to identify specific carloads that moved in a unit train, because loaded movements are not clearly delineated as "unit train traffic" in waybills, and empty moves do not always return to the origin of the loaded move and sometimes go on to diverse next destinations. For this reason, it is more accurate to undertake unit train modeling within MultiRail, so that the traffic that does not conform to unit train standards will drop through to the carload network and not get lost in a "gap" between the two modeling approaches.

- **Applicants correctly included organic growth in the post-merger traffic used to develop the operating plan in MultiRail but excluded that organic growth from the costing process**.[35] The contradiction in Applicants' use of "organic growth" projections indicates that Applicants did not use the results of the operating plan to drive the costing process. Consequently, train-miles, car-miles, and GTMs arising from the operating plan

[32] *See* work paper: FD 36500 – Work Paper – HC – Traffic File - Methodology.pdf , Section 3 (B). Section header indicates "desired month" was October, 2019, while details indicate that "XXX" In Canadian Pacific Railway Limited, Et Al. – Control – Kansas City Southern, Et. Al. STB Docket No. FD 36500, Elphick and Orr Dep. 160:15–160:17, Feb. 18, 2022: Deponent Elphick states: {"XXX"}

[33] "Rail blockade ends in Mexico," Freight Waves, December 2, 2020.

[34] FD 36500 – Work Paper – HC – Gross Ton Miles, Train Miles, Train Weights and MGT – Methodology.pdf, FD 36500 - Work Paper - HC - New Bulk Input w Year Splits 2021.10.20.xlsx, FD 36500 - Work Paper - HC - Trains Per Day and Gross Ton Miles - Working Copy with Haz Breakdown.xlsx, FD 36500 - Work Paper - HC - CP Bulk Cars Per Day By Sub.xlsx, FD 36500 - Work Paper - HC - KCS KCSM Bulk Train Cars Per Day by Subdivision.xlsx, FD 36500 – Work Paper – HC – Synergy Bulk Train Run Details - Year 1, 2, 3 with summary – Copy.

[35] Application Vol. 1, p. 442 states that financials do not include any organic growth; Application Vol. 2, p. 286, ¶85 states that the operating plan includes organic growth.

are more than twice the values Applicants ultimately used to develop their operating and capital expenses. As noted earlier, the operating plan produced an increase of {{XXX }} gross-ton-miles including organic growth, while Applicants' operating expense calculations are based on a value of 76.3 billion gross-ton-miles excluding organic growth.[36] Since organic growth is certain to occur (and was estimated by Applicants to be more than {{XXX }} by Year 3),[37] Applicants' financial projections clearly understate the costs and capital requirements associated with Year 3 operations.

Applicants' approach to projecting traffic introduced a multitude of opportunities for fundamental errors. Carload and intermodal traffic that moved in October 2020 is not representative of carload and intermodal traffic moved during October 2019 (much less the full Base Year). Likewise, Applicants introduced no evidence to support the assumption that bulk commodity traffic moved during October 2019 is representative of full Base Year bulk traffic. The nine hypothetical unit train pairs[38] created by Applicants may not accurately represent the merged railroads' new unit train grain traffic. Applicants' decision to include organic growth in the operations modeling process but then exclude it from the spreadsheet/costing model introduces major inconsistencies in Applicants' projections. Based on my review of the Application and work papers, Applicants provide no proof that their traffic estimates or the base operating plan are accurate or representative.

Applicants did not need to adopt such a complex and disjointed modeling approach. As part of developing the analysis of the proposed merger of Canadian National and KCS, I led a team

[36] The Summary Table tab of the work paper FD 36500 - Work Paper - HC - Cost Metrics Growth Model _ Base year 2019.xlsx presents an incremental GTM value of {{ }} when organic growth is included, and an incremental GTM value of 76.3 billion when organic growth is excluded (when annualized). See HC – Oliver Wyman - Change in Train Miles and GTM from Base Year to Year 3 Used in Cost Metrics/System Model and MultiRail Estimates – Methodology for analysis and associated data sources.

[37] The {{XXX}} percent organic growth is based on values provided in FD 36500 - Work Paper - HC - Cost Metrics Growth Model _ Base year 2019.xlsx, Reference tab.

[38] FD 36500 - Work Paper - HC - Trains Per Day and Gross Ton Miles - 2021.10.22 - Working Copy with Haz Breakdown.xlsx, Bulk Reference tab, shows nine new train pairs for loaded and empty traffic in the Train Symbol column.

that developed an operating plan using MultiRail software and full-year traffic data, including bulk commodity unit train traffic. The model was built on actual base year inputs and provided outputs in a consistent and rigorous fashion. There is no reason that Applicants could not have provided an operating plan based on the same rigorous process.[39] I also can state that based on personal experience with the CN-IC and Norfolk Southern-Conrail merger operating plans, both plans used full-year data that was from the same year as the base period.[40]

4.3 Applicants failed to correctly estimate line density, train counts, and yard activity

49 CFR Part 1111.8(a)(1) and 1111.8(a)(5)(2000) specifically require merger applicants to provide an estimate of post-merger traffic density and train counts on all main and secondary rail lines and to identify all yards that are projected to experience an increase in activity greater than 20 percent.[41] The operations planning process followed by Applicants does not provide sufficiently robust or accurate information to meet these requirements.

Accurate estimates of line density, train counts, and yard activities are critical to demonstrating that a merged railroad will be able to move the projected post-merger traffic over the network without degrading service. Research by the Association of American Railroads (AAR) has proven that as traffic on a railroad line approaches the line's practical capacity (which the AAR defines as 70 percent of its theoretical capacity[42]), the level of service on the line

[39] In workpaper FD 36500 – Work Paper – HC – Traffic File - Methodology.pdf Section 3 (B) Applicants state "FTI supplied CPRS with multiple years of data, but CPRS chose to use October 2020" from which one can infer that Applicants could instead have "chosen" to use the full year 2019 data to be consistent with the Applicant's selection of 2019 as their base year.

[40] Finance Docket No. 33556, Railroad Control Application, Surface Transportation Board, July 1998, Vol. 2, p. 127 (2.1 Base Period); Finance Docket No. 33388, Railroad Control Application, Surface Transportation Board, June 1997, Vol. 3B, p. 90 (2.1 Base Period).

[41] 49 CFR Part 1111.8(a)(1)(2000).

[42] {{XXX}} See: Canadian Pacific Railway Limited, Et Al. – Control – Kansas City Southern, Et. Al. STB Docket No. FD 36500, Elphick and Orr Dep. 60:25 – 61:16, Feb. 18, 2022

degrades.[43] Accurate line density data are essential in identifying line segments where degraded service will occur, therefore requiring the provision of capital investment to increase capacity.

Similarly, accurate estimates of yard activity are essential for identifying yards with insufficient capacity to handle post-merger switching activity. Failure to estimate post-merger yard activity correctly and to provide for the capital investment needed to keep yards fluid can lead to catastrophic network failures. For example, following the merger of the Union Pacific and Southern Pacific, Englewood Yard in Houston did not have enough capacity to handle the increase in traffic from the merger. The yard became overwhelmed, resulting in gridlock on Union Pacific routes in the Houston area, which then cascaded out into service disruptions across the railroad's network.[44]

Likewise, train counts and yard activity levels are central to the environmental review process. Clearly, developing accurate estimates of line and yard capacity is too important to be left to ad hoc and untested processes, particularly where, as here, Applicants had tools at hand, such as MultiRail, to develop estimates in a rigorous manner.

4.3.1 Line density

As previously discussed, in a customary operations planning process, all carload, intermodal, and bulk unit train traffic is flowed over the network and is coded into the operations planning software (i.e., MultiRail). The software develops estimates of traffic density and train counts by line segment and car handlings by yard. Applicants did not follow such a procedure. Instead, they employed an overly complex process to compute line density values that used a

[43] National Rail Freight Infrastructure Capacity and Investment Study, Association of American Railroads, September 2007, p. A-10, where it notes "Practical capacity is about 70 percent of the theoretical capacity and provides reliable service."
[44] "Problems in Wake of Merger Continue for Union Pacific," Wall Street Journal, October 2, 1997.

combination of (1) historic tonnage, (2) train counts (without weight values[45]) extracted from MultiRail for selected traffic and trains, and (3) a separate manual process for estimating tons for existing and new unit trains.[46] In addition to being based on inaccurate traffic data, including a purely statistical representation of organic growth-related changes in unit trains,[47] the Applicants' estimates do not include trains that operated over an arbitrarily determined subset of a line segment.[48]

As the designer of MultiRail, I know that this tool is fully capable of estimating the weights of trains. Once traffic has been loaded, and routed, the size of each train is estimated, including its weights. These weights are responsive to changes in the operating plan, such as train frequency and shipment routings. Thus, if you are trying to estimate train weights, and the effects of changing the operating plan design, it is far more effective to do this using MultiRail than by applying a set of fixed, historic train weights that are insensitive to the operating plan design.

In developing their line density analysis, Applicants chose to ignore tonnage values by line segment from MultiRail. Instead, they computed tonnage values using an aggregate tonnage spreadsheet model (which also was divorced from the tonnages in the system model).[49] Any differences between the aggregate tonnage spreadsheet model and the tonnages by line segment

[45] {XXX}. *See* Canadian Pacific Railway Limited, Et Al. – Control – Kansas City Southern, Et. Al. STB Docket No. FD 36500, Elphick and Orr Dep. 188:8 – 192:20, Feb. 18, 2022.
[46] FD 36500 - Work Paper - HC - Trains Per Day and Gross Ton Miles - 2021.10.22 - Working Copy with Haz Breakdown.xlsx.
[47] *See* Section 5.3.1 of this Verified Statement for details on the handling of unit trains.
[48] Applicants note in FD 36500 – Work Paper – HC – Trains Per Day - Methodology.pdf that "The train must pass by at least 25% of the subdivision's segment stations in order to be counted on it."
[49] FD 35600 - Work Paper - HC - 1.Proposed Final FTI Rail to Rail Diversion Results for Merger Application 10_21_20 Updat_Truk_Rev.xlsx.

were obfuscated by applying numerous "calibration factors" to the process.[50] These calibration factors had the effect of significantly distorting growth values in many cases, leading to further errors in density values. For example, while Applicants use an organic growth factor through Year 3 for KCS of approximately {{ in the system model, they instead applied the higher merged system average growth rate of {{ }} for the KCS subdivisions.[51] They then compounded this error through the use of "calibration factors" to cause the effective organic growth rate to exceed {{ }} on the Kansas City-Springfield line, more than double the correct value of {{ }}.[52] Applicants do not explain why they chose to use an untested (and unprecedented) process requiring a series of unorthodox adjustments, when the MultiRail software offered a much more transparent and integrated way to conduct the analysis thoroughly and accurately.

The Applicants' process produced line density (tonnage) results that are demonstrably incorrect on essentially every subdivision. In short, these values are wrong and cannot be used for any purpose.[53]

4.3.2 Yard activity

The Applicants' process for estimating changes in yard activity is similarly flawed. To begin with, any errors in traffic volumes and mix (e.g., due to it being for a non-representative time period[54] or due to processing errors in creating the MultiRail traffic data) carried through to the

[50] FD 36500 - Work Paper - HC - Trains Per Day and Gross Ton Miles - 2021.10.22 - Working Copy with Haz Breakdown.xlsx.
[51] *See* HC – Oliver Wyman - Review of Growth Factors in CPKC Application.pdf.
[52] *See* Sections 5.1 and 6.1 of this Verified Statement for specific examples; also see Section 5.3.1 for example of errors in unit train counts. *See* HC- Oliver Wyman - Review of Growth Factors in CPKC Application.pdf and HC - Oliver Wyman – Springfield Line 30 Percent Growth.pdf.
[53] *See* Sections 5.1 and 6.1 of this Verified Statement for specific examples of invalid line density values.
[54] *See* prior discussion of use of October 2020 for intermodal and carload traffic, and October 2019 for unit trains.

yard statistics in the Application. As shown in Exhibit 3-1 and previously discussed, in a customary operations planning process, activity per yard is a direct output of the MultiRail software. Applicants, however, produced values from MultiRail that excluded unit traffic, with no footnote on or explanation for the missing traffic.[55] Applicants then relied on a pieced-together combination of MultiRail outputs and manually calculated unit train traffic originating/terminating volumes by location to estimate yard activities for the purposes of the environmental filing.[56] The result is that *the yard activity values submitted by applicants to the Board in the environmental filing and the operating plan are not the same*. In addition, Applicants' estimate of yard activities intentionally excluded block swaps (a key element of the PSR efficiencies touted in the Application)[57] and underestimates intermodal yard counts by a factor of 2.5, using a non-standardized approach to counting intermodal platforms.[58]

Next, instead of providing the required comparison between the Base Year and Year 3 yard activity, Applicants provided a comparison between a so-called "optimized plan" and the post-merger plan in the main body of the Application, and an uninterpretable and mislabeled comparison of the optimized plan with the growth plan in an appendix.[59] Doing so does not comply with the Board's regulations.

[55] *See* Section 5.3.1 of this Verified Statement for discussion of Applicants' handling of unit trains and traffic.
[56] Based on file submitted to the Board by Venable LLP and CP under Comment ID "31353" (31353.pdf), which contains master segment and yard tables with information on environmental trains per day.
[57] Of the 21 new trains listed by Applicants in Application Vol 2., Appendix I, pp. 438-442, at least 20 appear to engage in block swaps, particularly at Shreveport, Sanchez, and Chicago.
[58] *See* HC – Oliver Wyman - Intermodal to RailCar Conversion Factor Source Compilation.pdf.
[59] Application Vol, 2, p. 292, ¶100 states that Appendix B "displays all yard volume changes under the Optimized Plan and Growth Plans" – as discussed in Section 6.3 of this Verified Statement, the reports in Appendix B are mislabeled, making it impossible to determine their exact content. The only tables in the main body of the Application are Table 3, on p. 297 of Vol. 2, which is strictly between the base plan and the optimized plan, and Table 5, on p. 305 of Vol. 2, which is between the optimized plan and the growth plan. A reliable, direct comparison between the base plan and the growth plan is not present in the Application.

Applicants also ignored the requirement to identify all yards that have a projected 20 percent or greater change in car handlings, leaving out the details of several highly impacted locations (Port Arthur, TX for example).

4.3.3 Train counts by subdivision

Applicants' train counts by subdivision also are unreliable due to a variety of factors, including the use of invalid base traffic (see Section 4.1), errors in estimating post-merger traffic volumes (particularly for intermodal – see Section 4.2), the exclusion of any train that did not traverse at least 25 percent of the stations on a line segment,[60] the use of a one-month sample period for unit trains,[61] errors in the entry of unit train counts,[62] and the failure to break out any passenger trains operating over a subdivision.[63] In addition, the source for the train counts used in the filing provided by Applicants in response to CN discovery request #115 does not match the values presented in the Application.[64]

One of the key "rules" applied by Applicants in developing the system model train counts was a decision to exclude all trains that traversed fewer than 25 percent of the "MultiRail nodes" in a subdivision.[65] MultiRail nodes are placed by the modeler based on topographic and operational characteristics of the network and bear no relationship to distance.[66] Thus, one pair

[60] Applicants note in FD 36500 – Work Paper – HC – Trains Per Day - Methodology.pdf that "The train must pass by at least 25% of the subdivision's segment stations in order to be counted on it."
[61] See FD 36500 – Work Paper – HC – Trains Per Day - Methodology.pdf.
[62] See Section 5.3.1 of this Verified Statement.
[63] No passenger trains are listed in Applicants' train counts by line segment tables (Application Vol. 2, Appendix A, pp. 363-368. In contrast, *see* Finance Docket No. 33556, Railroad Control Application, Surface Transportation Board, Vol. 2, July 1998, pp. 258-264, Appendix F (Train Densities) (CN-IC merger).
[64] *See* response #115, "Kansas City Southern and Canadian Pacific's Joint Responses and Objections to Canadian National Railway Company's First Set of Discovery Requests," p. 91.
[65] Applicants note in FD 36500 – Work Paper – HC – Trains Per Day - Methodology.pdf that "The train must pass by at least 25% of the subdivision's segment stations in order to be counted on it."
[66] In the MultiRail software, the physical rail network is represented as a series of node and links. Each node represents a station on the railroad or a location that plays a role in properly describing the railroad network, such as a junction point. Links are the tracks that connect nodes (stations).

of nodes could be one mile apart, and another pair could be 25 miles apart. To use node count as a screening criterion is improper and unreliable, as it is not truly a distance-based criterion. Furthermore, Applicants provide no rationale as to why trains should be excluded simply because they operate over only part of a subdivision. Indeed, Applicants' approach {{XXX}}.[67] The peak train count on a subdivision, even if it does not traverse the full subdivision, might be of more value than the average count of trains traversing the full subdivision, as the peak train count could be more important from a capacity and environmental perspective.

In Canadian Pacific Railway Limited, Et Al. – Control – Kansas City Southern, Et. Al. STB Docket No. FD 36500, Elphick and Orr Dep. 176:7 – 180:3, Feb. 18, 2022 deponent Elphick states that { } By witness Elphick's own admission, {XXX}.

4.4 Applicants largely abandoned their MultiRail operating plan in developing the merged carrier's operating expenses.

Compared to Class I merger filings since the mid-1990s,[69] Applicants' planning process is disjointed, resulting in misaligned, misleading, and erroneous outputs of such frequency and magnitude that Applicants apparently were unable to use their activity-based MultiRail operating statistics as the basis for projecting operating and capital costs to move Year 3 projected traffic.[70]

As noted previously,[71] in a customary merger planning process, current and projected traffic flows for the merging railroads are loaded into an operations model (such as MultiRail). Using the functionality included within the model, an operating plan is developed. This process

[67] HC - Remote Videotaped Deposition of Raymond A. Elphick and John F. Orr, STB Docket No. FD 36500, Elphick Deposition, pp. 178:22, Feb 18, 2022.
[68] HC - Remote Videotaped Deposition of Raymond A. Elphick and John F. Orr, STB Docket No. FD 36500, Elphick Deposition, pp. 178:9 – 178:10, Feb 18, 2022
[69] See discussion in Section 3 above.
[70] See discussion below and Verified Statement of Hugh Randall for additional detail on operating and capital expense modeling outputs.
[71] See Section 3.1 (Exhibit 3-1).

results in a blocking plan, train plan, a routing plan for each traffic movement, as well as resulting operating statistics. The operating statistics are then input into a financial model to develop operating costs. In this model, based on the historic relationships between operating statistics and each category of operating expense for the merging railroads, operating statistics are converted into estimated operating expenses for the combined railroad and become inputs to the post-merger financial projections for the merged railroad.[72]

While Applicants employed MultiRail as a first step in preparing their operating plan, Applicants did not follow the process used in past mergers that utilized the outputs of the MultiRail model to support the costing process.[73] For example, while Applicants included organic growth in the MultiRail traffic, they (inexplicably) chose to exclude it in developing post-merger operating expenses. As a result, it became impossible to use operating statistics such as train-miles from MultiRail in the costing process. This decision had a major (negative) impact on the reliability of Applicants' operating cost estimates. While MultiRail produced an estimated increase in train-miles of approximately {{ }} per year, the costing process was based on a "no organic growth" increase in train miles of only about {{ }} per year.[74] This lower value was generated by Applicants' system model, which incorporated various assumptions about efficiency gains, so as to produce a very low incremental increase in train-miles. None of those efficiency gains have been proven using MultiRail or any

[72] The verified statement by Kent and Klick in the CN-IC merger application provides an excellent example of the use of operating metrics to drive the costing process (see Finance Docket No. 33556, Railroad Control Application, Surface Transportation Board, July 1998, Verified Statement of Kent and Klick, starting on p. 289)

[73] Finance Docket No. 33556, Railroad Control Application, Surface Transportation Board, July 1998, Vol. 2, pp. 127-129, and Verified Statement of Kent and Klick, starting on p. 289; *See* also Finance Docket No. 33388, Railroad Control Application, Surface Transportation Board, June 1997, Volume 3B, pp. 90-92.

[74] *See* HC – Oliver Wyman - Change in Train Miles and GTM from Base Year to Year 3.pdf for associated analysis and workpapers.

other detailed operating analysis – to the contrary, they are based entirely on a set of externally provided assumptions.

Applicants obfuscate this fact by portraying metrics in their Application as if they were derived from the operating plan – for example, in Table 2 on page 28 of Volume 2 of the Application.[75] In fact, the metrics in Table 2 have little to do with the operating plan and were sourced instead from the previously cited system model.

In Canadian Pacific Railway Limited, Et Al. – Control – Kansas City Southern, Et. Al. STB Docket No. FD 36500, Elphick and Orr Dep. 180:8 – 184:22, Feb. 18, 2022, deponent Elphick is asked about Table 2, and the role of the system model. In response to a series of questions on whether MultiRail produced the statistics in Table 2 the following exchange took place:

{

}

In later questioning Elphick stated:

{ }

Exhibit 4-1 depicts my understanding of the process actually used by Applicants to generate the operating plan and metrics used for costing.

[75] *See* HC – Oliver Wyman - Review of Operating Plan Statistics and Their Sources.pdf.

Exhibit 4-1: Application operating plan flaws: no connection between the operating plan, system model, and financial projections

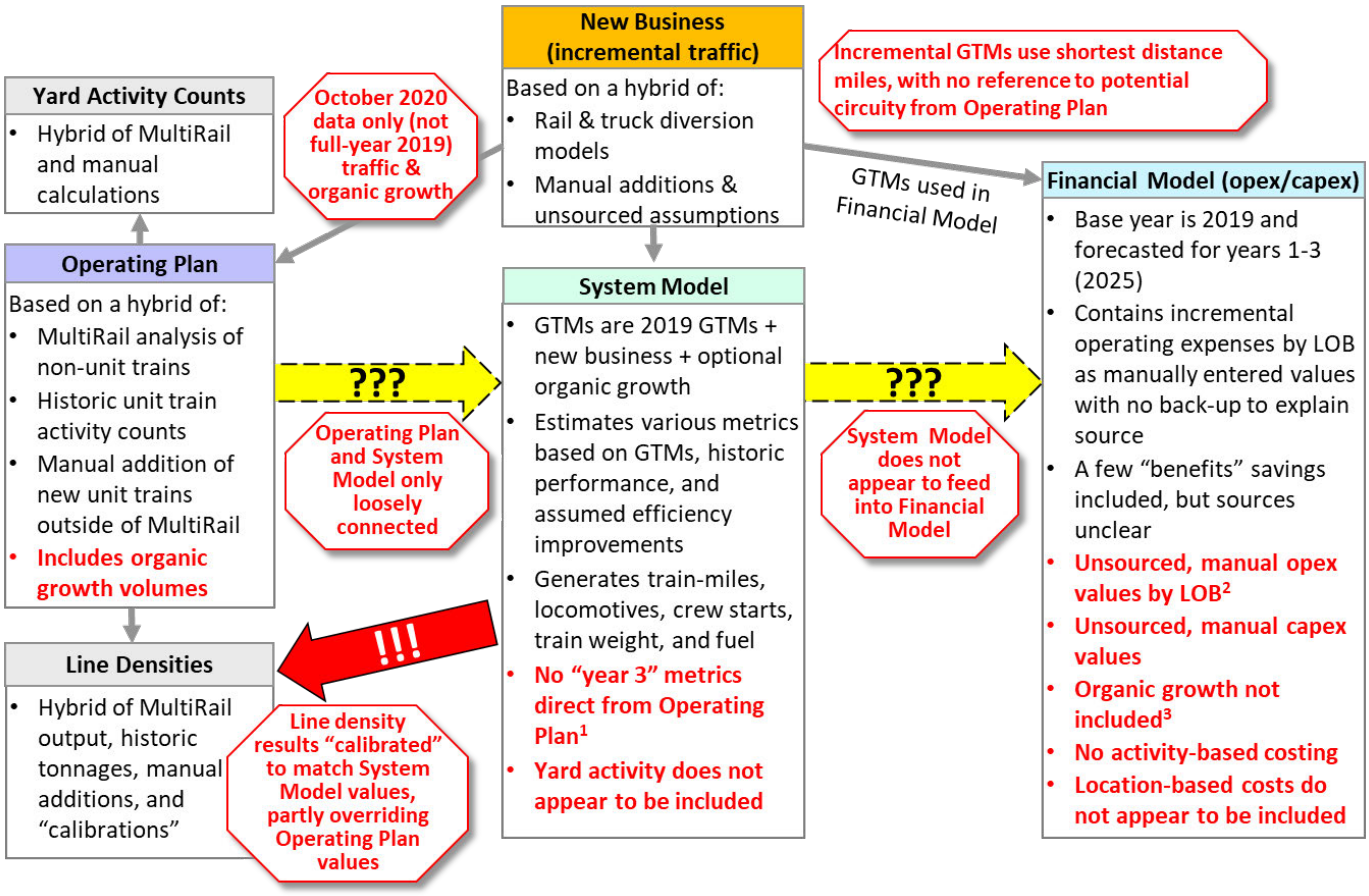


Exhibit 4-1 illustrates that the metrics used by the Applicants in the costing process are *not* based on the operating plan, but instead are based on a set of standalone assumptions about how various metrics will change in response to changes in volumes. In the system model, ton-miles are the key metric that drives the generation of almost all other metrics, such as changes in train-miles and crew starts. But the projected change in ton-miles in the system model was not based on the operating plan, but rather resulted from a process that does not utilize key considerations,

such as actual empty/loaded ratios and the effects of the operating plan on circuity – all of which are normally considered in the operating plan modeling process.[76]

Applicants have not explained why the metrics developed from their operating plan were not flowed through to the financial model, as they would in a typical merger application. As stated above, a review of the Application and associated work papers did not identify any links between the methodologies or Excel-based "models" that tied the operating plan to incremental operating expense costing. Applicants' projected operating costs are presented by line of business; a review of the Application and workpapers did not yield any statistics either in the operating plan or the system model that were organized in this manner.[77]

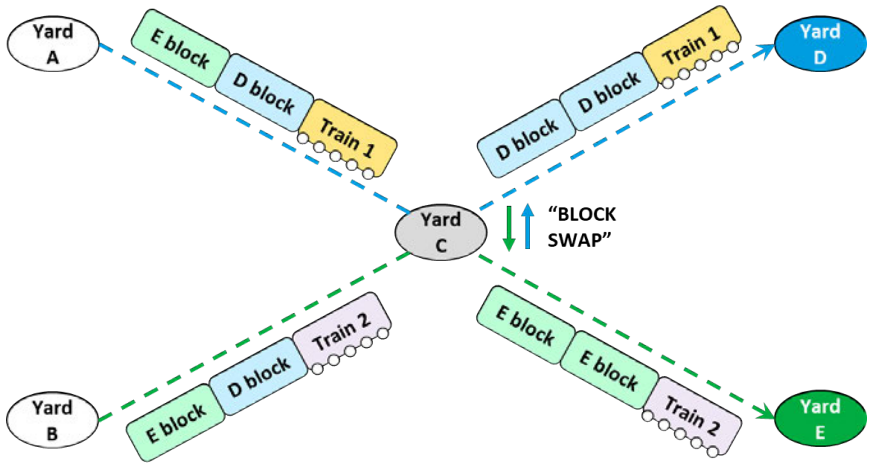
A central element of PSR and of the "optimized plan" presented by Applicants is a reduction in intermediate car classifications through the creation of more direct blocks closer to the origin of shipments and the increased use of block swaps. In point of fact, of the 21 new trains Applicants describe, my review indicates at least 20 of those trains are involved with block swaps, primarily at Shreveport, Sanchez, and Chicago.[78]

[76] FD 36500 - Work Paper - HC - 1.Proposed Final FTI Rail to Rail Diversion Results for Merger Application 10_21_20 Updat_Truck_Rev xlsx.
[77] *See* Verified Statement of Hugh Randall.
[78] Application Vol. 2, Appendix I, pp. 437-442.

A "block swap" refers to the movement of an intact group of cars from one train to another.

For example, consider the following diagram (Exhibit 4-2):

Exhibit 4-2: Block swap example



In this example, Yard A and Yard B each make blocks for D and E. When Train 1 leaves Yard A it carries both D and E blocks, and when Train 2 leaves Yard B it carries both D and E blocks. But Train 1 only goes to D (blue line) and Train 2 only goes to E (green line). However, since both trains travel via Yard C, they can "swap" blocks at that yard for the end points they do not serve: Train 1 can give its E block to Train 2, and Train 2 can give its D block to Train 1.

Such block swaps reduce the need to classify cars at Yard C into new blocks, while maximizing service quality to D and E. Note that while this does eliminate the need to do detailed switching of cars at Yard C for the cars traveling in these blocks, it does not eliminate the need to break apart both trains and set-off/pick-up cars at Yard C, which does impact the use of Yard C's capacity and environmental footprint.

Despite Applicants' reliance on block swaps to achieve efficiencies through implementation of PSR operating concepts, no mention is made of any activity measures related to yard switching activity, including intermediate switching, block swaps, or intermodal lifts in Applicants' system model, and nothing indicates that such measures were taken into account in

developing post-merger operating expenses. There is one small entry in the benefits section of the financial model that cites a reduction in "I&I Switching" of a few hundred thousand dollars per year.[79] This unexplained benefit is the only reference I could find to location-based car handling costs.

In sum, while the Application presents a veneer that somewhat resembles the type of operations planning process characteristic of the most recent Class I rail mergers, the processes they describe are, with apologies to Macbeth, "full of sound and fury, signifying nothing." In actuality, Applicants set aside the proven tools and models such as MultiRail in the costing process. Instead, Applicants embarked on a convoluted (and unprecedented) operating plan process that they never fully explain. Then, essentially abandoning their own operating plan, Applicants substituted operating costs derived from a simple, undocumented spreadsheet that accounted for less than half of the GTMs identified in the operating plan process – and used this as the critical driver of their operating and capital cost calculations.[80]

5. Specific Errors in Applicants' Analysis

Applicants' choices concerning traffic data and modeling raise serious issues concerning the credibility of their operating plan and operating metrics. In this section, I describe some of the more serious errors in Applicants' planning process, which are summarized in Exhibit 5-1. Beyond these more serious examples, there are a host of other issues with the operating plan, which are summarized in Section 6.

[79] FD 36500 – Work Paper - STB Rail Road Control Application Model – Final.xlsx, Inputs- Operating Benefits tab.

[80] Application Vol. 1, p. 442, ¶13 states organic growth was excluded from financials, Application Vol 2, p. 286, ¶85 states organic growth was included in the operating plan. *See also* FD 36500 - Work Paper - HC - System Model-Methodology.pdf; FD 36500 - Work Paper - HC - Cost Metrics Growth Model_Base year 2019.xlsx; and FD 36500 – Work Paper – STB Rail Road Application Model – Final.xlsx, Inputs - Revenues + Costs tab.

Exhibit 5-1: Summary of serious errors in Applicants' operating planning process[81]

Section	Description	Discussion
5.1	Traffic density on the main line between Sabula, IA and Airline Junction (Kansas City) is understated by up to 25 percent.	• The Sabula – Airline Junction line is the primary artery in the CP-KCS system and the only line linking the CP and KCS systems. • If Applicants use invalid or understated traffic volume estimates for this line, this in turn invalidates capital expense decisions and environmental assessments for this line. • Given the central role of the line, service issues arising from insufficient investment in capacity based on inaccurate traffic estimates might well spread to other portions of the system, as has occurred in past mergers.
5.2	Northbound intermodal traffic at Lazaro Cardenas is significantly understated in the Base Year, and the understatement carries forward into the Year 3 estimate.	• While the Base Year for the operating plan is 2019, Applicants chose to model carload and intermodal traffic based on traffic in October 2020. The Port of Lazaro Cardenas, however, was effectively closed during October 2020 by a blockade established by striking teachers. • The annualized October 2020 intermodal traffic at Lazaro Cardenas used by the Applicants is less than 10 percent of the actual 2019 traffic it is supposed to represent. This error in Base Year traffic carries forward into Year 3 and materially affects train design to and from the Port.
5.3	The train counts by subdivision are invalid and cannot be relied upon	• Merger regulations require Applicants to report the changes in trains per day on each line segment or subdivision between the pre- and post-merger operating plans – due to a variety of causes the train counts produced by the applicants are invalid and cannot be relied upon • Applicants' train counts are inherently unreliable in light of the numerous errors in the traffic on which Applicants' operating plan is based. • An unknown number of trains were arbitrarily excluded from train counts because they traversed fewer than 25 percent of the nodes on a line segment/subdivision. In all likelihood, this results in Base Year and Year 3 train counts that are understated. • Base Year unit trains were developed using one only month of data (October 2019). Applicants provided no analysis or other evidence to demonstrate that this period is representative of full-year 2019 unit train operations. • There is real potential that some traffic operated in unit trains was excluded from MultiRail and its train counts, but also not accounted for in the one-month snapshot of unit trains used by Applicants. • The trains per day values published in the Application do not match the work papers Applicants identified as being the source of those values.
5.4	The Application provides invalid data on car handling changes at yards and does not report numerous yards with projected growth in activity of more than 20 percent (as required by the Board's merger application	• Merger regulations require Applicants to report any yard at which they project activity will increase by more than 20 percent. This percentage is supposed to be measured between pre-merger operations and the steady-state post-merger case. • Applicants incorrectly use their so-called "Optimized Plan" as the starting point for measuring changes in yard activity, but that is a plan or scenario that can only be implemented beginning after the merger is consummated.

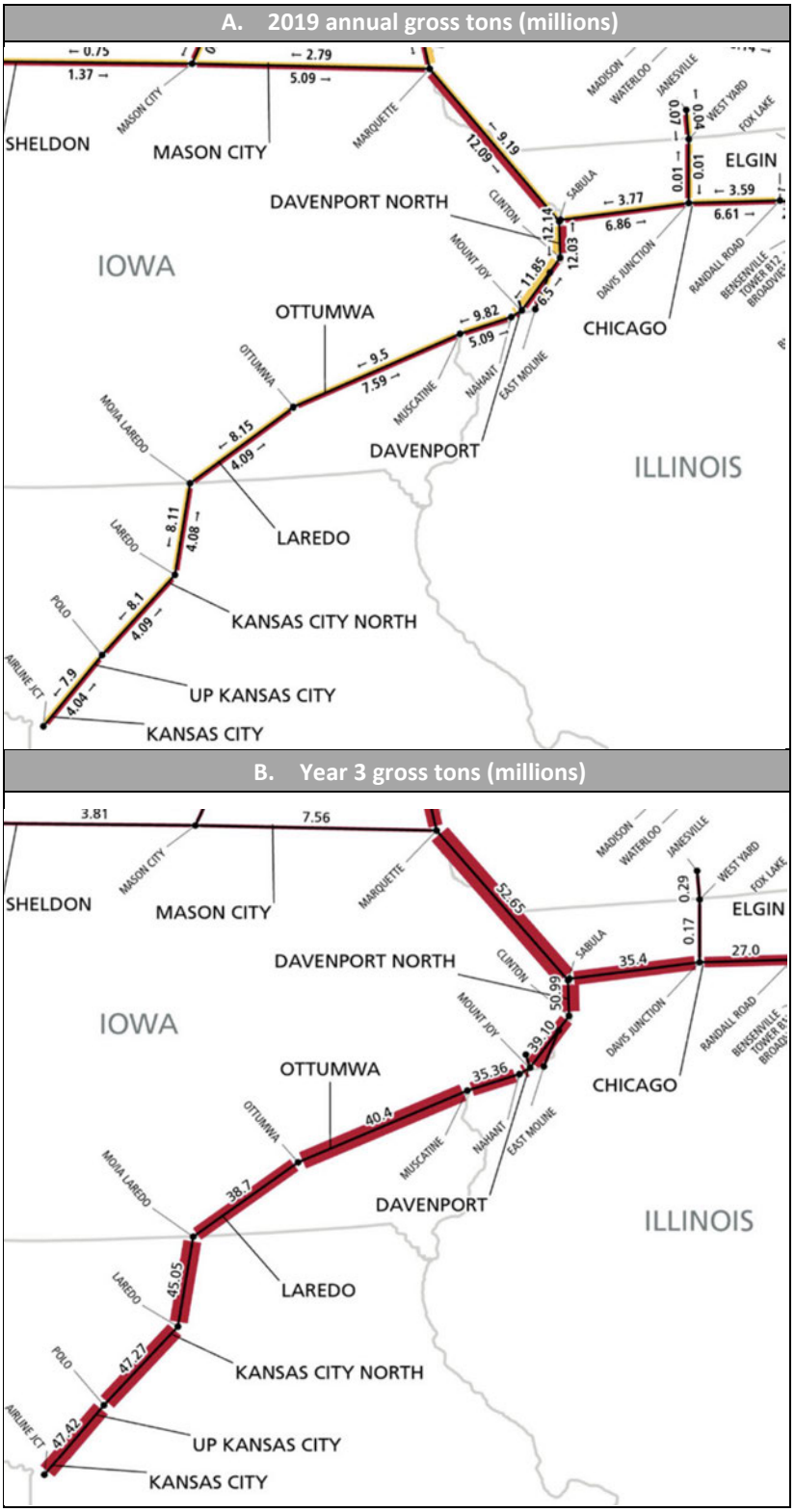
[81] Summary table only: All citations for error descriptions and discussion are provided in subsequent detail sections.

Section	Description	Discussion
	and environmental regulations).	• Applicants fail to include all yards that will experience an increase in activity of more than 20 percent, in part because they failed to include bulk traffic in their statistics. • Given experience in past mergers in which traffic exceeded a yard's capacity and triggered service disruptions, this requirement is an important cross-check of the Applicants' operating and capital plans.
5.5	Originating and terminating traffic estimated in the Application is out of balance at numerous locations.	• One of the primary methods to check the accuracy of a traffic base is to compare originations and terminations at each location, as originations and terminations by location should balance generally. • Numerous locations reported in the Application are out of balance, indicating that there likely are problems with the traffic data. • This in turn has a direct impact on the activity levels reported for yards, and likely has caused distortions in the blocking and train plans.

5.1 Traffic density between Sabula, IA, and Airline Junction, Kansas City

The line between Sabula, IA and Airline Junction near Kansas City is the sole artery that connects the CP and KCS systems and will be the CPKC network's critical north-south route. It is, therefore, essential that the tonnages projected for this line are accurate. Otherwise, Applicants are likely to fail to allocate sufficient capital to maintain capacity and keep this artery fluid. (Accurate tonnage also supports the environmental assessment process.) Exhibit 5-2 shows the tonnages reported in the Application for the Sabula-Airline Junction line, as well as the feeder lines into Sabula from the north. Exhibit 5-3 shows the underlying tonnage figures by line segment.

Exhibit 5-2: Base Year and Year 3 projected traffic for Sabula, IA-Airline Junction, Kansas City[82]



[82] Refer to Exhibit 14 traffic density maps in Volume 2 of Application, pp.508, 510.

Exhibit 5-3: Tonnage by line segment[83]

Line Segment	2019 Tonnage	Year 3 Tonnage	Difference
Nahant – Muscatine	14.91	35.36	20.45
Muscatine – Ottumwa	17.09	40.4	23.31
Ottumwa – MO/IA Laredo (state line)	12.24	38.7	26.46
MO/IA Laredo – Laredo	12.19	45.05	32.86
Laredo – Polo	12.19	47.27	35.08
Polo – Airline Junction	11.94	47.42	35.48

The 2019 tonnage demonstrates that traffic over the line, especially between Ottumwa and Airline Junction, varies very little, indicating that little traffic originates or terminates along this line. Yet, the Applicants project that in Year 3, tonnage on the line will vary widely between segments, from a low of 38.7 million tons to a high of 47.42 million tons (see Exhibit 5-3 above). To understand this anomaly, and to demonstrate that there are no significant new sources of traffic along this line in the Year 3 scenario, I conducted two location-specific analyses.

First, I conducted a manual review of all the diversion traffic identified in Applicants' Diversion Traffic Excel Workbook[84] and classified it either as traversing the line or not traversing the line. Because of the location of this line between the merging railroads, it is generally not affected by reroutes associated with extended hauls – and thus the analysis did not need to broadly consider potential volume adjustments where an extended haul move was already in the base (2019) traffic. "Extended haul" traffic was considered and counted only it if it was new to CP and would (for the first time) move over the Sabula – Airline Jct. line segment.[85] My analysis focused on the Muscatine-Ottumwa segment, with results as shown in Exhibit 5-4.

[83] Based on values from Exhibit 14: Density Charts in Volume 2 of Application, pp.461-504.
[84] *See* FD 35600 - Work Paper - HC - 1.Proposed Final FTI Rail to Rail Diversion Results for Merger Application 10_21_20 Updat_Truk_Rev.xlsx.
[85] *See* HC – Oliver Wyman - Evaluation of Ottumwa Line Segment (Muscatine - Ottumwa) Tonnage – Methodology.pdf for methodology and associated work papers.

Exhibit 5-4: Results of analysis of diverted traffic[86]

Line Segment	Applicants 2019 Tonnage	Applicants Year 3 Tonnage	Estimated Tonnage from Diversion	Organic Growth @{{XXX}}	Revised Estimated Tonnage	Percentage Under - Estimate
Muscatine-Ottumwa	17.09	40.40	{{XXX}}	{{XXX}}	{{XXX}}	{{ }}

The tonnage values for each shipment were directly based on the values Applicants presented in their system model.[87] The stated approach taken by Applicants was to compute tonnages by starting with base 2019 tonnages and then adding new business that is expected to result from the merger, plus an allowance for organic growth (here, Applicants used a {{XXX }} growth factor).[88] *The analysis revealed that the tonnages shown on the maps in the Application are {{XXX }} below the correctly calculated tonnages for this line segment.*[89]

Second, to test the fluctuation in traffic densities on the line segments between Ottumwa and Airline Junction shown in the Application, I loaded the diversion traffic into a version of MultiRail controlled by Oliver Wyman and flowed it across the network to develop the gross tonnage values for each line segment. This exercise both provided a cross-check to my analysis of the traffic on the Muscatine-Ottumwa segment and tested whether any traffic originates/terminates along the line. The result of my analysis, shown in Exhibit 5-5, is largely consistent with my earlier analysis. It demonstrates that, contrary to the data presented in the Application, there are no significant variations in tonnages between the segments.

[86] Applicant's 2019 and Year 3 tonnages are based on values provided in Exhibit 14: Density Charts in Volume 2 of Application, pp. 461-504. *See* HC – Oliver Wyman - Evaluation of Ottumwa Line Segment (Muscatine – Ottumwa) Tonnage - Methodology.pdf for analysis and associated sources to calculate the "Tonnage from Diversion."
[87] *See* FD 36500 – Work Paper – HC – System Model - Methodology.pdf.
[88] *See* FD 36500 - Work Paper - HC - Cost Metrics Growth Model _ Base year 2019.xlsx. (Organic growth is derived from the change in Year 3 and the Base year "Reference tab").
[89] *See* HC – Oliver Wyman - Evaluation of Ottumwa Line Segment (Muscatine - Ottumwa) Tonnage – Methodology.pdf for approach to analysis and how the 25 percent difference is calculated.

Exhibit 5-5: Results of MultiRail analysis of the line between Nahant and Airline Junction[90]

Line Segment	Applicants 2019 Tonnage	Applicants Year 3 Tonnage	Diversion Tonnage from OW MultiRail	Organic Growth @21%	Revised Estimated Tonnage	Estimated Percentage Error
Nahant - Muscatine	14.91	35.36	{{XXX}}	{{XXX}}	{{XXX}}	{{ %}}
Muscatine - Ottumwa	17.09	40.4	{{XXX}}	{{XXX}}	{{XXX}}	{{ }}
Ottumwa – MO/IA Laredo	12.24	38.7	{{XXX}}	{{XXX}}	{{XXX}}	{{ }}
MO/IA Laredo – Laredo	12.19	45.05	{{XXX}}	{{XXX}}	{{XXX}}	{{ }}
Laredo – Polo	12.19	47.27	{{XXX}}	{{XXX}}	{{XXX}}	{{ }}
Polo – Airline Junction	11.94	47.42	{{XXX }}	{{XXX}}	{{XXX}}	{{ }}

5.2 Base Year intermodal traffic at Lazaro Cardenas is understated

Exhibit 5-6 compares actual intermodal traffic during the full year 2019 with the 2019 Base Year intermodal traffic for Lazaro Cardenas that Applicants projected by annualizing traffic from the single month of October 2020.

Exhibit 5-6: Comparison of annualized intermodal units[91]

	From Lazaro Cardenas		To Lazaro Cardenas	
Annualized from	Loads	Empties	Loads	Empties
2019 Full Year Waybills	{{XXX}}	{{XXX}}	{{XXX}}	{{XXX}}
October 2020 Waybills	{{XXX}}	{{XXX}}	{{XXX}}	{{XXX}}

Exhibit 5-6 clearly illustrates the impact of Applicants' decision to rely entirely on October 2020 traffic data to create the Base Year operating plan for carload and intermodal traffic. The number of originating loaded containers in the annualized October 2020 data is less than 10 percent of the number of loaded containers in the actual 2019 full year data. This discrepancy is attributable largely to the fact that the Port experienced a blockade by striking teachers during

[90] Applicant's 2019 Tonnage and Year 3 Tonnage are based on values from Exhibit 14: Density Charts in Volume 2 of Application, pp. 461-504. Organic growth tonnage is calculated from multiplying the 2019 tonnage by 21 percent. *See* HC – Oliver Wyman - MultiRail Corridor Volume, Tonnage and Length Estimates for Diversion Traffic Methodology.pdf for how the "Diversion Tonnage" is obtained from MultiRail and associated outputs.

[91] *See* HC – Oliver Wyman - Comparison of Intermodal Traffic at Lazaro Cardenas between Oct 2020 and FTI 2019 Data – Methodology.pdf for associated analysis and sources.

October 2020.[92] (It is not clear whether Applicants were aware of that fact in selecting October 2020 as the sole source of carload and intermodal traffic for their Base Year MultiRail model.)

While most of the originating container traffic in the base period is local to Mexico, these missing container volumes must have had a material effect on the train design out of Lazaro Cardenas. The 2019 full year waybills equate to more than 10,000 feet of intermodal cars northbound per day, while the annualized October 2020 waybills generate less than 500 feet of intermodal cars northbound per day.[93] As a cross-check, I reviewed the number of cars originating/terminating in the base period at Lazaro Cardenas in the report contained in Volume 2, Appendix B of the Application,[94] and found the stated values to be consistent with the above finding. Moreover, the Applicants carried the erroneous estimate of Base Year traffic at Lazaro Cardenas forward into Year 3, likely distorting the Year 3 operating plan as well.

5.3 Application train counts are not reliable

The train counts by line (a specific filing requirement),[95] as published in the Application, are inaccurate due to the use of non-representative unit train data for the base period, intentional exclusion of other trains,[96] errors in how the operating plan was developed, and inconsistencies between the work papers and the values published in the Application.

Nothing in the regulations permits Applicants exclude from their operating plan (and environmental submission) selected trains that "only" touch a subset of the locations in a

[92] "Rail blockade ends in Mexico after 60 days of protests," Freight Waves, December 2, 2020.
[93] Uses CP standards for intermodal cars so formula is [Annual Containers]/[365 Days]/[4.7 Containers/Car]*[165 Feet/Car]. See HC – Oliver Wyman - Intermodal to Railcar Conversion Factor Source Compilation.pdf for sources.
[94] Application, Vol. 2, Appendix B: Change in Yard Volumes, p. 389 for Lazaro Cardenas has 8.4 originating cars per day; multiplying the figure by 4.7 * 365 yields 14,410 originating containers. See HC-Oliver Wyman - Intermodal to Railcar Conversion Factor Source Compilation.pdf for sources.
[95] CFR 49 Part 1111.8 (a)(1).
[96] FD 36500 – Work Paper – HC Trains Per Day - Methodology.pdf, p. 2.

division.[97] Yet, as discussed above, CP arbitrarily decided to remove from the train list generated by MultiRail any train that did not traverse at least 25% of the stations on any subdivision on which it operated. Combined with the known errors in the traffic included in Applicants' MultiRail modeling, it is virtually certain that the train counts in the Application are wrong.

In addition, *the train counts in the Application are inconsistent with the work papers cited by Applicants as being the source of those train counts*. In response to CN discovery request #115, Applicants stated that the FD 36500 – Work Paper – HC - Trains Per Day - Methodology.pdf is the file that explains how the trains per day shown in the Application were calculated and produced.[98] However, none of the corresponding Excel files cited in that methodology have figures that match the trains per day in the Application.

The only file where the identified level of trains per day even comes close is "FD 36500 – Work Paper – HC- Trains per Day and Gross Ton Miles – Working Copy with Haz Breakdown.xlxs," which provides a summary view of the trains per day by subdivision/segment (hereafter, the "Trains-per-Day Model").

The Trains-per-Day Model shows how trains were calculated/derived by providing data on Base Year non-unit and unit trains, growth year non-unit trains, unit train organic growth, and unit train synergy growth. (It is implied that the growth year non-unit train count includes both organic and synergy growth.) The materials indicate that:

- Non-unit train counts in the Trains-Per-Day Model were sourced from MultiRail, from which trains that traversed less than 25 percent of the MultiRail nodes in a subdivision were arbitrarily removed.[99]

[97] Applicants note in FD 36500 – Work Paper – HC – Trains Per Day - Methodology.pdf that "The train must pass by at least 25% of the subdivision's segment stations in order to be counted on it."
[98] FD 36500 – Work Paper – HC- Trains per Day.pdf; Application Volume 2, Appendix A. Trains per Day by Subdivision Review.
[99] *See* FD 36500 – Work Paper – HC – Trains Per Day - Methodology

- The Base Year unit trains were sourced from a set of operational snapshots that appear to be a one-month sample of unit trains operated during October 2019. Nothing in the Application or workpapers shows that these trains are representative of full year 2019 operations.[100]
- The organic growth in unit trains is a simple multiplier applied to the Base Year unit trains without regard to specific commodities.[101]
- The synergy growth in unit trains is based on a manual spreadsheet analysis of new unit trains to be operated based on the traffic diversion analysis (including traffic provided by witnesses Wahba and Naatz).[102]

Exhibit 5-7 demonstrates the discrepancies between the trains per day listed in the Application and the Trains-per-Day Model.

Exhibit 5-7: Trains per day from Application and Trains-per-Day Model[103]

Subdivision	Application[104]		Trains-Per-Day Model Values[105]		Difference	
	Current Trains/Day Base	Future Trains/Day Year 3	Current Trains/Day Base	Future Trains/Day Year 3	Base Period	Year 3
Ottumwa	4.2	18.4	{{XXX}}	{{XXX}}	{{XXX}}	{{XXX}}
Laredo CP	3.0	17.0	{{XXX}}	{{XXX}}	{{XXX}}	{{XXX}}
Kansas City	2.9	16.9	{{XXX}}	{{XXX}}	{{XXX}}	{{XXX}}
Shreveport	9.4	23.6	{{XXX}}	{{XXX}}	{{XXX}}	{{XXX}}
Greenville	5.5	7.0	{{XXX}}	{{XXX}}	{{XXX}}	{{XXX}}
Rosenberg[106]	8.5	17.7	{{XXX}}	{{XXX}}	{{XXX}}	{{XXX}}
Laredo KCS	10.5	19.4	{{XXX}}	{{XXX}}	{{XXX}}	{{XXX}}

[100] Based on FD 36500 – Work Paper – HC – 2019_Consolidated_Data_Master.txt.
[101] An organic growth rate of {{XXX}}% and {{XXX}}% is used for Year 3 and Year 5 for bulk traffic respectively. *See* HC – Oliver Wyman - Review of Growth Factors in CPKC Application.pdf.
[102] FD 36500 - Work Paper - HC - New Bulk Input w Year Splits 2021.10.20.xlsx, FD 36500 - Work Paper - HC - Summary of Volume Growth (Units) through Year 5 v4.xlsx.
[103] FD 36500 – Work Paper – HC- Trains per Day, Gross Ton Miles – Working Copy with Haz Breakdown; Application Vol. 2, Appendix A. Trains Per Day, pp. 364-368; and HC - Oliver Wyman - Train Counts Methodology.pdf
[104] Application Vol. 2, Appendix A. Trains Per Day by Subdivision, pp. 364-368.
[105] The highest number of trains per day by subdivision/segment are presented in the above table, data based on FD 36500 – Work Paper – HC- Trains per Day, Gross Ton Miles – Working Copy with Haz Breakdown.
[106] The trains per day listed in the filing for the Rosenberg subdivision match the trains per day summarized in the Excel file that is utilized for this analysis. It is the only subdivision from the list in the table above where both sources have trains per day that match.

Subdivision	Application[104]		Trains-Per-Day Model Values[105]		Difference	
	Current Trains/Day Base	Future Trains/Day Year 3	Current Trains/Day Base	Future Trains/Day Year 3	Base Period	Year 3
Saltillo	24.1	29.8	{{XXX}}	{{XXX}}	{{XXX}}	{{XXX}}
Caltzontzin	3.6	7.3	{{XXX}}	{{XXX}}	{{XXX}}	{{XXX}}

5.3.1 Non-Representative Unit Trains

The use of a non-representative set of unit trains for the Base Year plan, the application of global scaling factors for unit trains to estimate organic growth, and the potential that some traffic was not represented in either the bulk plan or carload plan raises further questions about the reliability of Applicants' train counts.

As an initial matter, *there is no bulk train operating plan provided at all in the Application*. Historic or "base" bulk trains are not identified at all – they are simply a statistical representation of line activities derived from a "snapshot," which appears to be from October 2019 for CP and from a 30-day sample for KCS with no specified time period.[107] Nothing demonstrates that these one-month snapshots are representative of full-year 2019 traffic patterns. The projected organic growth in these "bulk" trains is based on system average growth factors[108] that do not in any way tie back to Applicants' traffic studies.

The specific methodology Applicants used to calculate unit trains appears to be as follows:

- An operations monitoring type system was used to identify all unit trains that were operated by CP and KCS/KCSM during a one-month period. The route and consist (weight, length) of each was obtained, along with the train type.[109]

[107] FD 36500 - Work Paper - HC - CP Bulk Cars Per Day By Sub.xlsx; FD 36500 - Work Paper - HC - KCS KCSM Bulk Train Cars Per Day by Subdivision.xlsx.
[108] *See* HC – Oliver Wyman - Review of Growth Factors in CPKC Application.pdf for organic growth percentages used by CPKC.
[109] *See* FD 36500 – Work Paper – HC – Trains Per Day - Methodology.pdf and associated work papers: FD 36500 - Work Paper - HC - CP Bulk Cars Per Day By Sub.xlsx and FD 36500 - Work Paper - HC - KCS KCSM Bulk Train Cars Per Day by Subdivision.xlsx.

- Based on the routing of each observed unit train, the subdivisions each train traversed were identified, and the total train count and tons were tallied by subdivision. If a train had a hazardous materials designation (primarily crude oil and ethanol trains), then the traffic also was added to a hazardous materials car count.
- The resulting values by subdivision were divided by days in the time period covered by the sample (one month) and treated as the Base Year values for the operating plan.
- A global growth factor was applied to the unit train counts by subdivision to obtain organic growth in these trains. The same organic growth values of {{XXX}} percent for Year 3 and {{XXX}} percent for Year 5 were applied across all subdivisions, without consideration of the railroad, the commodity involved or the origin/destination of the traffic.[110]
- All of the "synergy" traffic was combined into nine (supposedly) representative train pairs.[111] The frequency of each train pair was set based on a target train size and forecasted diversion volume. The routings of these trains were then used to compute the additional train counts and tonnage associated with "synergy" traffic.
- Some final adjustments were made to "calibrate" these values. While no explanation of the reason for such "calibration" is set forth in the Application, it appears that this step was undertaken to make the overall values appear consistent with a simplistic spreadsheet model which the Applicants called the "System Model."[112]

If the train pairs used by Applicants are truly representative of the origins and destinations of new post-merger grain unit train movements, then I accept that the non-organic growth bulk trains for the post-merger scenario are likely accurate. But I question the accuracy of the Base Year unit train counts and organic growth unit train counts.

[110] *See* HC – Oliver Wyman - Review of Growth Factors in CPKC Application.pdf for organic growth percentages used by CPKC.
[111] FD 36500 - Work Paper - HC - Trains Per Day and Gross Ton Miles - 2021.10.22 - Working Copy with Haz Breakdown.xlsx, Bulk Reference tab, shows nine new train pairs for loaded and empty traffic in the "Train Symbol" column.
[112] FD 36500 – Work Paper – HC- Cost Metrics Growth Model Base year 2019.xlxs.

To determine whether the snapshot of unit trains is indeed representative, I examined the differences between the number of loads handled by KCS/KCSM for full-year 2019 versus October 2019 for selected commodities that move in unit trains.[113] Since I could not directly identify which moves were unit train moves from the data provided, I instead looked at volumes for grain, crude oil, and coal, assuming that differences in the volumes of these commodities between the full year and October 2019 would be consistent with differences in the number of unit trains operated. Among the findings from this analysis are the following:

Almost no crude oil traffic moved from Alberta to Texas or Louisiana during the month of October 2019. While {{XXX}} loaded cars were moved during all of 2019 (equivalent to {{XXX}} cars per month, or about {{XXX}} trains per month accounting for returning empty trains), I only found {{XXX}} such loaded car moves in October 2019.[114] To confirm this finding, I examined the number of crude oil trains Applicants identified in their October 2019 snapshot as transiting the Ottumwa to Laredo, MO segment of the line from Sabula to Airline Junction. All the crude oil traffic from Alberta would necessarily have to transit this line segment. What I found is a total of two trains, one southbound and one northbound – consistent with the low volumes that I identified.[115] Essentially, the Application is understating this very important element of the base CPKC operating plan by 85 percent in terms of train count ({{XXX}} versus {{XXX}} oil trains), and 92% in terms of cars ({{XXX}} versus {{XXX}} cars).

[113] *See* HC – Oliver Wyman - Evaluation of Bulk Traffic – Coal, Crude, and Grain Methodology.pdf for associated data and analysis.
[114] *See* HC – Oliver Wyman - Evaluation of Bulk Traffic – Coal, Crude, and Grain Methodology.pdf for associated data and analysis. A standard 115 cars per train conversion is used for crude oil, based on FD 36500 - Work Paper - HC - New Bulk Input w Year Splits 2021.10.20.
[115] FD 36500 - Work Paper - HC - CP Bulk Cars Per Day By Sub.xlsx.

To compound these errors, it appears that Applicants failed to capture this information properly in their analysis of line densities. In the same analysis in which I identified two crude oil trains transiting the Ottumwa-Laredo segment,[116] I found a total of {{XXX}} other unit trains also on the line in October 2019,[117] which translates to {{XXX}} unit trains per day on average.

Exhibit 5-8 shows the bulk train counts that Applicants used for part of the Sabula to Airline Junction line density analysis. Not only is the number of bulk trains understated on the Ottumwa to Laredo segment (it should be {{XXX}}, not {{XXX}}), all unit trains completely disappear on the segment between Clinton and Water Works. These findings indicate that the October 2019 "snapshot" of unit trains is not representative of full-year operations, and that errors in the recording of unit train counts mean that these counts cannot be relied upon.

Exhibit 5-8: Sabula, IA-Laredo, MO line segments: Application unit-train counts[118]

Line Segment	Base (2019) Unit Trains/Day
SABULA,IA - CLINTON,IA	{{XXX}}
CLINTON,IA - WATER WORKS,IA	{{XXX}}
WATER WORKS,IA - NAHANT,IA	{{XXX}}
NAHANT,IA - MUSCATINE,IA	{{XXX}}
MUSCATINE,IA - OTTUMWA,IA	{{XXX}}
OTTUMWA,IA - MO/IA LAREDO,MO	{{XXX}}
MO/IA LAREDO,MO - LAREDO,MO	{{XXX}}

Turning to organic growth of unit trains, a single, systemwide organic growth factor was applied to the base period unit train counts by line segment.[119] We know from history that different lines of business, such as coal and grain traffic, can have very different organic growth

[116] FD 36500 - Work Paper - HC - CP Bulk Cars Per Day By Sub, Crude tab, filtered for "Ottumwa" as Location.
[117] Based on review of FD 36500 - Work Paper - HC - CP Bulk Cars Per Day By Sub for all train types on Ottumwa division.
[118] FD 36500 – Work Paper – HC – Trains Per Day, Gross Ton Miles - Working Copy with Haz Breakdown .xlsx.
[119] *See* HC – Oliver Wyman - Review of Growth Factors in CPKC Application.pdf for organic growth percentages used by CPKC.

rates (for example, for coal in the current "anti-fossil fuel" regulatory environment).[120] Lane and geographic-based differences may also factor into growth rates. The use of undifferentiated global adjustment factors by the Applicants for organic growth completely ignores this issue.

Applicants developed an operating plan in MultiRail only for non-unit train operations. But, neither the Application or the workpapers explain how Applicants determined which Base Year traffic was "unit train" traffic and excluded from MultiRail. It is quite likely that there are gaps where some traffic excluded from MultiRail also was not captured in unit train counts.

It is also possible that some unit trains were not included in the "snapshot" of one month of data, as only specific train types were counted. Other unit trains would have been operated during the time period, such as military trains, trackage rights/haulage trains, rock/aggregate trains, etc. It is not clear if the traffic moving in these trains was included in the MultiRail Base Year operating plan, unit plan, or neither.

While nine train pairs were developed to account for new unit train traffic,[121] these trains are not documented in the formal Application, despite their significant volumes – particularly between Alberta and Texas for crude oil (approaching two trains/day in each direction), and between various points in Canada, the United States, and Mexico for grain. Given the significant percentage of CPKC trains that are "unscheduled" unit trains, Applicants' failure to describe these trains leaves a significant gap in their description of expected operations.

[120] Growth rates differed across commodities from 2015 to 2020, e.g., the amount of coal originated in the US by Class I railroads dropped by 45 percent, while grain loadings increased by 6 percent over the same period. *See* Growth Commodity Growth Rates 2015 - 2020 from AAR Class I Railroads Analysis.xlsx.

[121] FD 36500 - Work Paper - HC - Trains Per Day and Gross Ton Miles - 2021.10.22 - Working Copy with Haz Breakdown.xlsx, Bulk Reference tab, shows nine new train pairs for loaded and empty traffic in the "Train Symbol" column.

5.3.2 Conclusions

The train counts in the Application and in the Environmental Train Count Table[122] should not be relied upon for the following reasons:

- Applicants' train counts are inherently unreliable in light of the numerous errors in the traffic on which Applicants' operating plan is based. An unknown number of trains were arbitrarily excluded from train counts because they traversed fewer than 25 percent of the nodes on a line segment/subdivision. This results in Base Year and Year 3 train counts that are understated.
- Base Year unit trains were developed using one only month of data (October 2019). Applicants provided no analysis or other evidence to demonstrate that this period is representative of full-year 2019 unit train operations. Based on the clear distortions in the traffic data used for the operating plan, there is every reason to believe that similar distortions exist in the unit train counts.
- There is real potential that some traffic operated in unit trains was excluded from MultiRail and its train counts, but also not accounted for in the one-month snapshot of unit trains used by Applicants. The result would be that some of the traffic was not counted in Applicants' disconnected unit train planning process, causing distortions in unit train counts.
- To the extent that the number of unit trains is understated, investments required to increase line-of-road and yard capacity may be understated, jeopardizing Applicants' ability to provide the efficient single-line service levels needed to attract projected Year 3 traffic growth.
- The trains per day values published in the Application do not match the work papers Applicants identified as being the source of those values.

[122] Based on file submitted to the Board by Venable LLP and CP under Comment ID "31353" (31353.pdf), which contains master segment and yard tables, with information on environmental trains per day.

5.4 The Application fails to meet the requirement to identify all yards projected to experience more than a 20 percent increase in activity

The merger regulations require Applicants to identify any yard that will experience an increase in activity of 20 percent or more.[123] This information is important because, among other factors, it serves as a check to ensure that the capital expenditure plan considers situations in which added traffic will push yards to (or beyond) their practical capacity. In past mergers, an increase in traffic beyond a yard's practical capacity resulted in service failures that spread across the network.

My review of the Application and workpapers found that dozens of yards should have been reported were omitted from the Application. Some of these yards were small, so that even a small increase in traffic might generate a 20 percent increase in activity. Exhibit 5-9 focuses on the six largest yards with a projected increase in activity of greater than 20 percent that were not addressed in the Application. As Exhibit 5-9 indicates, the increase at several of the yards is quite substantial and may well exceed their current practical capacity. Some of these yards, such as Port Arthur, Hardisty, and Bruderheim, were not listed because Applicants failed to include unit traffic in their activity counts in the filing.

Exhibit 5-9: Six yards with a change of activity > 20 percent omitted from the Application[124]

Yard	Processed Cars Base	Processed Cars Year 3	Change	% Change
Port Arthur	{{XXX}}	{{XXX}}	{{XXX}}	85%
Hardisty	{{XXX}}	{{XXX}}	{{XXX}}	286%
Bruderheim	{{XXX}}	{{XXX}}	{{XXX}}	557%
Agincourt	{{XXX}}	{{XXX}}	{{XXX}}	41%
Jesus Maria	{{XXX}}	{{XXX}}	{{XXX}}	28%
Det Con Term	{{XXX}}	{{XXX}}	{{XXX}}	88%

[123] 49 CFR Part 1111.8(a)(1)(2000).
[124] *See* HC - Oliver Wyman - Yard Projections Methodology.pdf.

The Board's regulations require that Applicants compare pre-merger yard activity with post-merger yard volumes once the merged system has reached a steady state.[125] Applicants failed to satisfy this requirement, because they used the "Optimized Base Year" scenario (rather than the true Base Year) for pre-merger values. The Optimized Base scenario reflects the efficiencies CPKC hopes to achieve using precision scheduled railroading principles *after* the merger is consummated. As a result, the "Optimized Base Year" figures presented by Applicants do not actually reflect the pre-merger situation but instead represent a hypothetical intermediate stage between "Day 1" and Year 3 post-merger.

5.5 Originating and terminating railcar volumes are out of balance at many of the locations shown in the Application

One indicator of potentially inaccurate traffic data is the balance between originating and terminating cars by location. With few exceptions, the long-term trend should be for locations to be balanced in terms of originating versus terminating car counts. There may be some differences at interchanges due to directional agreements between a set of locations, but even these often trend toward statistical balance over longer periods of time. As a result, a clear lack of balance is often indicative of either the use of non-representative traffic or errors in deciphering (and correcting as necessary) the locations found in waybills. Such errors in the traffic data flow directly through to the activity counts for yards.

I examined the Base Year originating and terminating cars by location in Applicants' MultiRail yard volume comparison report.[126] While this report does not include unit train traffic, it provides a reasonable comparison of the originating and terminating volumes used by

[125] CFR Part 1111.8(a).
[126] Application Vol. 2, Appendix B Change in Yard Volumes Overall, pp. 369-403.

Applicants in creating their carload and intermodal operating plans. The results of my review are shown in Exhibit 5-10.

Exhibit 5-10: Originating and terminating cars/day for CPKC base period[127]

Location	Originating	Terminating	Balance	% Imbalance
Baton Rouge	47	93.6	46.6	33%
Detroit	71.2	138.5	67.3	32%
Heavener	11.5	32.3	20.8	47%
Lecheria	16.2	107.6	91.4	74%
Salinas Vic	96.3	74.9	-21.4	-13%
Shreveport	70.8	45.9	-24.9	-21%
St Paul	197.5	138.1	-59.4	-18%
Corpus Christi	95.6	166.5	70.9	27%
Robstown	159.3	49.7	-109.6	-52%
Total	**254.9**	**216.2**	**-38.7**	**-8%**
Intl Freight Gateway	31	16.1	-14.9	-32%
Kansas City	274.2	179.7	-94.5	-21%
Total	**305.2**	**195.8**	**-109.4**	**-22%**
Laredo	585.4	476.9	-108.5	-10%
Nuevo Laredo	4.5	101.2	96.7	91%
Total	**589.9**	**578.1**	**-11.8**	**-1%**
Bensenville	380.3	10.7	-369.6	-95%
Calumet	6	175	169	93%
Chicago Clearing	407.8	283.5	-124.3	-18%
Gibson	70.6	105.5	34.9	20%
Total	**864.7**	**574.7**	**-290**	**-20%**

- The first set of yards, Baton Rouge through St. Paul, reflect various levels of imbalance, which may well be indicative of issues with the underlying source data used by Applicants in MultiRail.
- Corpus Christie and Robstown are both interchanges with BNSF; while still out of balance when paired, at least the balance improves.
- International Freight Gateway and Kansas City show significant imbalances that, like the first set of yards, likely point to issues with the underlying data/limited time period used to develop the MultiRail traffic data.

[127] Application Vol. 2, Appendix B Change in Yard Volumes Overall, pp. 369-403. *See* Oliver Wyman - Rail Car Volumes methodology.pdf.

- Laredo and Nuevo Laredo point to (i) a likely failure in processing the traffic data to correct for how cross-border traffic is reported by KCS and KCSM, and (ii) some rebilling of traffic at the border. It is my understanding that very little traffic actually originates or terminates at Nuevo Laredo, so this is likely an error and most of the Nuevo Laredo traffic should have been remapped to Laredo. How this affected the representation of cross-border blocking and train operations is unclear – but it certainly caused an understatement of the switching activity at Laredo Yard (and a corresponding overstatement at Nuevo Laredo).
- Chicago also exhibits a significant amount of imbalance in its volumes, even when combining the most obvious locations that could have imbalanced interchanges. These differences raise significant doubts about the yard activity counts for Chicago and how representative Applicants' operating plan is for both the pre- and post-merger scenarios.

Once these imbalance issues are corrected using more representative traffic data or correction of waybill location mapping issues, the volumes at the locations as reported by the Applicants are likely to change, potentially changing the assessment of how the merger will affect yard operations.

6. Other Issues That Undermine the Validity of the Application

Other issues were found within the Application and associated work papers that call into question the validity of the operating plan, as shown in Exhibit 6-1. I conducted additional analysis of several of these issues. This section provides a summary of these additional issues, with further analysis added where appropriate.

Exhibit 6-1: Summary of additional issues related to the Application

Section	Description	Summary
6.1	Additional examples of bad line densities	Additional bad line densities were determined through the analysis of line density values (see subsection for details).

Section	Description	Summary
6.2	Critique of NS/CSX haulage/trackage rights volumes	No clear assessment of the volumes using the NS and CSX agreements for the movement of traffic from Chicago to Michigan and Buffalo was provided by Applicants. An assessment of these volumes was undertaken, which found that insufficient capacity exists to serve the Detroit intermodal market, and there will likely be periodic delays for cars waiting for space on CPKC capacity-controlled trains on NS. Depending on train length limits on CSX, there may also be issues to/from Eastern Canada during peak periods.
6.3	Review of carload volumes	There are several issues with carload volumes that undermine the validity of the operating plan (see subsection for details)

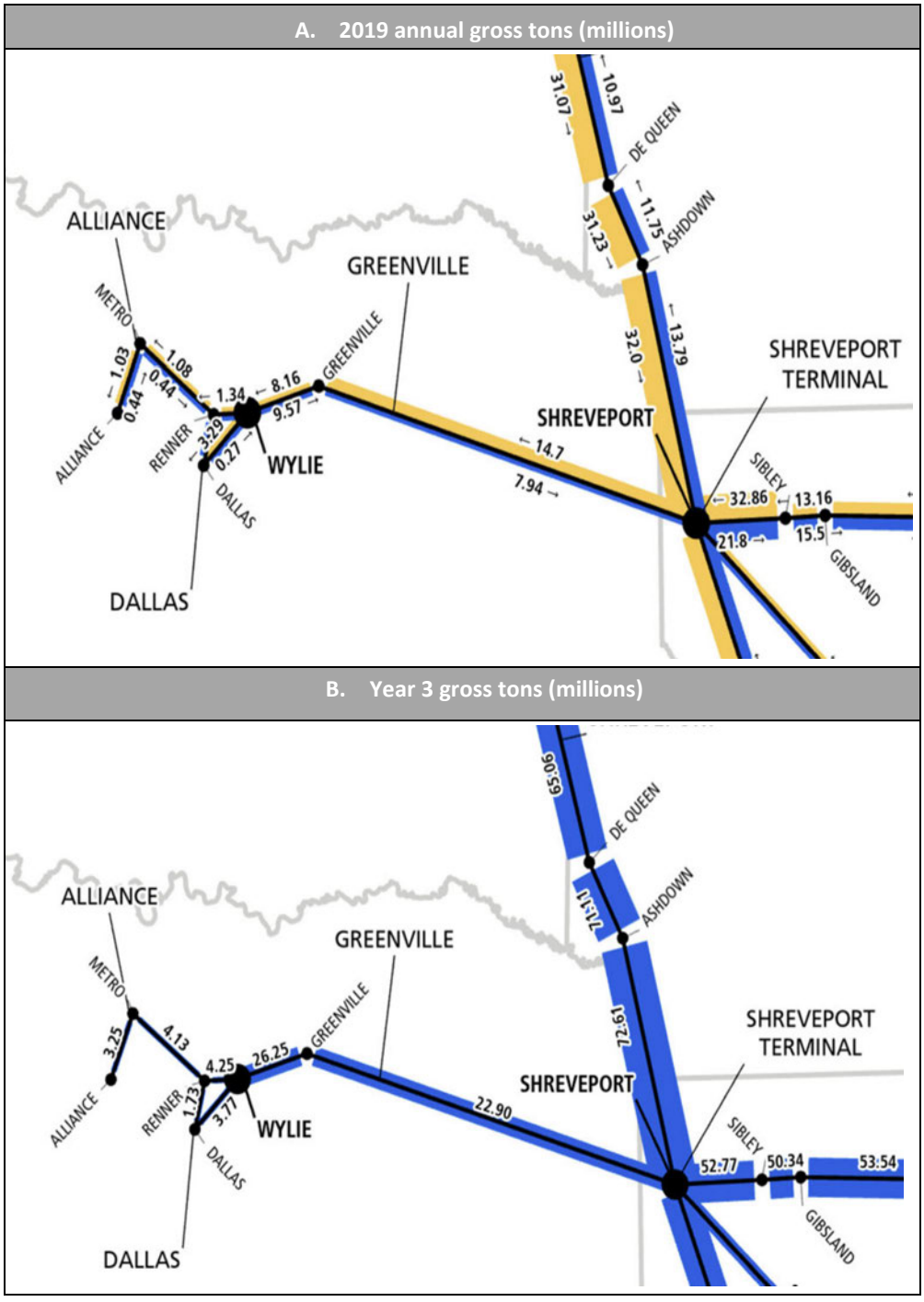
6.1 Detailed review of tonnages for additional line segments

Analyses are presented for the tonnages shown for the Shreveport-Wylie line and the main lines on KCSM. Both provide additional evidence that the tonnages on the line segments in the Application are incorrect.

6.1.1 Shreveport-Wylie

Density maps for Shreveport-Wylie are shown in Exhibit 6-2. I also performed a MultiRail analysis of tonnage on this line segment; the results are shown in Exhibit 6-3.

Exhibit 6-2: Shreveport-Wylie density maps[128]



[128] *See* Application Vol. 2, Exhibit 14 traffic density maps, pp. 512-513.

Exhibit 6-3: Shreveport-Wylie tonnage analysis[129]

Line Segment	Applicants 2019 Tonnage	Applicants Year 3 Tonnage	Estimated MultiRail Year 3 Tonnage From Diversion	Organic Growth @{{XXX}}%	Revised MultiRail Year 3 Estimated Tonnage	Percent Error
Shreveport – Greenville	22.64	22.9	{{XXX}}	{{XXX}}	{{XXX}}	{{XXX%}}
Greenville – Wylie	17.73	26.25	{{XXX}}	{{XXX}}	{{XXX}}	{{XXX%}}

The change of density at Greenville, from the location being a net terminator of traffic to a net originator of traffic, is significant. In 2019, for movement from Shreveport to Wylie, the tonnage drops at Greenville by 4.9 million gross tons ("MGT") in the westbound direction, but in Year 3 there is an increase of 3.4 MGT in the westbound direction. There is no evidence explaining why Greenville becomes a major generator of traffic in Year 3, particularly in the westbound direction. While Applicants' operating plan describes "large increases in IM volumes at Wylie,"[130] there is essentially no change in the tonnage over the entire Shreveport-Greenville segment between 2019 and Year 3. This inconsistency strongly suggests that the tonnage numbers developed by the Applicants are unreliable.

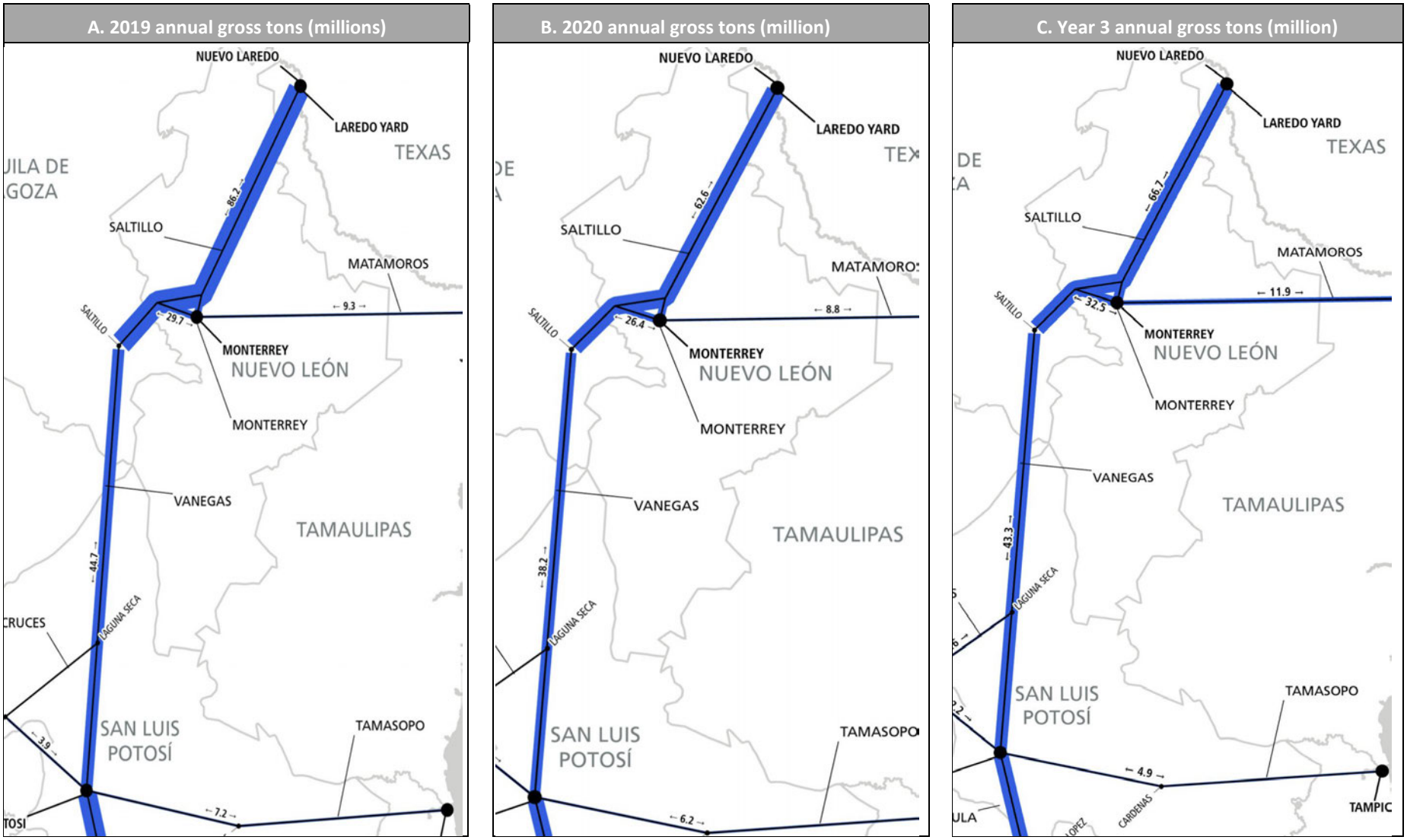
6.1.2 The post-merger traffic density of the KCSM main line is understated

Exhibit 6-4 shows the density charts in the Application for the Saltillo and Venegas divisions of KCSM. These are the northernmost divisions on the critical KCSM main line between Mexico City and the international crossing at Laredo. The Board's merger regulations specifically require that accurate density charts for main lines and secondary rail lines be

[129] Based on values from Application Vol. 2, Exhibit 14: Density Charts, pp. 461-504, and diversion traffic estimates from MultiRail (*see* HC – Oliver Wyman - MultiRail Corridor Volume, Tonnage and Length Estimates for Diversion Traffic Methodology for associated data and outputs).
[130] Based on Application Vol. 2, Table 10, "Intermodal Terminals have Adequate Capacity for Increased Handlings," p. 345.

included in the Application. Exhibit 6-5 lists the tonnages for these two divisions as reported by Applicants.

Exhibit 6-4: Density charts for the Saltillo and Venegas Divisions[131]



[131] Refer to Exhibit 14 traffic density maps in Volume 2 of Application, pp. 514-516.

Exhibit 6-5: Tonnage on the Saltillo and Vanegas Divisions[132]

Subdivision	2019 Tonnage	2020 Tonnage	Year 3 Tonnage	Difference 2019 – Year 3	Difference 2020 – Year 3
Saltillo	86.2	62.6	66.6	-19.6	4.0
Vanegas	44.7	38.2	43.3	-1.4	5.1

As Exhibit 6-5 shows, Applicants' operating plan assumes that traffic on the KCSM main line declined between 2019 and 2020, and that the tonnage will not recover by Year 3. This cannot be correct. It is my understanding that 2019 tonnage reflects official KCSM historic volumes, whereas 2020 tonnage and Year 3 tonnage reflect values computed by Applicants using a complex and error-prone estimation process.[133] These values would have been directly affected by the incorrect intermodal volumes at Lazaro Cardenas that resulted from Applicants' reliance on the single month of October 2020 traffic to estimate full-year values.[134]

The traffic density data detailed in Exhibit 6-5 demonstrates how incorrect inputs and erroneous methodologies at one stage of the operations planning process (e.g., traffic inputs and tonnage estimation) will invalidate the output of later stages (e.g., line segment traffic density calculations). This is not a trivial matter. As with the underestimate of density on the Sabula to Airline Junction segment, underestimated traffic continues through the planning process and becomes an incorrect input to the operating plan and capital expense plan. This can result in a distorted train and blocking plan, as well as an inadequate capital budget to make the investments in capacity required to keep this critical link in the KCSM network fluid.

[132] Based on values from Exhibit 14: Density Charts in Volume 2 of Application, pp. 502-504.
[133] FD 36500 - Work Paper - HC - Trains Per Day and Gross Ton Miles - 2021.10.22 - Working Copy with Haz Breakdown.xlsx.
[134] dwnld_Traffic_KCS.csv provided as part of the accompanying attachments to Traffic File - Methodology.pdf indicate the traffic data used was from October 2020.

Applicants' workpapers show that some of the original KCSM values for 2019 were in metric tons, which according to the methodology were incorrectly converted to imperial tons (also known as long tons), instead of being converted to short tons.[135] Correcting that error would make 2019 tonnage figures even higher. And it is insufficient to explain the scale of the differences between the various values for the given years in Exhibit 6-5.

6.2 The Applicants' operating plan may violate the constraints of the Michigan and Eastern Canada CSX and NS trackage/haulage rights

CP's existing agreements with NS and CSX impose limitations on the amount of traffic that CP can move beyond Chicago to Detroit and Eastern Canada. Applicants' operating plan does not appear to acknowledge the significant limitations on CP's current rights under those agreements. In the case of NS, CPKC is limited to two trains in each direction per day, with a maximum length of 12,000 feet, and a prohibition against the movement of automotive traffic (finished vehicles and parts) and of intermodal traffic not from legacy CP terminals.[136] In the case of CSX, which CPKC uses to get intermodal traffic to the Detroit area and Eastern Canada, CPKC is (and will continue to be) limited to a maximum of 2,500 feet to/from Detroit, and one train pair per day between Chicago and Buffalo/Toronto.[137] Furthermore, Applicant has indicated that {XXX}.[138]

Applicants are aware of this limitation, and cited the CSX limitation as affecting their diversion studies:

> "As a result of the service design analysis, certain capacity restraints were identified for intermodal shipments into and out of CP's Detroit intermodal terminal accessed via

[135] FD 36500 – Work Paper – HC – Methodology for Creating KCSM 2019 Density Chart and Map.pdf; FD 36500 - Work Paper - HC - KCSM 2019 density.xlsx.
[136] Application, Vol. 2, p. 272. See also Canadian Pacific Railway Limited, Et Al. – Control – Kansas City Southern, Et. Al. STB Docket No. FD 36500, Elphick and Orr Dep. 18:8 – 18:25, Feb. 18, 2022
[137] Application, Vol 2, pp. 268 and 272; *see* details of trains 142 & 143 in Application, Vol. 2, p. 438.
[138] See Canadian Pacific Railway Limited, Et Al. – Control – Kansas City Southern, Et. Al. STB Docket No. FD 36500, Elphick and Orr Dep. 19:14 – 18:21, Feb. 18, 2022

> CSXT trackage rights that include daily haul-length limits, and as a result we adjusted downwards our Detroit intermodal diversions by 55 percent."[139]

To provide an estimate of 2019 Base Year volumes, I examined the 2019 full year waybill data and identified all movements that originated in Mexico or from points in or west/south of Illinois on CP or KCS/KCSM and that terminated on CP in Michigan, Eastern Canada, and New York. Also included is intermodal traffic terminating in Michigan from CP intermodal terminals in British Columbia.

Domestic double-stacked traffic from eastern Canada, especially Montreal must also use the CSX routing to reach Detroit, while most international container moves will fit through the Detroit River Tunnel. Because we could not readily determine which of this traffic needed to use the CSX routing, to be conservative we assumed all of it would fit through the tunnel.

I divided this data between intermodal, multilevel, ethanol, and other carload traffic. I also identified the volumes of intermodal traffic moving to/from Michigan versus Eastern Canada and well as the traffic to/from British Columbia.[140]

Next, I examined the data from Applicants' traffic diversion studies and identified all traffic that would necessarily use the NS or CSX routes, using the same screening criteria as the 2019 base traffic. For the diverted carload traffic, I added allowances for empty moves, using the same empty/loaded ratios that Applicants use in their system model, and added empties that would balance the intermodal volumes in the backhaul direction.

I added Applicants' projected organic growth rate of {{ }} to the Base Year volumes and added in the diversions that CP projected to arrive at the total projected Year 3 volumes for both the NS and CSX lines.

[139] Application, Vol. 2, p. 145.
[140] *See* HC – Oliver Wyman – NS CSX Traffic Analysis – Methodology.pdf for associated data and analysis workpapers.

All of this traffic was loaded into an Oliver Wyman version of MultiRail and "flowed" across the network to generate the cars/containers, tons, and train-feet that would use each route.[141]

CSX-Chicago-Fostoria (North Baltimore)-Buffalo and CSX Fostoria (North Baltimore)-Detroit

I defined the base and growth CSX traffic as purely intermodal. Initially, I assigned the British Columbia to Michigan intermodal traffic to the CSX line as well. As will be shown below, capacity constraints preclude this traffic from using this route once the full CPKC intermodal diversion volumes are realized.

My analysis of current traffic volumes and Applicants' projection of future organic growth and traffic diversion volumes indicates that the average daily volume to Detroit will be about {{XXX}} feet, thus exceeding the current contractual limit of 2,500 feet.[142] The peak volume on the train going to Buffalo, prior to setting off/picking up the Detroit traffic, should be around {{XXX}} feet on average.[143] Depending on the maximum allowed length of this train, there could well be capacity issues during peak periods.

Not included in my analysis is the Quebec/Montreal to Detroit base intermodal volumes of {{XXX}} containers per year, which translates to an additional {{XXX}} feet per day.[144] Assuming these are international containers, they will have to be routed through the Detroit River tunnel, given the capacity constraints on the CSXT routing.

[141] *See* MultiRail Corridor Volume, Tonnage and Length Estimates for Diversion Traffic Methodology.pdf for associated outputs and how growth traffic was obtained.
[142] Application, Vol 2, pp. 268 and 272; see details of trains 142 & 143 in Application, Vol. 2, p. 438.
[143] *See* HC – Oliver Wyman – NS CSX Traffic Analysis – Methodology.pdf for associated data and analysis workpapers.
[144] *See* HC – Oliver Wyman – NS CSX Traffic Analysis – Methodology.pdf for associated data and analysis workpapers. *See also* HC – Oliver Wyman - Intermodal to Railcar Conversion Factor Source Compilation.pdf.

Exhibit 6-6 details the intermodal volumes to/from Detroit, and Exhibit 6-7 provides the estimated average train lengths for the three main segments of the CSX service.

Exhibit 6-6: Volume on the CSXT segment between Ohio and Detroit[145]

Traffic Group	Containers/ Day (Forward)	Containers/ Day (Reverse)	Feet/Day (Forward)	Feet/Day (Reverse)
British Columbia: Intermodal – Base	{{XXX}}	{{XXX}}	{{XXX}}	{{XXX}}
British Columbia: Intermodal – Growth	{{XXX}}	{{XXX}}	{{XXX}}	{{XXX}}
Intermodal – Projected	{{XXX}}	{{XXX}}	{{XXX}}	{{XXX}}
Total	{{XXX}}	{{XXX}}	{{XXX}}	{{XXX}}

Exhibit 6-7: Volume on CSXT corridor by segment, in feet[146]

Traffic Group	Chicago-Fostoria feet		Fostoria-Detroit feet		Fostoria-Buffalo feet	
Source	Forward	Reverse	Forward	Reverse	Forward	Reverse
Intermodal – Base	{{XXX}}	{{XXX}}	{{XXX}}	{{XXX}}	{{XXX}}	{{XXX}}
Intermodal – Growth	{{XXX}}	{{XXX}}	{{XXX}}	{{XXX}}	{{XXX}}	{{XXX}}
Intermodal – Projected	{{XXX}}	{{XXX}}	{{XXX}}	{{XXX}}	{{XXX}}	{{XXX}}
Total	{{XXX}}	{{XXX}}	{{XXX}}	{{XXX}}	{{XXX}}	{{XXX}}

The calculations for Detroit are based on an estimate of current container volumes to Detroit of about {{XXX }}/year, almost entirely originating in British Columbia. This is equivalent to {{XXX }} of train. Projected new business yields another {{XXX}} and {{XXX }} of train for the to and from Detroit directions, and Applicants' organic growth figure of {{XXX }} yields another {{XXX }}/{{XXX }} directionally. This totals to {{XXX }} in the peak direction.[148]

Since the traffic moving to Detroit exceeds the 2500-foot limit, we must then assume that the BC Intermodal to Michigan traffic would travel via the NS line. This lowers the project

[145] *See* HC – Oliver Wyman – NS CSX Traffic Analysis – Methodology.pdf for associated data and analysis workpapers.
[146] *See* HC – Oliver Wyman – NS CSX Traffic Analysis – Methodology.pdf for associated data and analysis workpapers.
[147] *See* HC – Oliver Wyman – Review of Growth Factors in CPKC Application.pdf.
[148] *See* HC – Oliver Wyman – NS CSX Traffic Analysis – Methodology.pdf for associated data and analysis workpapers.

traffic to Detroit to {{XXX }}, below the 2,500 feet limit. However, this is alarming considering:

- Most likely, part of the Quebec/Montreal intermodal traffic of {{XXX }} will be domestic containers and must travel on the same line.
- There is little room for daily traffic variations. Intermodal service will be affected if, say, 10% of the traffic from Montreal is domestic and must ride through Buffalo and onto the Fostoria-Detroit section, and on a given day there is volume of eastbound traffic 15% higher than average. This will create situations that routinely exceed the 2500-foot limit. In practice, the peaks and valleys of intermodal traffic are at least 20%, so reaching the length limit and causing service issues due to delaying shipments of intermodal traffic is highly likely.

NS-Chicago-Detroit

Next we examined the NS-Chicago-Detroit line. Due to the above analysis, I include the British Columbia to Michigan Intermodal traffic on the NS routing.

We initially calculated the number of daily trains using the 12,000 maximum feet allowed by agreement with NS for manifest trains[149]. For the bulk hazardous trains (Ethanol), we derived that the filing used {{XXX}} cars per train. This is based on their {{XXX}} trains per day and our calculation of {{XXX}} cars per day (including growth).

Exhibit 6-8: CPKC - NS-Chicago-Detroit carload traffic volumes[150]

Traffic Group	Cars/Day (Forward)	Cars/Day (Reverse)	Feet/Day (Forward)	Feet/Day (Reverse)	Trains/Day (Forward)	Trains/Day (Reverse)	Basis
Ethanol – Base	{{XXX}}	{{XXX}}	{{XXX}}	{{XXX}}	{{XXX}}	{{XXX}}	Applied {{XXX}}[151] cars/train
Ethanol – Growth	{{XXX}}	{{XXX}}	{{XXX}}	{{XXX}}	{{XXX}}	{{XXX}}	
Ethanol Total	{{XXX}}	{{XXX}}	{{XXX}}	{{XXX}}	{{XXX}}	{{XXX}}	
Other Carloads - Base	{{XXX}}	{{XXX}}	{{XXX}}	{{XXX}}	{{XXX}}	{{XXX}}	Applied 12000 feet/train
Other Carloads - Growth	{{XXX}}	{{XXX}}	{{XXX}}	{{XXX}}	{{XXX}}	{{XXX}}	

[149] Application, Vol. 2, p. 272. See also Canadian Pacific Railway Limited, Et Al. – Control – Kansas City Southern, Et. Al. STB Docket No. FD 36500, Elphick and Orr Dep. 18:8 – 18:25, Feb. 18, 2022

[150] *See* HC – Oliver Wyman – NS CSX Traffic Analysis– Methodology.pdf for associated data and analysis workpapers

[151] In FD 3500 Work Paper HC Trains Per Day and Gross Ton Miles – Working Copy with Haz Breakdown.xlsx, the applicants cite 0.67 trains per day including growth. Based on the waybill data, that resolves to approx. 95 cars per train.

Other Carloads - Projected	{{XXX}}	{{XXX}}	{{XXX}}	{{XXX}}	{{XXX}}	{{XXX}}	
Other Carloads – Total	{{XXX}}	{{XXX}}	{{XXX}}	{{XXX}}	{{XXX}}	{{XXX}}	
BC Intermodal			{{XXX}}	{{XXX}}	{{XXX}}	{{XXX}}	
Total Trains					**{{XXX}}**	**{{XXX}}**	

We note that the statistics that we derived using the 2019 waybills and the Applicants' diversion traffic appear to be consistent with the train counts in the CPKC filing. The Application's workpapers shows {{XXX}} trains/day[152], and we derived {{XXX}} trains per day. While we agree overall with the Application, it apparently averaged the two directions resulting in misleading conclusions.

Our analysis demonstrates there is a need to operate more than {{XXX}} trains per day towards Detroit and {{XXX}} trains per day from Detroit, including both ethanol and manifest trains. However, {{XXX}} trains/day towards Detroit is precariously close to the maximum allowed of 2 trains per day. We can also infer that in practice {{XXX}} trains per day – of smaller size – will be traveling in the reverse direction to keep crews and locomotives in balance.

It is doubtful that there is enough capacity under the current NS agreement to service the projected carload traffic volumes for three reasons: (1) not every manifest train will be filled out to exactly its maximum length, (2) there will be peaks in traffic volumes and (3) there is the need to try to coordinate unscheduled ethanol trains and scheduled manifest trains sharing the available capacity. This becomes a particular concern because CPKC will need more than one manifest train on some days to service the volumes it needs to handle. When the need arises to operate both manifest trains and an ethanol train, one of these trains will need to be delayed. We must also consider that some amount of manifest traffic (or intermodal) will have to be delayed

[152] *See* FD 36500 - Work Paper - HC - Trains Per Day and Gross Ton Miles - 2021.10.22 - Working Copy with Haz Breakdown.xlsx

when the primary manifest train is full, and the overflow train is not operating on that specific day – hardly an ideal approach under the principles of Precision Scheduled Railroading.

Operating a second, "overflow" manifest train is also challenging if one is basing one's plans on having every train be at its maximum length of 12,000 feet. While running in an over-subscribed manner can help ensure that the primary train will be full, the secondary train will more likely than not, be only partially filled. Thus, a more likely scenario might be to assume an average of 11,000 feet per manifest train, which would put the daily average train count over {{XXX}} trains in the head haul direction.

Exhibit 6-9: CPKC - NS-Chicago-Detroit train counts assuming 11,000 foot manifest trains

Traffic Group	Trains/Day (Forward)	Trains/Day (Reverse)	Basis
Ethanol – Base	{{XXX}}	{{XXX}}	Applied {{XXX}} cars/train
Ethanol – Growth	{{XXX}}	{{XXX}}	
Ethanol Total	{{XXX}}	{{XXX}}	
Other Carloads - Base	{{XXX}}	{{XXX}}	Applied 11000 feet/train
Other Carloads - Growth	{{XXX}}	{{XXX}}	
Other Carloads - Projected	{{XXX}}	{{XXX}}	
Other Carloads Total	{{XXX}}	{{XXX}}	
BC Intermodal	{{XXX}}	{{XXX}}	
Total Trains	**{{XXX}}**	**{{XXX}}**	

Add in natural peaks and valleys in volumes of approximately 20 percent, and the clear result will be ongoing capacity issues. Further, this arrangement will prove even less sufficient beyond 2025, if CPKC actually achieves all the organic growth that Applicants are projecting. In part this reflects the dangers of creating a solution based on averages that have no slack to take natural volume variations into account.

6.3 Assessment of carload traffic issues

The Lazaro Cardenas intermodal traffic is but one example of the significant errors that are present in the traffic data (see Section 5.2 for discussion of Lazaro Cardenas issues). I also show in Section 4.1 that Applicants' use of non-representative data from October 2020 and in Section

5.5 the location mapping errors resulted in unbalanced yard volumes and associated errors in the yard statistics.

In Section 5.3.1, I showed that the use of October 2019 for unit trains resulted in a failure to account for all the crude oil trains operating on the key Sabula to Airline Junction line. Several additional issues are presented in this section, including:

- Other effects of using non-representative traffic data;
- Inconsistent use of organic growth; and
- The need for empty modeling to be consistent and complete.

6.3.1 Impact of using non-representative traffic data to drive the plan

I conducted a focused investigation of two sets of car types that were not treated as unit train traffic: Multilevels (car type V), and boxcars (car types A, B, R). This was done by comparing the full year, 2019 CPKC waybills to the October 2020 CPKC waybills. Based on this analysis, I found that the annualized, loaded multilevels on KCS and KCSM for October 2020 were approximately {{XXX }} below 2019 volumes, and the annualized loaded boxcars on KCS and KCSM for October 2020 were approximately {{XXX }} below 2019 volumes.[153] These findings are not surprising, given the lingering effects of the COVID-19 pandemic throughout 2020. Both undercounts directly affect Applicants' pre- and post-merger yard activity estimates and projected line densities. It is also possible that applying the higher 2019 traffic volumes would necessitate material changes to the train plan, including (potentially) the need to operate additional trains.

Another error that arises from using non-representative traffic is that there can be changes in traffic patterns, which will cause a shift in train requirements between various routings. I

[153] *See* HC – Oliver Wyman - Multi-level and Boxcar Traffic Volume Comparison between Full Year 2019 and October 2020 – Methodology.pdf for associated analysis and data.

considered loaded multilevels going to Laredo, primarily for interchange to Union Pacific (representing well over half of all loaded multilevels on KCS-KCSM). Some of the more significant differences are shown in Exhibit 6-10 and suggest that train flow and traffic patterns are not likely to be properly estimated by Applicants' methodology, due to differences in traffic volumes between October 2020 and full year 2019 traffic patterns.

Exhibit 6-10: Differences in annualized volumes destined for Laredo[154]

Origin-Destination	2019 Full Year Waybill	October 2020 (Annualized)	Difference
Lecheria-Laredo	{{XXX}}	{{XXX}}	-7,894
Jesus Maria-Laredo	{{XXX}}	{{XXX}}	-2,703
Pesqueria-Laredo	{{XXX}}	{{XXX}}	-581
Derramadero-Laredo	{{XXX}}	{{XXX}}	577
Rojas-Laredo	{{XXX}}	{{XXX}}	2,186
Silao-Laredo	{{XXX}}	{{XXX}}	3,936
Panzacola-Laredo	{{XXX}}	{{XXX}}	7,818

The correction of the differences between the October 2020 traffic and the full-year 2019 traffic would lead directly to a shift in thousands of railcars between lanes, which clearly would affect line densities, yard volumes, and train sizes. Applicants stated that 2019 was their chosen Base Year. But, as Exhibit 6-14 graphically demonstrates, attempting to build a 2019 operating plan based on traffic data for a single month in a different year (2020) is likely to produce inaccurate results.

6.3.2 Inconsistent use of organic growth raises questions as to the accuracy of the post-merger plan

Applicants state that organic growth was included in the post-merger operating plan:

> "In order to confirm – and demonstrate to the Board – that the operation of the combined network will be fully resourced and capable of an efficient operation without congestion or service degradation. The traffic growth considered thus includes both

[154] *See* HC – Oliver Wyman - Multi-level and Boxcar Traffic Volume Comparison between Full Year 2019 and October 2020 – Methodology.pdf for associated analysis and data.

> anticipated volume growth for traffic currently handled by CP or KCS as well as volume growth that will be attracted by the combined network."[155]

Despite this assertion, there is no meaningful discussion in either the Application or the work papers explaining how organic growth traffic volumes were developed, or how they were input to the operating plan in MultiRail. Organic growth is a major element of post-merger traffic and revenue. As such, a credible operating plan must include a full explanation of the key assumptions made in developing organic traffic growth, and basis supporting any projected "organic" traffic increase. Applicants' "System Model"[156] contains unexplained and unsupported organic growth traffic values, as do a number of other work papers.[157] It appears that the growth values adopted by Applicants are generally "global" assumptions applied either to the entire CPKC network or applied differentially by predecessor railroad, in each case without regard to commodity or origin/destination.

A review of the work papers indicates that organic growth traffic was included in Applicants' MultiRail modeling,[158] and thus was reflected in the post-merger train counts and train-miles generated by MultiRail. However, the application of unexplained "calibration factors" to the GTM and train-mile values generated by MultiRail raises questions as to whether (or how) this organic growth traffic was ultimately reflected in the System Model that served as the foundation for Applicants' operating expense estimates. Without access to the actual pre- and post-merger MultiRail traffic files used to develop the operating plan, it is impossible to ascertain exactly how organic growth was handled. Based on the use of system averages, and the

[155] Application Vol. 2, pp. 286-287.
[156] FD 36500 - Work Paper - HC - Cost Metrics Growth Model _ Base year 2019.xlsx.
[157] FD 36500 - Work Paper - HC - Trains Per Day and Gross Ton Miles - 2021.10.22 - Working Copy with Haz Breakdown.xlsx applies organic growth parameters to the base period unit trains.
[158] FD 36500 - Work Paper - HC - Trains Per Day and Gross Ton Miles - 2021.10.22 - Working Copy with Haz Breakdown.xlsx.

overstatement of organic growth in the calculation of gross tons by line segment values,[159] I have no confidence that this growth was appropriately handled.

6.3.3 Empty modeling is inconsistent and incomplete

Because Applicants' modeling process included a mix of historic traffic and diverted traffic, empty car movements must be carefully considered in building a reliable operating plan. At a minimum, Applicants must account for sufficient empty movements for diverted traffic. However, it can be challenging to identify which empty movements should be adjusted in the case of extended haul traffic.

In some cases, particularly for grain and ad hoc unit trains, it also can be challenging to determine which empty moves correspond to loaded unit train movements when volume adjustments must be made. While in some cases one can identify unit train movements through multi-car waybills, one often needs to identify unit train moves by finding sets of cars with the same origin, destination, car type, commodity, load/empty status, and waybill date/time. This becomes a significant data analysis exercise. If the empty movements are treated similarly and are reverse routed to the loaded movement's origin after unloading, this is not too hard. But for commodities such as grain, the empty trains generally do not reverse route, but go to alternate loading sites instead. In addition, these unit trains are often broken up and the cars may then be moved to a variety of next loading sites. When this happens, figuring out which empty moves correspond to which loaded moves can become very tricky, and making volumetric adjustments to these empty moves when they are sent to multiple next loading sites can become almost impossible.

[159] *See* HC – Oliver Wyman - Review of Growth Factors in CPKC Application.pdf for details.

Therefore, to ensure consistency between loaded and empty movements for the pre- and post-merger operating plans, it is more reliable to actually model or generate empty movements, instead of using a mix of historic and generated empty movements. In particular, such an approach avoids the need to make complex adjustments to historic empty movements.

In developing empty movements, careful attention must be paid to historic directional traffic balance and empty/loaded ratios to ensure that the appropriate numbers of car-miles and ton-miles are associated with empty movements. Applicants elected to pursue the complex approach of making (supposedly) "surgical" adjustments to historic traffic for extended haul movements, while at the same time applying simplistic load/empty rules for key intermodal and automotive traffic.

As a result, I believe that the following errors were likely made by Applicants in the MultiRail modeling exercise:

- Empty multilevel volumes are understated. It appears that a {{XXX }} empty return ratio was used.[160] Examining the imbalance between loaded northbound and southbound moves from/to Mexico in Applicants' traffic diversion study reveals that the flow of loads is unidirectional in the northbound direction. This indicates that a much higher southbound empty return ratio ({{XXX-XXX}} percent) would be more appropriate for this traffic.[161]
- Empty intermodal container volumes are understated. It appears that a {{XXX }} empty return ratio was used for intermodal shipments.[162] Examining the imbalance between loaded northbound and southbound moves from/to Mexico in the traffic diversion study indicates that a southbound empty return ratio of approximately {{XXX

[160] Table on "Tonnage Assumptions" in FD 36500 – Work Paper – HC – System Model - Methodology.pdf, p. 4.
[161] *See* HC – Oliver Wyman - Evaluation of Load and Empty Ratios – Methodology.pdf for associated data and analysis.
[162] Table on "Tonnage Assumptions" in FD 36500 – Work Paper – HC – System Model - Methodology.pdf, p. 4.

}} would be more appropriate.[163] If one examines the volume of northbound containers from Mexico into the U.S., and compare this to the volume of southbound containers from the U.S. to Mexico in the CPKC traffic study you will find that for every {{XXX}} northbound loads there are about {{XXX}} southbound loads. Thus, to balance this movement of containers one needs to introduce {{XXX}} southbound empties for every {{XXX}} northbound loads, resulting in a {{XXX}} percent southbound empty return ratio.

- Certain other car types historically have an empty/loaded car-mile ratios that are greater than 1:1. This is particularly true of tank cars, which in the case of KCS have historic empty/loaded ratios of about {{XXX }}.[164]

All these errors result in an understatement of gross-ton-miles and car-miles and would also lead to an understatement of train-miles in the Applicants' "System Model."

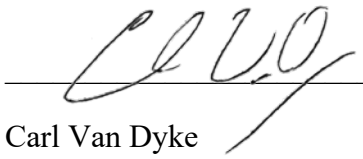
[163] 70% reverse route value is based on witnesses Wahba & Naatz's growth traffic data (FD 36500 – Work Paper – HC – Growth Initiative Calculations.xlsx), where they used an average value of 70% under "Assumed Backhaul" for the total intermodal volume at Lazaro Cardenas. *See* also HC – Oliver Wyman - Evaluation of Load to Empty Ratios.pdf

[164] *See* HC – Oliver Wyman - Evaluation of Load and Empty Ratios – Methodology.pdf for associated data and analysis.

VERIFICATION

I, Carl Van Dyke, declare under penalty of perjury that the foregoing information is true and correct. Further, I certify that I am qualified and authorized to file this statement.

Executed on this 28th day of February, 2022.



Carl Van Dyke

Appendix A. Carl Van Dyke Resume

Mr. Van Dyke is Managing Director of TransNetOpt, a consultancy focused on the use of computers to address transportation network planning and design issues. He is a retired Partner in the Surface Transportation Practice of Oliver Wyman, with a focus on improving the operations and general performance of transportation companies, and railroads in particular. He continues to undertake engagements on behalf of Oliver Wyman in the role of Senior Advisor. Mr. Van Dyke has spent over 40 years focused on the application of computers to transportation planning and operations issues, with particular emphasis on railroad network modeling, service design, train scheduling, line capacity analysis, and equipment management. In 1992, he founded MultiModal Applied Systems, which became part of Oliver Wyman in 2006.

He is best known for leading the design, creation, and application of the MultiRail planning products, including both the MultiRail-Passenger Edition and MultiRail-Freight Edition. The Freight Edition has been used by major freight railroads around the world, and has become the tool of choice for special studies such as mergers, privatization studies, operating plan redesigns, and routing/yard investment analysis. Over the past decade, Oliver Wyman-MultiModal has had a hand in the redesign of the operating plans of every major North American railroad, and is now pursuing a similar role in Europe, Africa, and the CIS.

Mr. Van Dyke has designed and implemented over a dozen freight rail, passenger rail, trucking, and container line operations planning models, many of which significantly advanced the state-of-the-art through the use of innovative algorithms and user interfaces. He also has played a key role in the adoption of algorithm-based methods for the real-time control of car routing and classification at a major North American carrier, and has led the development of a similar system which became the MultiRail-Enterprise Edition. Over the course of his career, he has provided technical assistance to dozens of railroads for the in-house use of MultiRail and other models, including all of the major North American carriers, and a number of commuter operators. The "scheduled railroad" operating plans deployed by five of the six Class I's were developed using MultiRail and Oliver Wyman-MultiModal's consulting services. Work with CP resulted in winning the 2003 Franz Edelman Prize in Operations Research from the Institute for Operations Research and Management Science (INFORMS).

An integral part of the modeling work undertaken by Mr. Van Dyke has been the analysis of traffic and operating plans related to mergers and reconfigurations of railroads. He first started undertaking this work by participating in the processing of the STB Waybill Sample and full waybill databases from individual railroads while at ALK Associates in the late 1980s. This work included traffic database processing, network traffic flow modeling, and diversion analysis. He went on to fill leading roles in traffic modeling and operating plan development efforts for the UP-SP, NS-Conrail, IC-CN, and CN-BNSF merger filings, as well as developing traffic models for the break-up of the Mexican railroads. Deep experience processing full-year proprietary railroad waybill databases was also gained through numerous projects including operating plan development efforts at Class I's in North America, and at a variety of railroads in countries such as Sweden, Switzerland, Italy, France, Kazakhstan, Germany, and South Africa.

Over the course of his career, Mr. Van Dyke has become very familiar with the computer systems that drive the operations and planning aspects of numerous railroads in both North

America and many other countries around the world. He has worked extensively with the IT departments at many of these railroads in the design and development of a wide variety of systems, and through this process has become familiar with the IT practices and organizations at these railroads. Examples include assistance to Class I's in the design of current production systems, development of roadmaps for systems improvement, and design and development of numerous planning systems.

Mr. Van Dyke's background in equipment management includes directing the design and development of a real-time, intermodal equipment management system for the rail industry, and adapting this model for use by a major steamship line. He also worked on the development of locomotive planning tools that have been applied to a number of major railways worldwide. While at ALK Associates, Mr. Van Dyke also served as President of Fleet Management, Inc., a company providing central management of railway car fleets. Mr. Van Dyke's other areas of expertise include the design and implementation of optimization and heuristic algorithms, logistics and market analysis, network rationalization, traffic analysis, and geographic information systems.

Mr. Van Dyke received an MS degree in civil engineering from MIT, with a concentration in transportation. He graduated *summa cum laude* from the University of Pennsylvania with a BSE in mechanical engineering. He has served on the National Council of the Transportation Research Forum, various Transportation Research Board committees, and was a charter member and former Chairman of the Rail Applications Special Interest Group of INFORMS. MultiRail, based on its impact on the rail industry, was named "technology of the decade" by *Trains Magazine* in November 2010. He is a co-author of a book on the use of operations research in the rail industry, which was published by Springer Verlag in 2015. He makes presentations and writes articles on a regular basis on various transportation analysis topics.

Exhibit 3

Verified Statement of Hugh Randall

BEFORE THE
SURFACE TRANSPORTATION BOARD

STB FINANCE DOCKET NO. 36500

CANADIAN PACIFIC RAILWAY LIMITED; CANADIAN PACIFIC RAILWAY COMPANY; SOO LINE RAILROAD COMPANY; CENTRAL MAINE & QUEBEC RAILWAY US INC.; DAKOTA, MINNESOTA & EASTERN RAILROAD CORPORATION; AND DELAWARE & HUDSON RAILWAY COMPANY, INC. – CONTROL – KANSAS CITY SOUTHERN, THE KANSAS CITY SOUTHERN RAILWAY COMPANY, GATEWAY EASTERN RAILWAY COMPANY, AND THE TEXAS MEXICAN RAILWAY COMPANY

CN'S COMMENTS ON APPLICATION AND REQUEST FOR CONDITIONS

Verified Statement of Hugh Randall

February 28, 2022

PUBLIC VERSION

Contents

1. Qualifications....1

2. Assignment and Summary of Findings....1

3. Applicants' Capital Expenses Are Significantly Understated for Their Projected {{XXX }} Growth....3

3.1 Applicants have failed to prove the adequacy of their committed capital investment funding....7

3.2 Applicants have failed to make provision for capital projects that will be required to accommodate post-merger traffic volumes....9

4. Applicants Significantly Understate Operating Expenses By At Least $2 Billion and Project an Operating Ratio of 30 Percent for Merger-Related Traffic....23

4.1 The methodology employed by Applicants to estimate post-merger operating expenses is flawed and opaque....25

4.2 Applicants' operating expense estimate omits some expenses and underestimates others....29

4.3 Large operating expense savings claimed for the first year of the merger are unlikely to be realized....31

4.4 Applicants' projected Year 1-3 operating expense projections are further belied by industry benchmarks....34

4.5 The shortfall in Applicants' projected operating expenses is substantial....36

Appendix A. Yard Capacity Assessment....39

Appendix B. Subdivision Capacity Assessment....41

B.1 CP Line: St. Paul, MN/Elgin, IL to Kansas City, MO....41

B.2 KCS Line – Beaumont, TX to Laredo, TX....43

B.3 KCSM Line – Laredo, TX to Metro Mexico City, MX....45

Appendix C. Description of Rail Crossings Assessment....46

Appendix D. Methodology for Estimating Capacity....47

Appendix E. Deposition Quotes on Capacity Analysis for KCS Lines....49

Appendix F. Hugh L. Randall Resume....53

1. Qualifications

My name is Hugh Randall. I am a Senior Advisor to and a Partner Emeritus of Oliver Wyman, a global general management consulting firm with more than 60 offices in 31 countries. My office address is 1717 Main Street, Suite 4400, Dallas, TX 75201.

I have been engaged as a consultant to the transportation industry for the past 30 years and was formerly head of Oliver Wyman's global transportation consulting practice. In that capacity, I have directed consulting projects for railroads, airlines, trucking companies, parcel carriers, maritime shipping companies, freight forwarders, and contract logistics users and providers. Those studies have encompassed clients in North America, Europe, Asia, Latin America, and southern Africa.

Prior to joining Oliver Wyman, I held several senior management positions in the rail and trucking industries, including Assistant Vice President – Intermodal Planning, Assistant Vice President – Operations, and General Manager – Atlantic Region at Conrail; Executive Vice President and Chief Financial Officer at Ryder/PIE; and Managing Director of CSX/Sealand Logistics. I hold a BA degree from Antioch College and an MBA from Harvard University. My full resume is provided in Appendix F.

2. Assignment and Summary of Findings

I have been asked to review and comment on (1) Applicants' estimate of the capacity improvements and other capital expenditures that would be required to handle the additional traffic volumes projected by Applicants safely and efficiently, and (2) Applicants' projected

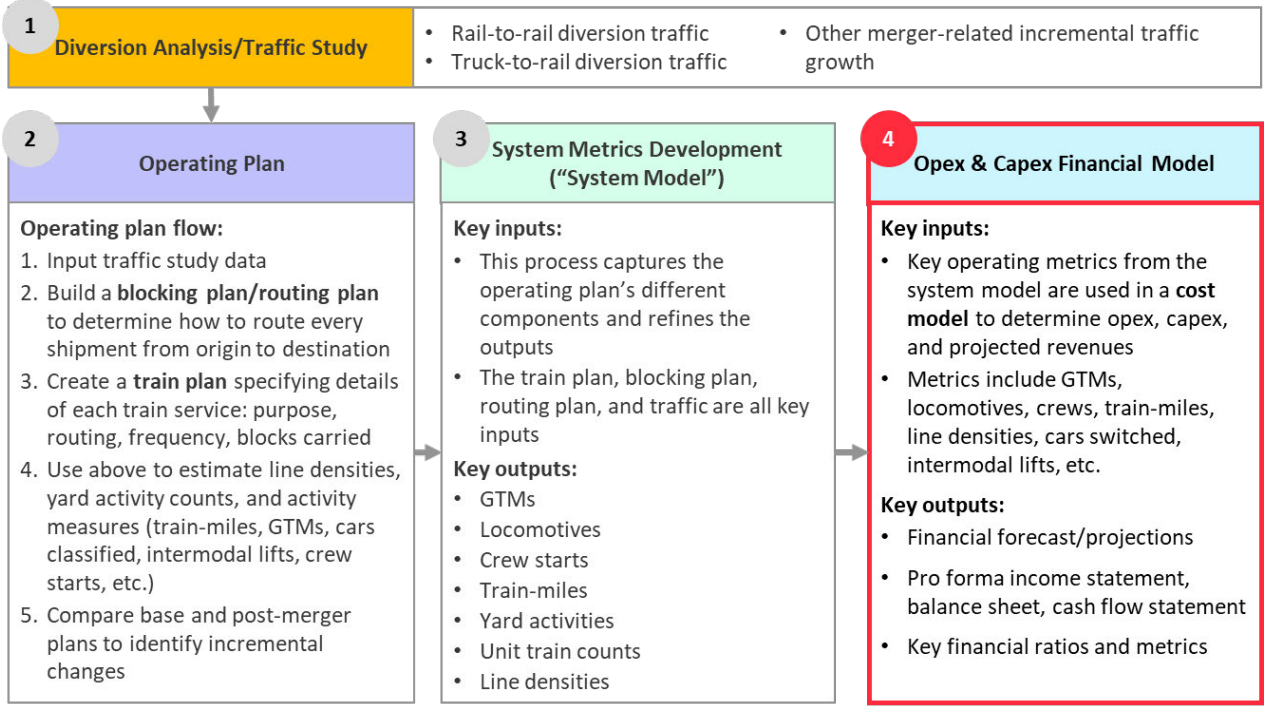
post-merger operating expenses, in each case as presented in the Application[1] and in the work papers of Applicants' witnesses. Solely for purposes of this Verified Statement, I have assumed that the envisioned merged railroad, CPKC, will achieve the traffic increases projected in the Application.

As shown in Exhibit 2-1, complete and accurate operating and capital expense plans are essential elements of the merger planning process. Accurate operating and capital expense plans, in turn, depend on accurate traffic projections and operating statistics (such as train-miles and gross ton-miles – "GTMs"). The capital and operating expense plans provide an essential cross-check to determine whether the Applicants have committed sufficient resources to execute their operating plan.

As CN witness Hunt demonstrates, Applicants' post-merger traffic projections are wildly inaccurate. CN witness Carl Van Dyke identifies numerous errors and omissions in Applicants' operating plan that render the resulting operating statistics invalid. As my testimony will demonstrate, these flaws in Applicants' traffic study and operating plan, and other errors described below, render the operating and capital expense estimates and post-merger financial exhibits set forth in the Application meaningless.

[1]The Application filed on October 29, 2021 by Canadian Pacific Railway Limited, Canadian Pacific Railway Company, and their US rail carrier affiliates (collectively, "CP") and Kansas City Southern and its US rail carrier affiliates (collectively, "KCS") seeking approval of the acquisition of control by CP of KCS. In this Verified Statement, I refer to CP and KCS collectively as "Applicants," and the proposed merged carrier as "CPKC."

Exhibit 2-1: Elements of a reliable merger plan: The financial model (operating and capital expense) is dependent on the accuracy of Applicants' traffic projections and post-merger operating plan[2]



3. Applicants' Capital Expenses Are Significantly Understated for Their Projected {{XXX }} Growth

Making adequate investment in infrastructure and equipment is essential to a railroad's ability to provide efficient and reliable service. The Board understands this linkage: The Board has focused on railroad service issues and the potential for service disruption on one railroad to impact other parts of the interconnected North American rail network, and has inquired whether

[2] This is the logic flow explicitly cited in the Canadian National-Illinois Central and Norfolk Southern-Conrail merger applications to the Board. *See* FD33556, Canadian National Railway Company, Grand Trunk Corporation, and Grand Trunk Western Railroad Incorporated – Control – Illinois Central Corporation, Illinois Central Railroad Company, Chicago, Central & Pacific Railroad Company, and Cedar River Railroad Company Railroad Control Application, Volume 2 of 4, Section 2.0. Oliver Wyman has been unable to find a statement indicating an explicit connection between the operating plan and financial model in the Canadian Pacific-Kansas City Southern Application.

railroads have adequate infrastructure and car supply to provide reliable service to their customers.[3]

The Board's pre-2001 merger regulations, which govern this proceeding, explicitly require the Applicants to address:

> "The anticipated equipment requirements of the proposed system, including locomotives, rolling stock by type, and maintenance-of-way equipment; plans for acquisition and retirement of equipment; projected improvements in equipment utilization and their relation to operating changes; and how these will lead to the financial and service benefits described in the summary."[4]

The Board again explicitly recognized the importance of a comprehensive capital expenditure plan when it promulgated the current service assurance plan requirement for Class I railroad mergers, which require:

> "Applicants must develop a capital improvement plan (to support the operating plan) for timely funding and completion of the improvements critical to transition of operations. They should also describe improvements related to future growth and indicate the relationship of the improvements to service delivery."[5]

These regulations describe the elements of an adequate capital investment plan. Exhibit 2-1 above shows the steps a railroad would typically follow to develop a capital expenditure plan using its projected traffic, operating plan, and system metrics to identify investments in track and facilities, rolling stock, and other assets required to accommodate the railroad's anticipated traffic. Capital investments logically are targeted to those projects and locations where additional capacity and/or resources are needed to ensure competitive transit times and service reliability. [6]

[3] *See*, for example, Ex Parte No. 724, which was initiated in response to service quality complaints concerning Canadian Pacific and led to weekly performance data reporting requirements for all Class I railroads.
[4] 49 CFR 1180.8(a)(3) (2000).
[5] 49 CFR 1180.10(d) (2001).
[6] Applicant railroads have likewise recognized that an accurate capital plan is essential to demonstrating that a merger will be operationally and financially viable. For example, in its application to control the Illinois Central, Canadian National provided the Board with a section

Here, Applicants have failed to present a detailed capital investment plan that makes adequate provision for additional track and yard capacity, bridge renewal and replacement, and rolling stock and resources at locations where they claim the proposed merger will generate substantial increases in traffic and train and yard activity. In particular:

- The Application does not contain the detailed, location-specific information required to assess the adequacy of Applicants' capital investment plan. While the Application asserts that Applicants will spend $5.7 billion in Years 1-3 for what is vaguely described as "capex," only about {XXX } of that sum is actually allocated to specific investments that are described in the Application.[7]
- Applicants state that their financial projections do not include revenues and expenses related to organic growth.[8] However, as confirmed in witness Van Dyke's Verified Statement, Applicants' operating plan outputs include the impact of {{XXX }} organic growth in GTMs by 2025 (the assumed Year 3 of the merged system) and 19.8 percent growth in GTMs as a result of the merger, for a total increase of {{XX }}

concerning "Line Infrastructure, New Construction, and Other Capital Investments." That section included subsections concerning line infrastructure, merchandise/unit train yards, intermodal/auto terminals, new and upgraded connections, locomotives, information systems, and a summary of capital investments. In each case, Canadian National identified the specific projects to be undertaken and the specific funds budgeted. (*See*, for example, FD33556, Canadian National Railway Company, Grand Trunk Corporation, and Grand Trunk Western Railroad Incorporated – Control – Illinois Central Corporation, Illinois Central Railroad Company, Chicago, Central & Pacific Railroad Company, and Cedar River Railroad Company Railroad Control Application, Volume 2 of 4, Section 7.0.)

[7] Verified Statement of John A. Orr and Raymond F. Elphick at p. 84 identify $276 million for one merger-related capital project, including new sidings and CTC on the mainline between Sabula Jct., IA and Beaumont, TX. For a second capital project, Verified Statement of James Clements at p. 9 identifies $138.6 million for IT and communications integration of the two railroads. For a third capital project, Orr and Elphick V.S. at p. 70 identify $45 million for locomotive rebuilds in Year 3. (Orr and Elphick V.S. at p. 70, identify $135 million for locomotive rebuilding but defer rebuilding of 90 locomotives in Years 1 and 2, saving $90 million. From this statement, I infer that Applicants will spend $45 million to rebuild 45 locomotives in Year 3). The sum of these three expenditures is $459 million, which is 8 percent of the $5.7 billion for capital improvements ($1.9 billion per year as identified in Appendix G of Application 1 for three years equals $5.7 billion).

[8] Verified Statement of Chris De Bruyn, p. 6.

in GTMs by Year 3.[9] It is unclear whether Applicants' average of $1.9 billion per year budgeted (but largely unspecified) capital investment funding, in their financial projections for each of Years 1-3, includes adequate funding for capacity improvements to handle organic and merger-related GTM growth of {{XXX }} by Year 3 of the merged system, as well as funding for the normal renewal of assets.

- Whether Applicants intend that the average $1.9 billion per year will cover both organic and merger-related growth, this amount of funding appears to be inadequate, especially when compared with Applicants' own pre-merger capital spending. Between 2014 and 2019, CP and KCS together made capital investments equal to, on average, 24.2 percent of their annual revenue.[10] In no year did the railroads spend less than 21.0 percent of their combined revenue on capital investments. Yet the Application indicates that the merged CPKC would spend only 19.3 to 20.6 percent of post-merger revenue during each of Years 1-3.

  In terms of dollars spent for capital expenditures during 2014-2019, CP and KCS in total spent an average of $1.9 billion per year.[11] During that period, the GTMs carried by CP and KCS combined grew by 3 percent.[12] The $1.9 billion per year budgeted for Years 1-3 is no more than the average annual spend for 2014-2019, even though post-merger annual GTMs are projected to increase by more than {{XXX }} from 2019 to Year 3.[13] Also, one would expect Applicants to dedicate a greater percentage of revenue to undertake capital projects in the early years, so as to prepare the network to handle increased volumes of post-merger traffic. Applicants' capital expenditure plan is insufficient to support just organic growth, much less the projected $1 billion in

[9] Application, Vol. 2, p. 287, Exhibit 13 Table 2; Oliver Wyman Capex worksheet No. 1, GTMs tab.
[10] Railroad Facts, 2015 to 2020 editions (which contain statistics for 2014 to 2019), Association of American Railroads. *See* HC - Oliver Wyman – HC - Capex Worksheet No. 1 for calculation.
[11] Railroad Facts, 2015 to 2020 editions, Association of American Railroads. *See* HC - Oliver Wyman - Capex Worksheet No. 1 for calculation.
[12] Based on data reported in CP's annual reports and KCS's Consolidated Investors' Reports, the combined GTM growth from 2014 to 2019 was 3 percent (371,526 million GTMs in 2014 to 382,543 million GTMs in 2019). (CP Annual Report 2014, p. 26 and 2019 Annual Report p. 57; KCS Consolidated Investors Report Q4 2014, p. 12 and Q4 2019 p. 13.) *See* HC - Oliver Wyman - Capex Worksheet No. 1, GTMs tab.
[13] *See* HC - Oliver Wyman - Capex Worksheet No. 1 – GTMs tab for GTM growth calculation.

additional merger-related traffic.[14] Applicants offer no explanation as to how the merged CPKC could handle a {{XXX }} increase in GTMs and maintain service levels, while not increasing the level of capital spending they have incurred in the normal course of business. In the absence of such an explanation, Applicants' capital plan is simply not credible.

- Applicants failed to provide for a number of capital projects that will almost certainly be required to accommodate their projected traffic growth. As discussed below, such improvements include expanding capacity of tracks, yards, intermodal terminals, and auto ramps at locations that will experience substantial increases in train activity; and providing sufficient locomotives and railcars to handle projected traffic volumes.

3.1 Applicants have failed to prove the adequacy of their committed capital investment funding

Applicants have not provided a detailed description of capital investments that will be made post-merger, nor have they shown that a merged CPKC will have adequate funding allocated to its capital plan, given projected traffic growth.

While the Application includes $5.7 billion in Years 1-3 for what is vaguely described as "capex," Applicants have allocated only about 8 percent of that sum for specific identifiable projects.[15] Nowhere in the Application or work papers do Applicants identify the nature or location of other specific capital projects that they propose to undertake during Years 1-3, much less the estimated cost and timing of such work. In the absence of such evidence, it is impossible for interested parties or the Board to assess the adequacy of Applicants' capital spending plans. Applicants also have not demonstrated that the amount of capital provided in their financial exhibits will be sufficient to accommodate merger-related and organic volume growth.

[14] Application Vol. 1, Appendix F, Income statement (Change in Revenue Between Year 3 and Base Year), pp. 131-142.
[15] Orr and Elphick V.S., pp. 70 and 84; Clements V.S., p. 9.

In the absence of project-specific information, benchmarks can be used to evaluate Applicants' capital plan.

Historical capital spending by CP and KCS prior to the merger. As shown in Exhibit 3-2, CP and KCS collectively averaged capital expenditures equal to 24.2 percent of revenue between 2014 and 2019. *In no year were their combined capital expenditures less than 21.0 percent of their combined revenue.* Yet the Application indicates that Applicants plan to spend only 20.6 percent of revenue in Year 1, 20.0 percent of revenue in Year 2, and 19.3 percent of revenue in Year 3 on capital projects, despite a projected increase of {{XX }} in GTMs by Year 3.[16]

Exhibit 3-2: CP and KCS (full system) combined capital spending, 2014-2019[17]

$ billions

	2014	2015	2016	2017	2018	2019	Avg. 2014-19
Revenue	$8.6	$7.7	$7.0	$7.6	$8.3	$8.7	$8.0
Capex	$2.3	$2.1	$1.5	$1.8	$2.0	$1.9	$1.9
Capex as % of revenue	27.4%	27.4%	21.0%	23.3%	23.7%	21.9%	24.2%

Dollars spent for capital expenditures is another relevant benchmark. During 2014-2019, CP and KCS together spent an average of $1.9 billion per year, while GTMs grew by 3 percent during that period.[18] Yet Applicants propose to spend the same $1.9 billion per year for Years 1-3 post-merger,[19] an amount that is woefully deficient in light of their projected increase of more than {{XXX }} in GTMs by Year 3 of the merger compared to 2019. It is simply not credible to assume that Applicants can adequately address the merged railroad's capital needs by

[16] Application Vol. 1, Appendix G, p. 143; Oliver Wyman Capex worksheet No. 1, Capex tab.
[17] Railroad Facts, 2015 to 2020 editions, Association of American Railroads; *see* HC - Oliver Wyman Capex Worksheet No. 1 for calculation. Includes all North American operations.
[18] Based on data reported in CP's annual reports and KCS's Consolidated Investors' Reports, the combined GTM growth from 2014 to 2019 was 3 percent (371,526 million GTMs in 2014 to 382,543 million GTMs in 2019). (CP Annual Report 2014, p. 26 and 2019 Annual Report, p. 57, KCS Consolidated Investors Report Q4 2014, p. 12 and Q4 2019, p. 13.) *See* HC - Oliver Wyman - Capex Worksheet No. 1, GTMs tab.
[19] Application Vol. 1, Appendix G, pp. 143-154, cash flow statement.

spending no more per year than they spent before the merger, while accommodating significantly higher traffic growth. Moreover, Applicants are asking the Board to accept this clearly inadequate capital plan with no detailed explanation as to how or where the $5.7 billion in capital expense funding would be deployed. The Applicants' capital plan is clearly completely inadequate in terms of describing the investment needs of the merged railroads.

3.2 Applicants have failed to make provision for capital projects that will be required to accommodate post-merger traffic volumes

To understand whether Applicants' proposed capital spending sufficiently accounts for the capacity that would be consumed by their projected traffic increases, I conducted the following analysis. I note that in many cases my analysis was constrained by the lack of detailed information that ordinarily would be provided in a capital planning process (for example, the Applicants did not provide a complete set of track or bridge condition reports until the week before opposing statements were due).

- I assessed the line-of-road and yard capacity increases that would be required to handle projected increases in carloadings, using CP's methodology for assessing capacity compared to expected demand.
- I compiled a list of locations (such as subdivisions, yards, at-grade crossings with other Class I railroads, and bridges) where Applicants did not identify any specific capital projects, but where the projected increase in trains per day (or, in the case of yards, car handlings per day) make it virtually certain that significant capital investment will be necessary to maintain fluid operations to serve customers. I also reviewed certain trackage rights agreements where CPKC as a tenant railroad may be required to expand capacity to accommodate an increase in its traffic, but where Applicants have not identified any specific capital allocation. Given the projected increases in trains and yard handlings in the Application, I identified a number of critical capital expenditures that were not identified in the Application, as shown in Exhibit 3-3 and described below.

Exhibit 3-3: Critical capital expenditures missing from the Application but likely required

Category	Potential capex issue	Resources impacted
Line of road	• Significant train delays and service disruptions are likely without additional capital spending • The number and location of long sidings to handle 10,000-foot trains are likely inadequate to prevent post-merger delays • No capital allocation for busy at-grade crossings controlled by other railroads • No capital allocation for increased traffic on lines accessed via trackage rights • No capital allocation for Mexican lines	• Seven subdivisions • Three at-grade UP/BNSF rail crossings • Two UP line segments used by CPKC under trackage rights agreements
Yards	• No capital allocated to handle increased workloads, except at Bensenville • Adequacy of Bensenville expansion cannot be determined from information provided	Yards located in: • Bensenville, IL • Schiller Park, IL • Shreveport, LA • Wylie, TX • St. Paul, MN
Automotive ramps/ intermodal terminals	• No capital allocated to handle increased workloads	• All auto ramps/intermodal terminals except Bensenville
Bridges	• No capital allocated for bridge expansion/ replacement to handle increased traffic	• Neches River Bridge • KCS Bridge at Laredo
Revenue cars	• Insufficient new cars being added to handle projected loadings, given projected retirements	• Insufficient gondolas and centerbeam flats for steel and forest products loadings
Locomotives	• Insufficient new and rebuilt locomotives to handle increased traffic	• Less than 1 percent increase in fleet size to move {{XXX }} more GTM's in Year 3 • 45 rebuilds per year (need 90)

3.2.1 Insufficient capital investment for expanded track capacity (line of road)

I assessed the ability of each CP and KCS/KCSM subdivision on the north-south post-merger route between CP's Marquette subdivision (south of St. Paul), on the one hand, and KCSM's Tula subdivision (north of Mexico City), on the other hand, to absorb the increase in train activity projected in the Application, *using Applicants' own approach to capacity analysis*.[20] As shown in Exhibit 3-4, Applicants project a large increase in trains per day for

[20] A description of my (and CP's) capacity assessment methodology is provided in Appendix D.

almost every one of those subdivisions, as well as an increasing number of trains that will require 10,000-foot sidings (which is CP's stated objective for non-bulk trains, to achieve its post-merger productivity assumptions).

Exhibit 3-4: Applicants' projected increase in trains per day by subdivision[21]

Subdivision	State	Base Trains/Day	Year 3 Trains/Day	% Growth	Base (Non-Bulk Trains)	Year 3 (Non-Bulk Trains)
Chicago	IL	2.9	11.1	283%	{{XXX}}	{{XXX}}
Marquette	IA	7.7	14.3	86%	{{XXX}}	{{XXX}}
Davenport	IA	7.1	21.6	204%	{{XXX}}	{{XXX}}
Ottumwa	IA	4.2	18.4	338%	{{XXX}}	{{XXX}}
Laredo	TX	3.0	17.0	467%	{{XXX}}	{{XXX}}
Kansas City	MO	2.9	16.9	483%	{{XXX}}	{{XXX}}
Pittsburg	KS	13.5	28.5	111%	{{XXX}}	{{XXX}}
Heavener	OK	11.3	25.9	129%	{{XXX}}	{{XXX}}
Shreveport	LA	9.4	23.6	151%	{{XXX}}	{{XXX}}
Beaumont	TX	8.9	20.3	128%	{{XXX}}	{{XXX}}
Rosenberg	TX	8.5	17.7	108%	{{XXX}}	{{XXX}}
KCS Laredo	TX	10.5	19.4	85%	{{XXX}}	{{XXX}}
Saltillo	MX	24.1	29.8	24%	{{XXX}}	{{XXX}}
Vanegas	MX	15.1	20.8	38%	{{XXX}}	{{XXX}}
Tula	MX	14.6	19.5	34%	{{XXX}}	{{XXX}}

As summarized below, even after spending $276 million in specific planned capacity-expanding line-of-road investments during Years 1-3, CPKC is likely to encounter significant train delays, due to a lack of capacity to handle the planned increase in trains on almost every subdivision. This appears to be the result of a disconnect in Applicants' operations planning processes, as described by CN witness Van Dyke in his Verified Statement. One of those

[21] Trains per Day, Base and Year 3: Application, Appendix A. Trains per Day by Subdivision, Vol 2, pp. 364-368; Non Bulk Base and Non Bulk Year 3: Oliver Wyman utilized the FD 36500 - Work Paper - HC - Trains Per Day and Gross Ton Miles - Working Copy with Haz Breakdown.xlsx file to get the percentage of trains that were bulk vs. non-bulk and applied it to the trains per day from Appendix A of the Application. *See* HC - Oliver Wyman Capex - Worksheet No. 2.

disconnects involves train counts by subdivision. The counts in Exhibit 3-4 include both organic and merger-related growth through Year 3 of the merger. However,the projected capital expenditures in Application's financial exhibits *exclude organic growth*. So, it is, at best, unclear whether Applicants' capital expenditure plan was sized to accommodate the {{XXX }} increase in GTMs resulting from organic and merger-related growth. What is clear, as described in Appendices B and C of this Verified Statement, is that Applicants' specified capital investment allocations to upgrade these lines is substantially inadequate. The result is that, by Year 3, CPKC is likely to experience significant train delays on most subdivisions.

In light of Applicants' projection that the combined CPKC system would see {{XXX }} growth in GTMs by Year 3, I could not understand why Applicants included *no capital expenditure for several lines where trains per day are scheduled to double*. From the joint deposition of CP witness Raymond Elphick and KCS witness John Orr,[22] the co-sponsors of Applicants' Operating Plan (Exhibit 13), I learned that {{XXX.}} Witness Elphick initially asserted that {XXX.}[23] However, upon further questioning, he {{XXX.}}

[22] HC - Remote Videotaped Deposition of Raymond A. Elphick and John F. Orr, STB Docket No. FD 36500, February 18, 2022. Terence M Hynes and Michael Rosenthal, representing Canadian National and Union Pacific, respectively, conducted the portions of the deposition cited in my testimony.

[23] HC - Remote Videotaped Deposition of Raymond A. Elphick and John F. Orr, STB Docket No. FD 36500, Elphick Deposition, pp. 71-74 and 93-97, Feb 18, 2022.

{XXX } Exhibit 3-5 sets forth a summary of the deposition testimony of witness Elphick regarding two of the subdivisions for which Applicants performed only such cursory capacity discussions. (*See* Appendix E for the full text of these discussions from the deposition.)

Exhibit 3-5: Elphick/Orr deposition extracts on the capacity assessment of KCS lines[25]

Rosenberg to Victoria		
{XXX}	{XXX}	{XXX}

Beaumont to Rosenberg		
{XXX}	{XXX}	{XXX}

[24] *Id.*
[25] *Id.*

Considering Applicants' planned investments to upgrade the St. Paul-Chicago-Beaumont line segment of their north-south line, I found that seven out of 15 subdivisions[26] and three at-grade crossings of busy BNSF or UP lines are likely to experience significant train delays and potential service disruptions without additional capital investment, for the following reasons:

- *More than {{XXX }} of the CPKC trains operating on {{XXX}} subdivisions will be 10,000 feet in length*.[27] This includes four subdivisions (the Chicago Subdivision and all three subdivisions in Mexico) on which *more than {{XXX }} of trains are*

[26] *See* Appendix C, subdivisions coded red in Tables B-1, B-3, and B-4.
[27] HC - Oliver Wyman - Capex Worksheet No. 2., s*ee* Summary tab.

projected to be 10,000 feet in length.[28] It is highly unlikely that those subdivisions currently have enough 10,000-foot sidings to maintain fluid service, given the anticipated increase in 10,000-foot trains, yet Applicants offer no specific plans to lengthen existing sidings or install additional sidings.

- The Application projects an *increase of 330 percent in trains operating on the Sabula to Kansas City mainline*, from an average of 4.3 trains per day at present to an average of 18.5 per day.[29] This line includes busy at-grade crossings with UP at Clinton, IA and with BNSF at Savannah, IL and Ottumwa, IA. UP and BNSF control those crossings, and each crossing is currently used by an average of 28-35 BNSF or UP trains per day.[30] Without capital investment to expand capacity at those locations, the massive increase in projected CPKC train movements at these busy crossings will threaten the fluidity of operations at each location.

- CPKC's planned route to/from Mexico, via the Laredo gateway, includes KCS trackage rights over two critical segments in Texas: UP's lines between Beaumont and Rosenberg, TX (a busy set of UP mainlines through Houston over which BNSF and Amtrak also operate trains) and between Victoria and Robstown, TX. *Applicants' operating plan contemplates that CPKC trains over these segments will more than double* – an increase from 7.7 trains per day to 16 trains per day between Beaumont and Rosenberg, and from 7.7 trains per day to 16.8 trains per day between Victoria and Robstown.[31] Applicants do not explain how CPKC will be able to add these trains on trackage they do not own (whether such increases are even permitted under the relevant trackage rights agreements and whether any additional capital investment would be required). Despite repeated requests, Applicants have not provided copies of the relevant trackage rights agreements with UP, which are necessary to determine whether CPKC will be permitted to double its daily trains over these lines without UP's concurrence, whether such concurrence has been granted, and, if so, what responsibility CPKC will have to fund capacity expansion of the lines to accommodate post-merger train activity. UP has expressed concern

[28] HC - Oliver Wyman - Capex Worksheet No. 2., *see* Summary tab.
[29] HC - Oliver Wyman - Capex Worksheet No. 1, *see* Other Calculations tab.
[30] Grade Crossing Inventory, FRA Office of Safety.
[31] Application Vol. 2, Appendix A, Trains Per Day by Subdivision, pp. 364-368.

regarding the Applicants' planned increase in traffic, stating that "their (the Applicants') Application, including their Operating Plan, should address all the consequences of the proposed transaction."[32]

Applicants' operating plan does not demonstrate that the increased CPKC traffic over the Beaumont-Rosenberg line will not interfere with operation of Amtrak's Sunset Limited intercity passenger service. Applicants are obligated to provide this proof.[33] UP echoes this concern, stating that "The Application does not support Applicants' claim that their proposed transaction will not adversely affect Amtrak."[34] Amtrak's Sunset Limited transits this busy corridor three times per week. With CPKC doubling its trains on this line segment and across the Neches River Bridge, there will be an increased risk of delaying this Amtrak train. CP's recent Agreement with Amtrak dated February 2022 does not address the Sunset Limited.[35]

- Despite the projected increase in post-merger traffic to and from Mexico, Applicants have *identified no planned capital projects to expand capacity on KCSM's lines in Mexico*. This is of particular concern because *more than {{XXX }} of CPKC trains, which will carry time-sensitive intermodal and automobile traffic, will move in 10,000-foot trains*. Additional siding capacity will be required to handle that traffic in Mexico.
- With the construction of Bensenville Yard not expected to be completed until 2025 (the presumed Year 3 of the CPKC merger), transfer movements between Bensenville and Schiller Park yards will likely increase significantly as (1) work is shifted to Schiller Park and back to Bensenville, to enable the rebuilding and expansion of Bensenville Yard; and (2) to accommodate the significant increase in Bensenville's workload due to organic and merger-related growth. Each transfer move between these two yards involves crossing the

[32] Union Pacific Railroad Company's Petition to Reject Application as Incomplete, STB Finance Docket 36500, p. 14.
[33] 49 CFR 1111.8(a)(2) (2000).
[34] Union Pacific Railroad Company's Petition to Reject Application as Incomplete, STB Finance Docket 36500, p. 15.
[35] Amtrak-Canadian Pacific Agreement, Section 6, conveyed to Cynthia T. Brown, Chief Section of Administration, Office of Proceedings, Surface Transportation Board, by letter from Sophia Ree, dated February 2, 2022.

tracks of two busy Metra commuter lines (the Milwaukee District West Service to Elgin and the North Central Service to Antioch) and a lengthy reverse move to Schiller Park. There is no evidence that any simulation studies were carried out to determine the impact of this increase in transfer movements on the quality of Metra's services, and in fact counsel for CP has said no modeling was done related to Metra. *See* Letter from David L. Meyer, Counsel for CP, to STB, Docket No. FD 36500 (filed Feb. 23, 2022). And there are no specified capital investment projects in Applicant's capital plan to mitigate or eliminate any impact on Metra's services.

- Other line segments have no planned investments. That includes line segments of the Springfield Line, for which CN is seeking a divestiture condition. When two railroads merge and have parallel lines, the concern is that the merged entity will concentrate investment on one, to the detriment of the other. That is what will happen here. CP is investing in its mainline between Kansas City and Chicago but has not identified *any* investments in KCS's parallel route between Kansas City and Springfield/East St. Louis.

3.2.2 Insufficient capital investment for yards, auto ramps/intermodal terminals, and bridges

Insufficient capital investment for key yards

The Application does not specifically allocate capital dollars during Years 1-3 to any yard in the CPKC system except CP's Bensenville Yard (and the amount of anticipated investment to expand Bensenville is not disclosed in the Application). However, *each of the following CPKC system yards is unlikely to have sufficient capacity to accommodate the increased workloads assigned to them* in Applicants' operating plan.

- Bensenville and Schiller Park (Chicago): Applicants' work papers project a completion date of 2025 for the rebuilding and expansion of Bensenville Yard and assert that the resulting capacity will be adequate to handle post-merger loading.[36] However, Applicants

[36] Kansas City Southern and Canadian Pacific's Joint Responses And Objections to Canadian National Railway Company's First Set Of Discovery Requests, Response to Request No. 100, STB Finance Docket 36500, p. 79.

provide no proof as to how they will handle a significant increase in post-merger yard work in a smaller space, following the sale of land to the Illinois Tollway to fund the rebuilding and expansion.

The merged system will be operating in Years 1-3 with Bensenville under construction and while the combined network is coping with an anticipated {{XXX }} in GTMs (including a 19.8 percent increase related to the merger). Much of this increase will consist of intermodal and automotive traffic that will flow through Bensenville and Schiller Park. There is no indication in the filing that Applicants did any capacity studies to see how Year 2 and 3 volumes would fit through the yard, how many additional transfers to Schiller Park would be required during this period, and, as mentioned above, how much delay this would cause for the two affected Metra lines.

- Shreveport: The operating plan indicates that Applicants plan to *more than double the number of trains moving through Shreveport, from 9.4 trains per day to 23.6 trains per day* (including originating, terminating, and through trains). The yard will be assigned 81 more cars to switch, 14 more blocks to make, and an unspecified increase in blocks to swap between trains. Through trains affect yard operations, because they occupy the mainline during crew changes.[37] It is virtually certain that the 30 yard tracks and mainlines at Shreveport in their current configuration will not be sufficient to handle the increase in workload (particularly in light of the fact that only one of the two mainlines adjacent to the yard can be used for originating/terminating and block swapping). Yet Applicants have not identified any planned capacity expansion at Shreveport yard.
- Wylie, Schiller Park, and St. Paul yards are each assigned more work in Applicants' post-merger operating plan. However, Applicants have not identified planned capacity expansion at any of those yards to accommodate the increased activity.

Further detail on the Bensenville, Wylie, Schiller Park, and St. Paul yards is provided in Appendix A.

[37] Orr and Elphick V.S., pp. 41, 43, 49, and 51

Insufficient capital investment for auto ramps and intermodal terminals

Applicants cite the ability to offer single-line service for northbound movements of imported containers and finished vehicles from Mexico as one of the primary benefits of the merger.[38] Yet the Application makes no provision for capacity expansion of any CPKC system auto ramps or intermodal facilities other than Bensenville and Schiller Park. Also, despite a projected increase in intermodal and automotive loadings from 27,272 and 4,364 pre-merger to 72,796 and 7,043 in Year 3 (168 percent and 62 percent increases, respectively), Applicants have designated no funding for expansion of their IFG intermodal and automotive terminal 24 miles south of Kansas City. Further detail on these intermodal and auto terminal expansion plans is provided in Appendix A.

Insufficient capital investment in key bridges

The Application does not identify capital spending for critical bridges that will be affected by projected traffic increases:

- KCS owns and operates a 20-mph single-track drawbridge over the Neches River in Beaumont, TX. The bridge is also used by BNSF, UP, and Amtrak trains. The Application projects that *CPKC daily train volume will more than double, from an average of 8.9 trains per day in the Base Year (2019) to 20.3 trains per day in Year 3*.[39] The need to replace this bridge – even at current traffic levels – has been noted by the

[38] Witnesses Brown & Zebrowski in their work papers show $125 million in autos from Mexico to Chicago interchange, Canada, Chicago, Twin Cities, and Kansas City. *See* the "Results" tab of HC - Diversion Identification work paper for Year 3 incremental revenue attached to their V.S.. They also have new moves of autos from Ontario to Kansas City and from the Gulf to Canada. Witnesses Wahba & Naatz in their work papers show an additional $16 million in autos from Guanajuato to Chicago interchange (35%), Chicago local (35%), Kansas City (10%), Toronto (10%), and Twin Cities (10%). *See* Row 10 in the HC - Growth Initiative Calculations work paper attached to their V.S.

[39] Application Vol. 2, Appendix A, Trains per Day by Subdivision, Beaumont Subdivision, pp. 364-368.

Texas Department of Transportation.[40] But the Application makes no provision for capital spending to increase the capacity of the existing bridge or to replace it.

- The KCS Bridge at Laredo, TX, which is used by both KCS and UP, is a critical link for traffic moving between Mexico and points in the United States and Canada. By Year 3, given the projected increase in trains crossing the bridge, congestion may become a problem. Construction of a second railroad bridge at Laredo has been approved by US Presidential permit, and KCSM believes the remaining three permits needed to begin construction will be obtained in time to begin construction at the start of 2023.[41] Yet the Application makes no provision for the cost of constructing a second bridge.

Applicants also make no mention of carrying out detailed capacity studies of the Neches Bridge to determine what capital investments will be needed to accommodate projected traffic growth.

3.2.3 Insufficient increase in revenue cars

The Application projects that CPKC will earn $1.021 billion of incremental revenues from: (1) post-merger traffic moving in {{XXX}} new units (carloads and containers) diverted from trucks and other railroads, and (2) {{XXX}} existing units that will have a longer length of haul.[42] These traffic diversions will generate a projected increase of 19.8 percent in GTMs.[43] Applicants posit that they will be able to handle this increase in GTMs with 2,002 fewer revenue cars, a 3.4 percent decrease.[44] Moreover, they plan to retire without replacement 833 general

[40] 2019 Texas Rail Plan, which cites bridge replacement as a long-range project (2023-2039), Texas Department of Transportation, Table 5-3, pp. 329-330.
[41] Federal Register:: Authorizing the Kansas City Southern Railway Company To Construct, Connect, Operate, and Maintain Railway Bridge Facilities at the International Boundary Between the United States and Mexico; "KCSM outlines projects for 2022," T21com.mx and Google Translate, January 11, 2022.
[42] HC - Oliver Wyman - Capex Worksheet No. 1, Carloads and containers growth tab.
[43] HC - Oliver Wyman - Capex Worksheet No. 1, GTM tab.
[44] Orr and Elphick V.S., pp. 71, 73-74, Calculation 2,002/59,405 =3.4%.

flatcars (including centerbeam flatcars) and 2,063 gondolas (including coil-steel cars), even as they experience an increase of 3,722 carloads[45] per year of forest products and 2,277 carloads per year of steel-related products.[46] In addition, no capital allocation has been made in the Application for revenue cars for projected organic growth. It seems unlikely that CPKC can accommodate a nearly {{XX }} increase in total GTMs from organic and merger-related growth simply by increasing the number of annual car turns with a smaller fleet, particularly given the significant increase in lengths of haul per load (and the need to return empties).[47]

3.2.4 Insufficient supply of new and rebuilt locomotives

The Application reflects an assumption that the merged CPKC will be able to move {{*XXX }} *more GTMs by Year 3* without acquiring any additional locomotives.[48]

The Application also appears to contemplate that *the average age of the combined CPKC locomotive fleet will increase significantly, from 16.5 years to 19.1 years*.[49] Applicants plan to continue with a locomotive rebuilding program. To maintain the current average fleet age of 16.5 years,[50] CPKC would need to rebuild approximately 90 road locomotives per year. However, Applicants' planned budget for locomotive rebuilding – one of the few specific capital projects identified in the Application – contemplates only 45 rebuilds per year. Moreover, Applicants plan to suspend their rebuilding program altogether during Years 1 and 2, and to reduce the pre-merger locomotive fleet by 135 units by temporarily storing the road locomotives that are the

[45] Orr and Elphick V.S., pp. 73-74. (124+73+1,397+372+97 = 2,063 gondolas) & (67+315+246+205 = 833 general flatcars).
[46] Brown and Zebrowski V.S., Application Vol. 2, pp. 157-158 (1,684+2,038 =3,722 carloads of forest products, 1,444+833 = 2,277 carloads of steel-related products).
[47] Orr and Elphick V.S., pp. 71 and 73-74.
[48] Orr and Elphick V.S., p. 68; HC - Oliver Wyman - Capex Worksheet No. 1, GTMs tab.
[49] HC - Oliver Wyman - Capex Worksheet No. 1, Locomotives tab.
[50] *Id.*

most expensive to operate during Years 1 and 2 – rather than rebuilding these units in anticipation of higher Year 3 traffic volumes. Applicants apparently plan to return 90 of these units (without rebuilding) to service in Year 3.[51] Taken together, these decisions will leave CPKC with a locomotive fleet that is older.[52] The likely consequence of this decision will be reduced locomotive reliability and increased maintenance expense.

In short, Applicants propose to handle an overall {{XXX }} increase in GTMs in Year 3 with a road locomotive fleet that is the same size as pre-merger,[53] but three years older than the current road locomotive fleet. With an older and less reliable locomotive fleet, Applicants' operating plan is likely to be more difficult to execute. While it may be possible to increase the length of some trains, depending on the length of sidings, the number of locomotives assigned to each train is a function of the weight of the train and ruling grades on a line, not the train's length in feet. Applicants' desire to increase many trains to a 10,000-foot configuration (the standard in CP's precision scheduled railroading (PSR) guidelines) might produce some increase in locomotive utilization, but only if trains are not currently using the full capacity of the locomotives assigned to them. In the work papers, Applicants appear to assume an increase in train speeds as the means to turn locomotives faster and improve utilization. But it is unlikely, even with an increase in train speeds, that the reduced locomotive fleet will be sufficient to handle a {{XXX }} increase in GTMs.[54]

[51] Orr and Elphick V.S. at p. 70 identify $45 million for locomotive rebuilds in Year 3. (Orr and Elphick V.S. at p. 70 identify $135 million for locomotive rebuilding but defer rebuilding of 90 locomotives in Years 1 and 2, saving $90 million. From this statement, I infer that the Applicants will spend $45 million to rebuild 45 locomotives in Year 3.)
[52] HC - Oliver Wyman - Capex Worksheet No. 1, Locomotives tab.
[53] Fleet size of 1,615 from Orr and Elphick, V.S., Table 6, p. 68.
[54] Orr and Elphick V.S., footnote 9 on p. 68; HC - Oliver Wyman - Capex Worksheet No. 1, GTMs tab.

4. Applicants Significantly Understate Operating Expenses By At Least $2 Billion and Project an Operating Ratio of 30 Percent for Merger-Related Traffic

Determining whether the incremental post-merger operating expenses projected by Applicants are in line with the projected increase in post-merger traffic is another important factor that the Board must assess in reviewing the viability of the proposed transaction. In past merger applications, applicants have employed a standardized modeling process to generate operating expenses based on projected changes in workload. Here, however, Applicants used a flawed and inaccurate approach to cost analysis and financial projections. As a result, Applicants have not shown that their operating expense estimates accurately reflect the cost of post-merger operations.

Indeed, Applicants' projected operating expenses for the first three post-merger years are understated by approximately $2.47 billion when compared to the operating expenses actually incurred by CP US and KCS US during the 2015-2019 period.[55] When compared to the average operating expenses incurred by the four largest Class I railroads (BNSF, UP, CSX, NS) between 2015 and 2019, Applicants' post-merger operating expense estimates appear to be understated by approximately $2.0 billion.[56] This represents an understatement of the merged railroad's operating expenses of approximately 10.7 to 12.9 percent of total operating expenses for those years.

The most significant flaws in Applicants' operating expense estimate include the following:

- Applicants did not base their estimate of incremental operating expenses on the analyses or outputs of their operating plan or system model. Instead, Applicants based their

[55] Analysis of US Class I Railroads – years 2015 to 2019, Association of American Railroads. *See* Oliver Wyman Opex Worksheet.
[56] *Id.*

estimate solely on a table of incremental operating expenses that is hard-coded into an unsourced spreadsheet in Applicants' work papers.[57] In other words, while Applicants submitted the veneer of an operating expense development process (including a purported MultiRail analysis of post-merger operations), the operating expenses reflected in the Application are nothing more than assumptions that are unsupported by documentation or analysis.

- Applicants' incremental post-merger operating expenses are clearly not credible, given their projected increase in post-merger traffic volumes. Comparing Base Year 2019 to Year 3 of the merged system, Applicants claim that the merged CPKC will incur only $306.3 million[58] in incremental operating expenses, an increase of only 5.67 percent over the Base Year, even though they project an increase of 19.8 percent in GTMs in Year 3.[59]

- Applicants project that this new business will generate $1,021.9 million in additional revenues.[60] Based on their projected incremental operating expenses of $306.3 million, this equates to a 70 percent flow-through of revenue to operating income, or a *projected operating ratio of only 30 percent for the incremental traffic*.[61] That is far lower than any operating ratio ever achieved by any Class I railroad in North America on either baseload or incremental traffic.[62] This strongly suggests that Applicants' operating expenses are greatly understated.

- Applicants' claimed operating cost savings are projected to occur in an unrealistically accelerated time frame. Specifically, *Applicants assume that $93.5 million, or 80.8 percent, of the total projected $115.7 million savings in operating expenses will be*

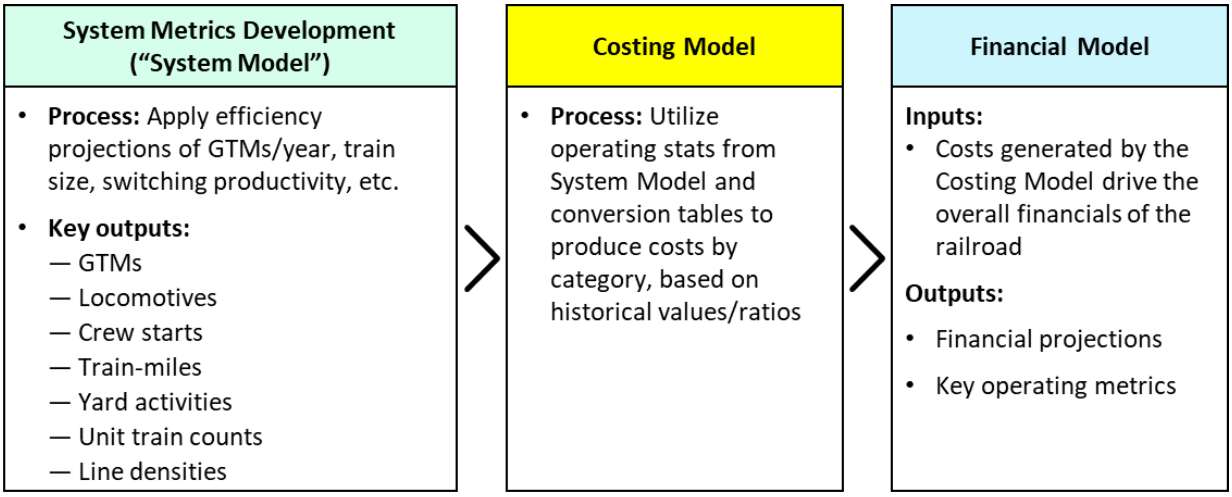
[57] FD 36500 – Work Paper - STB Rail Road Control Application Model – Final.xlsx, Inputs – revenues + costs tab.
[58] *See* Application Vol. 1 at 427. Elsewhere in the Application (Vol. 1 at 140), Applicants state that Year 3 operating expenses would be even lower, at $282 million. Nowhere in the filing is this discrepancy explained.
[59] Application Vol. 2, Table 2, p. 287. Base Plan GTMs = 385.6 billion, Growth Plan GTMs = 461.9 billion, Growth =19.8 percent. The 5.67% increase was calculated by dividing $306.3M by $5.4 billion. *See* Oliver Wyman Opex worksheet for calculation.
[60] Application Vol. 1, Appendix B. Summary of Benefits, p. 74.
[61]The 30 percent incremental traffic operating ratio is calculated by taking $306.3 million divided by 1,021.9 million.
[62] 2020 operating ratio range for Class I railroads: 60.7 to 73.6 percent, from Railroad Facts, 2020 Edition, Association of American Railroads. *See* Oliver Wyman Opex Worksheet.

achieved in Year 1 post-merger. For transportation, fuel-related, and locomotive leasing/depreciation cost savings, Applicants assume that fully 96.5 percent will be realized in Year 1.[63] Since CP cannot begin to physically integrate its network with KCS or influence KCS operations until the merger is approved, it is unlikely that Applicants would be able to implement all of the operating changes required to generate virtually all of the achievable operating expense savings in the first post-merger year.

4.1 The methodology employed by Applicants to estimate post-merger operating expenses is flawed and opaque

Exhibit 4-1 illustrates the logical and typical sequence of steps involved in preparing complete and accurate operating expense projections.

Exhibit 4-1: Logical process for developing accurate post-merger operating statistics and financial projections



As described in Exhibit 4-1, in past merger proceedings, applicants:

- First produced estimates of **traffic growth**, which were then added to the carriers' pre-merger traffic base to produce an estimate of traffic that would be handled by the merged railroad.
- The estimated post-merger traffic file was then input into an **operations planning model** to develop an operating plan for the merged railroad. (MultiRail, which Applicants

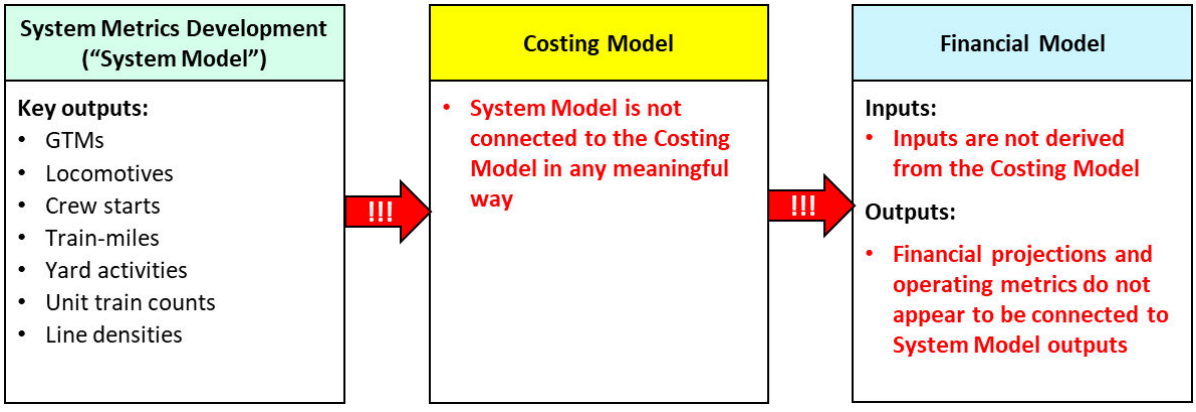
[63] FD 36500 – Work Paper - STB Rail Road Control Application Model – Final.xlsx, CPKC Summary of Benefits tab; Oliver Wyman Opex worksheet.

purport to have used in planning for this merger, is one such model that has been used for that purpose in many prior merger proceedings.) The resulting operating plan identifies the number of trains and the level of yard activity required to handle post-merger traffic efficiently.

- Prior merger applicants then used a **system model** to derive operating statistics (such as GTMs, train-miles, crew starts, etc.) from the operating plan.
- The operating statistics produced by the system model were then input to a **costing model**, where they were converted into projected operating expenses based on the historic relationship of each category of operating expense with projected changes in operating activity, as represented by projected changes in GTMs.
- The projected operating expenses, in turn, were input to a **financial model** to develop pro forma financial statements for the post-merger period.

As illustrated in Exhibit 4-2, Applicants here did not apply a logical process capable of producing credible and complete operating expenses for the merged CPKC system. As a result, Applicants have failed to prove that they have adequately accounted for the incremental operating costs that they would incur in moving their projected {{XXX }} increase in GTMs by the end of Year 3.

Exhibit 4-2: Applicants' approach to developing projected post-merger operating statistics and financial projections



As CN witness Van Dyke describes in greater detail, Applicants' operating plan, from which operating expenses should have been derived, is seriously flawed.[64] In the normal planning process, the merged carrier's projected traffic is flowed through a model of the railroad's network (for example, in MultiRail) to project post-merger train-miles, car handlings, etc., which are the fundamental building blocks used to estimate railroad operating expenses. However, Applicants did not follow that logical (and time-tested) process here. Instead, final values for each incremental operating expense category simply appear as hard-coded numbers in a table found in Applicants work papers (shown in Exhibit 4-3).[65]

[64] As witness Carl Van Dyke explains, "Applicants appear to have intentionally decided to develop their operating plan and operating expenses separately. Applicants' post-merger operating plan includes both 'synergy growth' traffic from their traffic diversion studies and 'organic growth' (growth resulting from general economic conditions unrelated to the proposed merger). On a systemwide basis, Applicants' posit organic growth in traffic volumes of {{XXX}} percent increase from the Base Year to post-merger Year 3.However, in calculating the merged CPKC's operating expenses, Applicants considered only 'synergy growth of 19.8%' traffic and excluded 'organic growth' traffic. It is not clear why Applicants took this inherently contradictory approach. What is clear is that the resulting operating expenses do not account for the cost of handling the {{XXX }} increase in 'organic growth' traffic. As a result, their claimed operating expenses bear no relation to their operating plan." Verified Statement of Van Dyke at 5.

[65] FD 36500 – Work Paper - STB Rail Road Control Application Model – Final.xlsx, inputs – revenues + costs tab.

Exhibit 4-3: Hard-coded CPKC traffic, revenue, expense, and profit projections[66]

	Year 1 (2023)	Year 2 (2024)	Year 3 (2025)
Diverted Carloads/Units			
Automotive	{{XXX}}	{{XXX}}	{{XXX}}
Energy, chemicals, and plastics	{{XXX}}	{{XXX}}	{{XXX}}
Forest products	{{XXX}}	{{XXX}}	{{XXX}}
Grain	{{XXX}}	{{XXX}}	{{XXX}}
Domestic intermodal	{{XXX}}	{{XXX}}	{{XXX}}
International intermodal	{{XXX}}	{{XXX}}	{{XXX}}
Metals, minerals, and consumer products	{{XXX}}	{{XXX}}	{{XXX}}
Total	**195,093**	**351,620**	**509,490**
Incremental Revenues			
Automotive	{{XXX}}	{{XXX}}	{{XXX}}
Energy, chemicals, and plastics	{{XXX}}	{{XXX}}	{{XXX}}
Forest products	{{XXX}}	{{XXX}}	{{XXX}}
Grain	{{XXX}}	{{XXX}}	{{XXX}}
Domestic intermodal	{{XXX}}	{{XXX}}	{{XXX}}
International intermodal	{{XXX}}	{{XXX}}	{{XXX}}
Metals, minerals, and consumer products	{{XXX}}	{{XXX}}	{{XXX}}
Total	**$418.0M**	**$726.7M**	**$1021.9M**
Incremental Costs			
Automotive	{{XXX}}	{{XXX}}	{{XXX}}
Energy, chemicals, and plastics	{{XXX}}	{{XXX}}	{{XXX}}
Forest products	{{XXX}}	{{XXX}}	{{XXX}}
Grain	{{XXX}}	{{XXX}}	{{XXX}}
Domestic intermodal	{{XXX}}	{{XXX}}	{{XXX}}
International intermodal	{{XXX}}	{{XXX}}	{{XXX}}
Metals, minerals, and consumer products	{{XXX}}	{{XXX}}	{{XXX}}
Total	**$129.2M**	**$217.8M**	**$306.3M**
Incremental Profits			
Automotive	{{XXX}}	{{XXX}}	{{XXX}}
Energy, chemicals, and plastics	{{XXX}}	{{XXX}}	{{XXX}}
Forest products	{{XXX}}	{{XXX}}	{{XXX}}
Grain	{{XXX}}	{{XXX}}	{{XXX}}
Domestic intermodal	{{XXX}}	{{XXX}}	{{XXX}}
International intermodal	{{XXX}}	{{XXX}}	{{XXX}}
Metals, minerals, and consumer products	{{XXX}}	{{XXX}}	{{XXX}}
Total	**$288.9M**	**$508.8M**	**$715.6M**

[66] *Id.*

Applicants provide no explanation in the Application or supporting work papers describing how these total incremental operating expense figures were derived. All that can be discerned from Applicants' submission is that witness Baranowski's costing assumptions (see Section 4.2 below) result in an extremely low level of incremental operating costs per GTM in relation to projected incremental revenues.

4.2 Applicants' operating expense estimate omits some expenses and underestimates others

Applicants' Verified Statement of witness Baranowski describes how he estimated incremental operating expenses for the merged railroad.[67] According to witness Baranowski, Applicants' outside experts and internal marketing executives collectively estimated the number of incremental carloads that would be added to the merged railroad's traffic base during the first three years following the merger.[68] To estimate Year 1-3 incremental operating expenses, witness Baranowski then employed a costing methodology that assigned only *short- and medium-term* incremental operating expenses to the projected *long-term* increase in traffic. Specifically, witness Baranowski excluded depreciation from his operating expense calculations. This is a major flaw in Applicants' operating cost calculations, given that depreciation accounted for fully 19 percent of Class I railroad expenses in 2020.[69]

[67] Baranowski describes his costing methodology in Electronic Work Paper "Incremental URCS Unit Costs.xlsx," which describes his allocation of Transportation, Mechanical and MOW expenses to activity statistics; Electronic Work Paper "URCS Diversion Costing Metrics Adjustments.xlsx," which describes his methodology for deciding what costs to include in his definition of incremental costs to handle incremental carloads, and Electronic Work Paper "URCS Phase III Calculation for Growth Traffic.xlsx, Tab Final Summary."
[68] A description of these traffic growth projections, also prepared by Applicants using a deeply flawed process, is provided in the Verified Statement of David Hunt.
[69] Railroad Facts 2021, Association of American Railroads, p. 11.

The incremental operating expenses for Years 1-3 developed using the methodology employed by witness Baranowski[70] are artificially low due to his omission of depreciation and certain other recognized categories of operating expenses (summarized as "Unspecified" in Exhibit 4-4 below). As a result of those omissions, the unreasonably low level of operating expenses projected by Applicants are highly unlikely to be achieved during any year of the merger, and certainly will not be sustainable over the long term. The unrealistic nature of the amounts and allocation of incremental operating expenses for each functional category developed by witness Baranowski can be seen by comparing witness Baranowski's calculations with the allocation of operating expenses by Class I railroads as a group, by CP (for its US operations), and by KCS (for its US operations), as shown in Exhibit 4-4. Neither Applicants (nor witness Baranowski) attempt to explain how (or why) the merged CPKC's operating costs would be so markedly different from industry norms – *including the Applicants' own real-world experience*.

Exhibit 4-4: Comparison of allocation of incremental operating expense by function [71]

Category	CPKC Year 3		2015-2019 Average % for:		
		% of Total	US Class I's	CP (US)	KCS (US)
Maintenance of way	$38.8M	13%	21%	30%	23%
Maintenance of equipment	$37.0M	12%	20%	11%	22%
Transportation	$230.5M	75%	46%	43%	41%
Unspecified	$0M	0%	13%	16%	14%
Total	$306.3M	100%	100%	100%	100%

[70] Application Vol. 1, p. 427.
[71] Verified Statement of Michael Baranowski, Application Vol. 1, p. 427; Source for CP US, KCS US, Class I's (includes all US Class I's): Analysis of US Class I Railroads – years 2015 to 2019, Association of American Railroads. Calculations are included in the Oliver Wyman Opex Worksheet.

As the breakdown of operating expenses in Exhibit 4-4 clearly demonstrates, *witness Baranowski's calculations ignored general and administrative expenses altogether and significantly underestimated maintenance of way and maintenance of equipment expenses*. As discussed above, he also accounted only for short- to medium-term operating expenses, thereby omitting depreciation. While witness Baranowski does not provide an explanation for his functional allocation of operating expenses, it is likely that omitting depreciation contributed to his underestimate of maintenance of way and maintenance of equipment expenses. Both of those categories account for a disproportionate share of depreciation expense relative to other railroad operating expense categories.[72]

In an asset-intensive business such as the railroad industry, projecting an increase in long-term revenues without also accounting for the associated long-term expenses (including depreciation) required to renew the railroad's assets will ultimately lead to the demise of the business. Applicants' flawed approach, which assumes $306.3 million in incremental operating expenses, equal to only 30 percent of incremental revenues, results in a projected 70 percent flow-through to operating income, a level of performance that (I believe) has never been achieved by any North American Class I railroad.

4.3 Large operating expense savings claimed for the first year of the merger are unlikely to be realized

Applicants' estimated operating expense savings attributable to the merger are unrealistically front-loaded, which has the effect of inflating Applicants' projection of operating income. Specifically, Applicants assume: (1) that 80.8 percent of the total three-year merger-

[72] 2020 Class I average: Maintenance of way: 25%, Maintenance of equipment: 20%, Transportation: 41%, Unspecified: 13%. *See* Oliver Wyman Opex Worksheet.

related savings of $115.7 million (including 96.5 percent of assumed transportation/fuel/locomotive savings of $92.5 million) will be achieved in the first year of the merger as KCS's operations are "optimized" and integrated with CP's, and (2) that subsequent productivity improvements of $23.1 million (primarily purchasing efficiencies) will be realized in Years 2 and 3 of merged operations.[73]

Without identifying what specific expense reduction measures would be implemented in Year 1, witness Baranowski assumes that CPKC will realize this extremely high percentage of total projected operating expense savings during the first year of the merger, (supposedly) by implementing CP's precision scheduled railroading (PSR) on KCS.[74] This aggressive assumption ignores the fact that a significant portion of the implementation of PSR has *already been realized by KCS without the merger*. Beginning in January 2019, KCS commenced an aggressive initiative to implement PSR, which helped to reduce its operating ratio from 69.1 percent in 2019 to 62.2 percent in 2020.[75] As stated in KCS's Q4 2020 Consolidated Investor Report:

> "During 2020, the KCS network experienced a rapid decline in volumes followed by an unprecedented volume rebound, forcing the Company to quickly adjust its service model to match customer demand while optimizing its cost structure. These actions resulted in significant improvements to train length and fuel efficiency, improving 12% and 5%, respectively. *PSR initiatives also contributed directly to operating expense savings of $96 million in 2020 and are projected to deliver incremental savings of $50 million in 2021.*"[76]

Given that KCS has largely implemented PSR, , and that CP already employs PSR on its own network, it is simply not realistic to assume that the merged CPKC can realize an additional

[73] Baranowski V.S., Table 9, p. 11. Calculations are included in Oliver Wyman Opex Worksheet.
[74] Orr and Elphick, V.S., p. 38, where they state that "CP's long experience with PSR….informed the approach to designing a consolidated plan for CP/KCS."
[75] "Kansas City Southern Announces EVP Precision Scheduled Railroading Sameh Fahmy Will Leave the Company," Business Wire, October 13, 2021; KCS Consolidated Investor Report Q4, Kansas City Southern, January 22, 2021, p. 6.
[76] Consolidated Investor Report Q4, Kansas City Southern, January 22, 2021, p. 3.

$92.5 million in transportation, fuel, and locomotive savings from the merger, much less almost entirely during Year 1. Changes in operations (and related operating expense savings) do not happen overnight. Whatever additional incremental PSR efforts might be launched on Day 1 of the merged operations will almost certainly take months to implement – indeed, rushing the implementation of major operational changes could lead to substantial service failures, as has happened in connection with previous Class I mergers, such as the UP/SP merger.

As described in the operating plan, key claimed cost savings will require operating changes that will need to be planned and implemented, such as:

- Work will need to be transferred from Kansas City to Shreveport and St. Paul.[77]
- Clerical and dispatching activities will need to be moved from St. Paul to Kansas City.[78]
- Labor agreements and crew rosters will almost certainly need to be adjusted and/or renegotiated before changes to workloads and work activities can be implemented.[79]
- T&E and Mechanical personnel will need to be relocated and qualified to operate over new territories.[80]
- New blocking plans will need to be developed and put in place.[81]
- New locomotive distribution, servicing, and fueling plans will need to be implemented.[82]

[77] Orr and Elphick V.S., pp. 34-36.
[78] Verified Statement of Dean Vargas, p. 5.
[79] Verified Statement of Myron W. Becker, p. 10; Exhibit E of the Operating Plan (pp. 350-361) shows the pre- and post-merger locations of each category of employee.
[80] Orr and Elphick V.S., pp. 40-52 describe CPKC's changes in train and yard operations post-merger, many of which will require changes in domiciles for T&E and Mechanical personnel.
[81] Orr and Elphick V.S., p. 34.
[82] Orr and Elphick V.S., pp. 40-52 and 67 describe the many changes in train operations for CPKC operations. In preparation for implementation of merged operations, locomotive domiciles will need to be changed so they will align with new train plans, Mechanical personnel will need to be repositioned so that they are aligned with the train plan's fueling and locomotive servicing requirements. Exhibit E of the Operating Plan shows the locations of operating employees pre- and post-merger.

Given these and other measures that must be undertaken to merge the operations of CP and KCS, Applicants' claim that fully 80 percent of the total operating expense savings will be achieved during Year 1 is simply not credible. In my opinion, Applicants' assumption that the merged system can realize 80 percent of total three-year operating expense savings during the first post-merger year is unrealistic, especially given that KCS has already largely implemented PSR.

4.4 Applicants' projected Year 1-3 operating expense projections are further belied by industry benchmarks

To further assess the reasonableness of Applicants' projected operating expenses, I examined the historical relationship between operating expenses, gross-ton miles, and revenues for the four largest Class I railroads (BNSF, CSX, NS, and UP) and for CP's US operations and KCS's US operations based on the 2015-2019 period. I compared those figures to the projected revenues, GTMs, and operating expenses for the combined CPKC (as reflected in the Application and work papers).[83] As Exhibit 4-5 shows, when compared to the average operating expenses per GTM achieved by the four largest Class I railroads – *and by Applicants themselves in their real-world operations* – the projected operating expense per GTM for CPKC of $0.0126 during the first three post-merger years is well below historical benchmarks.

[83] Analysis of US Class I Railroads – years 2015 to 2019, Association of American Railroads; FD 36500-Work Paper- HC- Cost Metrics Growth Model_ Base year 2019; FD 36500 – Work Paper - STB Rail Road Control Application Model – Final.xlsx.

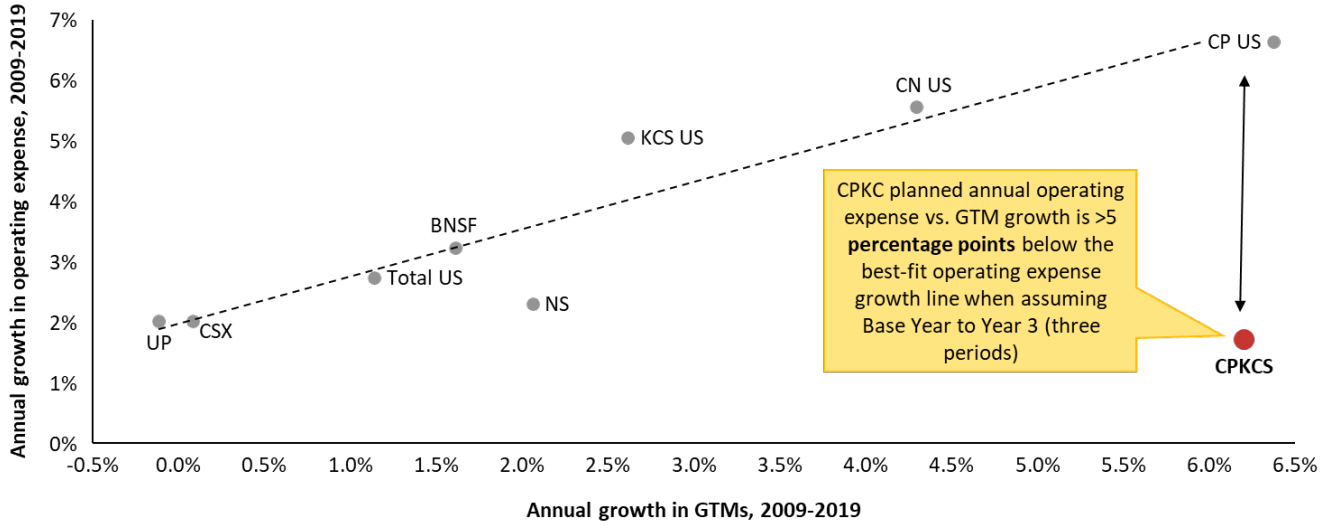
Exhibit 4-5: Operating expense per GTM comparison[84]

Railroads	Average Operating Expense per GTM 2015-2019	Projected Operating Expense per GTM	Percentage Difference
US Four Largest Class I's (BNSF, CSX, NS, UP)	$0.0141	$0.0126	10.7% Less
CP (US) and KCS (US)	$0.0145	$0.0126	12.9% Less

Another way to illustrate the unrealistically low operating expense per GTM posited by Applicants is shown in Exhibit 4-6, which shows changes in operating expense per GTM for all of the Class I railroads between 2009 and 2019. Again, this analysis strongly suggests that Applicants have significantly underestimated the operating expense per GTM that the combined CPKC system is likely to experience.

Exhibit 4-6: Change in operating expense vs. change in GTMs, CPKC plan vs. historical data for US Class I railroads[85]

CPKC: Scatterplot measures change between Year 0 (2019) and Year 3; Class I benchmark measures change between 2009 and 2019. CPKCS: 3-Year CAGR; benchmarks: 10-Year CAGR



[84] Analysis of US Class I Railroads – years 2015 to 2019, Association of American Railroads; FD 36500-Work Paper- HC- Cost Metrics Growth Model_ Base year 2019; FD 36500 – Work Paper - STB Rail Road Control Application Model – Final.xlsx. Operating expense includes amortization and depreciation. Calculations are included in the Oliver Wyman Opex Worksheet.
[85] FD 36500-Work Paper- HC- Cost Metrics Growth Model_ Base year 2019; FD 36500 – Work Paper - STB Rail Road Control Application Model – Final.xlsx Analysis of US Class I Railroads

In addition to operating expense per GTM, another common way to measure financial performance in the rail industry is the operating ratio (operating expense as a percentage of revenue). As shown in Exhibit 4-7, the implied operating ratio for CPKC's post-merger incremental traffic (based on the incremental revenues and operating expenses set forth in the Application) is far below the historic norms for the US operations of Applicants themselves, and for the US Class I railroads as a group.

Exhibit 4-7: Comparison of historic average operating ratios with Applicants' projection[86]

Railroads	Average Operating Ratio 2015-2019	CPKC Projected Operating Ratio	Percentage Difference
Four Largest Class I's (BNSF, CSX, NS, UP)	67%	58%	13.3% Less
CP (US) and KCS (US)	69%	58%	16.2% Less

4.5 The shortfall in Applicants' projected operating expenses is substantial

As shown in Exhibit 4-5 above, the operating expense per GTM estimated by witness Baranowski and incorporated in the Application is well below "real-world" levels achieved by the Class I railroads and by CP and KCS themselves. Based on these benchmarks, Applicants' total projected operating expenses for the first three years of operation are greatly understated.

– years 2015 to 2019, Association of American Railroads; Oliver Wyman analysis. Total for US Class I's includes CSX, UP, BNSF, NS, KCS (US), CP (US), CN (US). Calculations are included in Oliver Wyman Opex Worksheet.

[86] Note: Applicants projected operating expense by year: $5.4 billion in Year 1, $5.56 billion in Year 2, and $5.69 billion in Year 3. FD 36500-Work Paper- HC- Cost Metrics Growth Model_ Base year 2019; FD 36500 – Work Paper - STB Rail Road Control Application Model – Final.xlsx; Analysis of US Class I Railroads – years 2015 to 2019, Association of American Railroads. Calculations are included in the Oliver Wyman Opex Worksheet.

Exhibit 4-8: Adjustments to Application operating expenses based on comparison to four largest Class I's and CP (US and KCS (US), 2015-2019[87]

Railroads	Project Operating Expense CPKCS	Dollar Understated	Percentage Understated
US Four Largest Class I's (BNSF, CSX, NS, UP)	$16.70B	$2.00B	-10.7%
CP (US) and KCS (US)	$16.70B	$2.47B	-12.9%

Indeed*, as Exhibit 4-8 shows, based on Applicants' own pre-merger operations, operating expenses for the CPKC system in the US during Years 1-3 are understated by $2.47 billion.* This benchmark is the best benchmark, because it reflects the particular characteristics of Applicants' networks and traffic bases in the United States.

[87] FD 36500-Work Paper- HC- Cost Metrics Growth Model_ Base year 2019; FD 36500 – Work Paper - STB Rail Road Control Application Model – Final.xlsx; Analysis of US Class I Railroads – years 2015 to 2019, Association of American Railroads. Calculations are included in the Oliver Wyman Opex Worksheet.

VERIFICATION

I, Hugh Randall, declare under penalty of perjury that the foregoing information is true and correct. Further, I certify that I am qualified and authorized to file this statement.

Executed on this 28th day of February, 2022.

Hugh Randall

Hugh Randall

Appendix A. Yard Capacity Assessment

- Bensenville (Chicago): The Applicants do not provide sufficient information concerning the redesign of Bensenville Yard on less land (some having been sold to the Illinois Tollway) to prove that it will be able to handle:
  - For manifest trains, the switching of 112 additional cars/day (an 11 percent increase from the Base Case) and the preparation of four more blocks per day.[88]
  - For intermodal trains, construction of a high-volume terminal capable of handling 10,000-foot trains; the grounding/loading of 274 intermodal cars, a 213 percent increase; and an increase in lifts of 548 per day.[89]
  - For finished autos, construction of a new facility to handle 76 multilevel autoracks per day, compared to three autoracks per day in the optimized plan,[90] including the storing of hauled automobiles until they can be moved out of the yard by auto-carrier trucks.
- Wylie: The capital plan assumes that Wylie's volume will increase by 52 percent (292 cars/containers per day).[91] The Applicants do not provide sufficient information to prove that the existing facility will be able to handle this increase in volume.
- Schiller Park East (Chicago): The capital plan includes new intermodal trains connecting Mexico with Detroit and Eastern Canada. The trains to/from Mexico will originate/terminate in Bensenville Yard; the trains to/from Detroit/Eastern Canada will originate/terminate in Schiller Yard, 4.5 miles from Bensenville. Moving blocks between these yards is very complex, involving a simultaneous crossing of two Metra lines and carrying out a reverse move for more than a mile.[92] The Application is silent as to the number of additional transfers that will be needed and the volumes of intermodal cars that will need to be moved. The Applicants fail to demonstrate that, given their plan for

[88] Orr and Elphick V.S., p .49.
[89] Orr and Elphick V.S., p. 49 Lifts equals 274 cars times 2 containers per car.
[90] Orr and Elphick V.S., p. 49.
[91] Orr and Elphick V.S., p. 89.
[92] Google Maps; CN Timetable No. 3 for Central Division, July 1, 2020.

handling intermodal traffic, Schiller Park Yard will have the capacity to handle this increased workload without capital expenditure. The Applicants also fail to demonstrate that the planned increase in intermodal units being transferred will not adversely affect Metra's commuter operations, as required by 49 CFR 1111.8(a)(2) (2000).

- St. Paul: While the yard tracks may be able to handle the proposed increase in switching of 69 cars/day,[93] the Applicants do not provide the information necessary to prove that the yard will have enough mainline and receiving/departure tracks to handle an increase of:
  - {{XXX }} in non-bulk trains/day to be made up and taken apart (from an average of {{XXX}} in 2019 to an average of {{XXX}} in Year 3); and
  - {{XXX }} in bulk (largely oil and grain) unit trains/day in each direction moving between Western Canada, the Gulf of Mexico, and Mexico (from an average of {{XXX}} in 2019 to an average of {{XXX}} in Year 3), whose crews will need to change adjacent to St. Paul Yard.[94]

[93] Orr and Elphick V.S., p. 49.
[94] HC - Oliver Wyman - Capex Worksheet No 2, Summary tab.

Appendix B. Subdivision Capacity Assessment

B.1 CP Line: St. Paul, MN/Elgin, IL to Kansas City, MO

This CP line, used infrequently pre-merger, ends in Kansas City, the only place where CP and KCS connect. It will become a critical link in the route that CPKC plans to use to operate new single-line services between Mexico and the Gulf Coast to the Upper Midwest and Eastern and Western Canada. To move the more than {{XXX}} new units of freight that CPKC projects will be diverted from trucks and other railroads through the merger,[95] *train volumes on this route are expected to increase by 330 percent*, from 4.3 per day to an average of 18.5 per day.[96] To handle this massive increase in trains, CP plans to invest more than $276 million to upgrade this line,[97] as well as the KCS line from Kansas City to Beaumont, TX, with most of this investment being allocated to extending existing sidings and building new sidings. The planned increase in train volumes is expected to consist of approximately {{XXX }} of 10,000-foot intermodal/automotive/merchandise trains and {{XXX }} of 7,300-foot unit oil and grain trains.[98]

Using CP's methodology for estimating line capacity (described in Appendix C), I assessed the post-merger and post-capex operating capacity for each of the six subdivisions on the line. The results of my capacity simulations, using the same methodology applied by CP, are summarized in the exhibits below, with the relative severity of each subdivision's capacity issues, based on the projected increase in Year 3 trains per day, color-coded (**red** = most severe –

[95] HC - Oliver Wyman - Capex Worksheet, No. 1, Carloads and Containers Growth tab.
[96] HC - Oliver Wyman - Capex Worksheet No. 1, Other Calculations.
[97] Orr and Elphick V.S., p. 84.
[98] HC - Oliver Wyman - Capex Worksheet No. 1, Other Calculations.

will exceed practical capacity; **orange** – will be at practical capacity; **green** – will be less than practical capacity).

Exhibit B-1: CP Line from Elgin, IL/St. Paul, MN to Kansas City

Subdivision	Miles[99]	Speed Limits (mph)[100]	Base Year Trains/Day[101] % Bulk vs Non-Bulk	Year 3 Trains/Day[102] % Bulk vs Non-Bulk	Year 3 CPKC Capacity Issues
Chicago	101	Avg: 33 Max: 40	2.9 {{XXX }} {{XXX }}	11.1 {{XXX }} {{XXX }}	11.1 trains/day = 100% of estimated practical capacity in this subdivision
Special Considerations	CP crosses a BNSF mainline in Savanna, IL. BNSF controls this "first-come, first-served" automated crossing; speed for both RR's at the crossing is 25 mph; 32 BNSF trains/day.[103] Large increase in CPKC trains likely to cause more train delays				
Marquette	159	25-35	7.7 {{XXX }} {{XXX }}	14.3 {{XXX }} {{XXX }}	27 miles between Eckard &Harpers Ferry, practical capacity 13.3 trains/day 45 miles between Harpers Ferry & Brownsville, practical capacity 8.9 trains/day
Special Considerations	CP operates over CN for 1.6 miles in Dubuque, IA; speed limit of 25 mph; CN's train volume was 11/day in 2016.[104] With CPKC's increase in train frequency, delays likely to increase				
Davenport	55	40	7.1 {{XXX }} {{XXX }}	21.6 {{XXX }} {{XXX }}	27 miles Camanche to Bettendorf with a practical capacity of 13.7 trains/day
Special Considerations	7.3 mile segment between Camanche and Deer Creek, including crossing of UP mainline in Clinton, IA; 20 mph limit across 6 of these 7 miles, UP operates 33-35 trains/day[105] and controls this crossing. Large increase in CPKC trains/day likely to result in increased train delays				
Ottumwa	107	40	4.2 {{XXX }} {{XXX }}	18.4 {{XXX }} {{XXX }}	Estimated practical capacity for the entire subdivision is 16.7 trains/day
Special Considerations	CP crosses BNSF at Ottumwa. BNSF dispatcher controls this crossing and BNSF operates 26 trains/day; Amtrak operates an additional 2 trains/day.[106] Addition of CPKC trains likely to increase train delays				
Laredo	102	40	3 {{XXX }} {{XXX }	17 {{XXX }} {{XXX }}	39.2 mile segment between Moravia & Powersville with a practical capacity of 12.2 trains/day

[99] Oliver Wyman CP Capacity Analysis Worksheet.
[100] *Id.*
[101] HC - Oliver Wyman - Capex Worksheet No. 2, Summary tab.
[102] *Id.*
[103] *See* FRA Office of Safety – Grade Crossing Inventory document.
[104] *See id.*
[105] *See id.*
[106] *See id.*

Subdivision	Miles[99]	Speed Limits (mph)[100]	Base Year Trains/Day[101] % Bulk vs Non-Bulk	Year 3 Trains/Day[102] % Bulk vs Non-Bulk	Year 3 CPKC Capacity Issues
Kansas City	94	40	2.9 {{ }} {{ }}	16.9 {{ }} {{ }}	25.8 mile segment between MP 431 to Polo with a practical capacity of 18 trains/day

Exhibit B-2: KCS Line from Kansas City to Beaumont, TX

Subdivision	Miles[107]	Speed Limits (mph)[108]	Base Year Trains/Day[109] % Bulk vs Non-Bulk	Year 3 Trains/Day[110] % Bulk vs Non-Bulk	Year 3 Capacity Issues
Pittsburg	123	55	13.5 {{ }} {{ }}	28.5 {{ }} {{ }}	Operating 29.1 trains will utilize 96% of the line's capacity in the 20.4 miles between Jaudon and Drexel and more than 80% between Amsterdam & Mulberry
Heavener	209	55	11.3 {{ }} {{ }}	25.9 {{ }} {{ }}	Even for 7,300-foot trains, capacity will be 96% utilized for 18 miles between Marble City & Gans and 89% utilization for 15.8 miles between Joplin and Dalby
Shreveport	209	55	9.4 {{ }} {{ }}	23.6 {{ }} {{ }}	In the 24-mile section between Rich Mountain & Potter, capacity will be at 95% utilization; between Jury and Sandra, utilization will reach 87%
Beaumont	205	55/59	8.9 {{ }} {{ }}	20.3 {{ }} {{ }}	In the 28-mile section between Hollywood & Mansfield, 20.3 trains/day will utilize 92% capacity; the 25-mile section between Neame/Singer capacity will reach 85%

B.2 KCS Line – Beaumont, TX to Laredo, TX

KCS's route from Beaumont to Laredo includes two line segments over which KCS operates using trackage rights over UP lines. These operations occur between Beaumont and Rosenburg, TX and between Victoria and Robstown, TX. The route also includes two line segments on KCS-owned track between Rosenburg and Victoria, TX and between Robstown and

[107] Oliver Wyman KCS Capacity Analysis Worksheet.
[108] *Id.*
[109] HC - Oliver Wyman - Capex Worksheet No. 2, Summary tab.
[110] *Id.*

Laredo, TX. In addition to the capacity constraints that CPKC will encounter on these two owned line segments (shown in the exhibit below), the process of moving between KCS owned and UP trackage rights introduces additional capacity issues, such as waiting for dispatcher approval to move between KCS and UP trackage and vice-versa. At present, there are no sidings on KCS's single-track line at either Robstown or Victoria, two of the entry points to the UP trackage rights lines. Despite train volumes projected to double by Year 3, the Application does not allocate any capital expenditure funding to increase capacity on either of the two subdivisions or on the UP trackage rights segments over which CPKC proposes to double KCS's current train operations.

Exhibit B-3: Beaumont to Laredo – CPKC operating on its own tracks

Subdivision	Miles[111]	Speed Limits[112](mph)	Base Year Trains/Day % Bulk vs Non-Bulk[113]	Year 3 Trains/Day % Bulk vs Non-Bulk[114]	Capacity Issues
Rosenberg	87	55/59	8.5 {{ }} {{ }}	17.7 {{ }} {{ }}	Even if the new 10,000-foot siding between Kendleton and Louise is built, capacity on this line will be limited to 16 – 10,000-foot trains/day
Special Considerations	KCS operates over UP trackage between Beaumont and Rosenberg. Discussed in detail above				
Laredo	205	55/59	10.5 {{ }} {{ }}	19.4 {{ } {{ }}	Even with the one additional siding that is expected to be built, capacity to move 10,000-foot trains will be limited to 14.7/day. Additional sidings may be required at three locations
Special Considerations	KCS operates over UP trackage between Rosenburg and Victoria. Discussed in detail above				

[111] Oliver Wyman KCS Capacity Analysis Worksheet.
[112] *Id.*
[113] HC - Oliver Wyman - Capex Worksheet No. 2, Summary tab.
[114] *Id.*

B.3 KCSM Line – Laredo, TX to Metro Mexico City, MX

Applicants allocated no capital in their plan for capacity expansion in Mexico, even with significant projected volume increases and significant constraints on the ability to handle trains of the maximum 10,000-foot length specified in the operating plan. This is of particular concern because CPKC's growth volumes consist primarily of time-sensitive intermodal and automotive traffic, which tends to move in longer, lighter tonnage trains. Clearly, additional sidings and (perhaps) siding length extensions will be required to keep the network fluid for the projected train volumes and to handle the larger 10,000-foot maximum train sizes proposed by CPKC. My capacity assessments of the three districts where additional (or expanded) 10,000-foot sidings will be needed are shown in the exhibit below.

Exhibit B-4: KCSM Line from Nuevo Laredo to Mexico City

District	KMs[115]	Speed Limits[116] (mph)	Base Year Trains/Day % Bulk vs Non-Bulk[117]	Year 3 Trains/Day % Bulk vs Non-Bulk[118]	Capacity Issues
Saltillo	387	59	24.1 {{ }} {{ }}	29.8 {{ }} {{ }}	The current siding lengths limit the capacity for long trains to 16 per day. Several new 10,000-foot sidings will likely be needed. Capacity between Brazil & Rodriguez is projected to be slightly above 80%.
Vanegas	345	59	15.1 {{ }} {{ }}	20.8 {{ }} {{ }}	The current capacity for long trains on this line is less than 12 (6 each way per day) compared to a projected 20.8, so only about 56% of the trains can be long trains per day. Several new 10,000-foot sidings will likely be needed.
Tula	439	59	14.6 {{ }} {{ }}	19.5 {{ }} {{ }}	The segment from Ahorcado to Puerto Carrozas is 55KM between viable passing sidings and is projected to be operating at 96% of capacity post-merger. An additional siding may be needed.

[115] Oliver Wyman KCSM Capacity Analysis Worksheet.
[116] *Id.*
[117] HC - Oliver Wyman - Capex Worksheet No. 2, Summary tab.
[118] *Id.*

Appendix C. Description of Rail Crossings Assessment

The CPKC operating plan does not address potential difficulties in moving large volumes of additional traffic over at-grade crossings with other railroads. To determine the service impact of increasing CPKC trains moving over these crossings, Applicants should have performed a detailed rail capacity simulation for the following crossings:[119]

- Ottumwa, IA: An average of 26 BNSF and two Amtrak daily trains move over this crossing, which BNSF controls. For CP today, this is an operationally difficult, capacity-consuming crossing. Southbound trains must ease down a 1.6 percent grade so they can stop if needed before the crossing. Northbound, CP trains also must ease up to the crossing in case they have to stop. Just beyond the crossing, northbound CP trains must immediately climb a 1.6 percent grade. *CPKC train movements through this crossing are projected to grow by more than 400 percent, from an average of 4.2 in 2019 to 18.4 in Year 3*. BNSF has a speed limit of 30 mph and CP has a speed limit of 20 mph.
- Clinton, IA: This crossing of UP's E-W mainline requires CP trains to operate on UP trackage for seven miles through the town of Clinton. Six of the seven miles are subject to a speed restriction of 20 mph (which at this speed uses up 79 percent of the capacity of the CP line). While Applicants are investing in two sidings at the approaches to the UP crossing, my capacity analysis indicates that this investment will be insufficient to overcome projected capacity problems in the Davenport Subdivision. UP controls this crossing and 33-35 UP trains move through Clinton daily. With CPKC planning an increase of trains from 7 to 21.6 per day in Year 3, congestion will increase and UP and CP trains will be delayed.
- Savanna, IL: CP crosses a BNSF mainline in Savanna, IL. This is currently an automatic, first-come first-served crossing, which has a 25-mph speed restriction for both railroads; 32 BNSF trains per day move across this crossing. With an increase in CPKC train frequency from 3 to 11 daily, an increase in delays is likely.

[119] The source for all train volumes moving through these three crossings is the FRA Office of Safety, Grade Crossing Data Inventory.

Appendix D. Methodology for Estimating Capacity

Estimating the capacity of a line is a function of a variety of factors, including the number of tracks, siding length, distance between sidings, train speed, the size of trains, and the number of trains per day. The best-in-class method of capacity analysis employs a tool called the Berkeley Simulation Software Rail Traffic Controller (RTC) Model, which includes a train performance calculator to evaluate train schedules input by the user. Here, Applicants instead used a "spreadsheet model" based on train running times between sidings, plus a delay for entering and leaving the passing siding. From these data a theoretical capacity can be calculated.

The practical capacity of a line is 70 percent of its theoretical capacity, to accommodate track maintenance activities, recovery from disruptions (which can include mechanical failures, derailments, and weather-related issues), bunching rather than smooth timing of trains (often caused by mixing unscheduled unit trains into the network along with scheduled intermodal and manifest trains), and switching activities at customer facilities along the route.[120] This methodology is consistent with the spreadsheet work papers provided by Applicants for the KCS lines in the United States and the CP lines from Kansas City to Chicago and St. Paul. This is especially important in a merger filing, where everything is considered based on an "average" day. There are day-of-week variations in train numbers as well as seasonal variations which in real life operations must be handled without significant delays.

Applicants provided capacity worksheets for the KCS lines in the United States using this methodology, but their analysis included all sidings regardless of length, without considering the sizes of the specific trains to be operated. While the operating plan calls for a 10,000-foot

[120] National Rail Freight Infrastructure Capacity and Investment Study, Association of American Railroads, September 2007, p. A-10, where it notes "Practical capacity is about 70 percent of the theoretical capacity and provides reliable service."

maximum train length, Applicants used many sidings that are well short of 10,000 feet in calculating line capacity. Moreover, their analysis of the KCS-owned lines between Rosenberg and Laredo assumed the existence of sidings that are not in the provided timetable and also are not identified as post-merger capital projects in the Application.

For KCSM lines in Mexico, no capacity analysis was done, and no capital plans were disclosed. However, service issues between Mexico City and Laredo will adversely impact traffic destined into the US at Laredo, TX. My analysis suggests that, unless some capital is spent to improve capacity, it is likely that CPKC will experience congestion issues on the Mexican portion of the network, especially given that most of the projected traffic growth for Applicants in Mexico is intermodal and finished automobiles, and CPKC plans to run this traffic with 10,000-foot trains, as with all non-bulk traffic.

Appendix E. Deposition Quotes on Capacity Analysis for KCS Lines[121]

Rosenberg to Victoria
{XXX}

[121] HC - Remote Videotaped Deposition of Raymond A. Elphick and John F. Orr, STB Docket No. FD 36500, Elphick Deposition, pp. 71-74 and 93-97, Feb 18, 2022.

Beaumont to Rosenberg
{XXX}

{XXX}

{XXX}

Appendix F. Hugh L. Randall Resume

Mr. Randall, a Partner Emeritus in Oliver Wyman's Transportation & Services practice and previously head of its global transportation consulting practice, has directed consulting projects for railroads, airlines, trucking companies, parcel carriers, maritime shipping companies, freight forwarders, and contract logistics users and providers. These studies have encompassed clients in North America, Europe, Asia, Latin America, and southern Africa.

Mr. Randall has carried out a wide range of projects in the areas of post-merger integration, due diligence/transactions, business strategy, market entry, operations improvement, and organizational realignment.

Relevant rail assignments directed by Mr. Randall in North America include the following:

- For a Class I railroad, Mr. Randall led a comprehensive and intensive examination of seven major business processes, to determine how best to change such processes to enable cost reduction and efficiency improvement. The project was carried out and implemented successfully, resulting in a savings in excess of $150 million.
- For a Class I railroad, Mr. Randall led an intermodal strategy study and an extended reach initiative. Both these projects were implemented successfully, enabling the railroad to increase market share, revenues, and profitability.
- For a Class I railroad, Mr. Randall directed a comprehensive extended reach initiative, exploring ways to expand the revenue base through increased use of transloading, rail-truck partnerships, intermodal services, and other initiatives. This project resulted in an increase in revenue, market share, and profitability for the railroad.
- For a Class I railroad, Mr. Randall directed a confidential M&A study examining the feasibility of acquiring another Class I railroad.
- At the request of a Class I CEO, Mr. Randall presented an assessment of the international container shipping industry and intermodal services to the Board of Directors.

Before joining Oliver Wyman, Mr. Randall held a series of senior management positions in railways, trucking, and consulting. At Consolidated Rail Corporation (Conrail), for the chairman and CEO, he oversaw five-year strategic planning for the railroad's freight and passenger services. Mr. Randall also served as General Manager of Conrail's Atlantic region and Assistant Vice President – Operations, with responsibility for developing and managing Conrail's operations improvement program.

At Ryder PIE Nationwide, Mr. Randall was Executive Vice President and Chief Financial Officer. In that position, he was responsible for the financial, planning, and administrative functions of a billion-dollar LTL trucking company. And as a Vice President at Booz•Allen and Hamilton, Mr. Randall directed consulting projects involving railways, trucking companies, and logistics functions throughout the world.

Mr. Randall received a BA in accounting and administration from Antioch College and an MBA from the Harvard Graduate School of Business Administration.

Exhibit 4

Verified Statement of
Mark E. Zmijewski

BEFORE THE
SURFACE TRANSPORTATION BOARD

STB FINANCE DOCKET NO. 36500

CANADIAN PACIFIC RAILWAY LIMITED; CANADIAN PACIFIC RAILWAY COMPANY; SOO LINE RAILROAD COMPANY; CENTRAL MAINE & QUEBEC RAILWAY US INC.; DAKOTA, MINNESOTA & EASTERN RAILROAD CORPORATION; AND DELAWARE & HUDSON RAILWAY COMPANY, INC. – CONTROL – KANSAS CITY SOUTHERN, THE KANSAS CITY SOUTHERN RAILWAY COMPANY, GATEWAY EASTERN RAILWAY COMPANY, AND THE TEXAS MEXICAN RAILWAY COMPANY

CN'S COMMENTS ON APPLICATION AND REQUEST FOR CONDITIONS

Verified Statement of Mark E. Zmijewski

February 28, 2022

Table of Contents

I. INTRODUCTION AND CONCLUSIONS 3

II. ANALYSIS OF THE FINANCIAL EFFECTS OF CP's ACQUISITION OF KCS ON CP 9

A. CP's Forecasts Submitted to the STB and the Alternative More Conservative Forecasts 9

1. CP's Pro Forma Exhibits 10

2. Conservative Forecasts 12

B. Analysis of CP's Post Acquisition Financial Risk (Debt Burden) 15

1. Comparison of the De Bruyn VS 2021 Estimated CP Leverage Ratio to CP's Actual 2021 Leverage Ratio 15

2. CP's Post-Acquisition Leverage Ratios 18

3. All of CP's Free Cash Flow Will be Used to De-Lever the Company Post Acquisition 20

4. CP's Post-Acquisition Credit Rating 23

C. Analysis of CP's Return on Invested Capital (ROIC) 26

1. The De Bruyn VS Did Not Analyze ROIC 26

2. CP's Target ROIC Has Been in the 15.3% and 15.5% Range (Roughly 15%) 27

3. CP's Actual 2021 Post-Acquisition ROIC 30

4. CP's Post-Acquisition ROIC Based on the Forecasts 31

5. Conclusions – CP's Post-Acquisition ROIC 33

III. ASSESSMENT OF CP'S CLAIMED EFFICIENCIES 34

A. Framework and Methodology to Assess Merger Efficiencies 36

1. Methodology for Verifying Efficiencies 38

2. Assessing Merger-Specificity of Efficiencies 40

3. Concluding Comments on the Framework and Methodology 42

B. Summary of CP's Claimed Efficiencies 42

1. Operating Revenue Gains 44

2. Operating Benefits 46

C. Analysis of Claimed Efficiencies 51

1. Revenue Increase from Traffic Gains 51

2. Cost of Handling Added Traffic 58

3. Operating Benefits 60

4. The Operating Ratio of the Merged Company Provides Additional Evidence that the Claimed Efficiencies Are Not Verifiable 69

List of Exhibits

Exhibit III-1: Assessment of Claimed Efficiencies

Exhibit III-2: Summary of Benefits ("Claimed Efficiencies")

Exhibit III-3: Claimed Personnel Savings. KCS Corporate Risk Executives

Exhibit III-4: Claimed Non-Personnel Expenditures Savings

Exhibit III-5: Claimed IT Savings

Exhibit III-6: Claimed Audit and Listing Fees Savings

Exhibit B-I: Canadian Pacific Railway (CP) Recreated Pro-Forma Income Statement

Exhibit B-II: Canadian Pacific Railway (CP) Recreated Pro-Forma Balance Sheet

Exhibit B-III: Canadian Pacific Railway (CP) Recreated Pro-Forma Statement of Cash Flows

Exhibit B-IV: Kansas City Southern (KCS) Recreated Pro-Forma Income Statement

Exhibit B-V: Kansas City Southern (KCS) Recreated Pro-Forma Balance Sheet

Exhibit B-VI: Kansas City Southern (KCS) Recreated Pro-Forma Statement of Cash Flows

Exhibit B-VII: Canadian Pacific Railway (CP) and Kansas City Southern (KCS) Recreated Pro-Forma Consolidated Income Statement

Exhibit B-VIII: Canadian Pacific Railway (CP) and Kansas City Southern (KCS) Recreated Pro-Forma Consolidated Balance Sheet

Exhibit B-IX: Canadian Pacific Railway (CP) and Kansas City Southern (KCS) Recreated Pro-Forma Consolidated Statement of Cash Flows

Exhibit B-X: Canadian Pacific Railway (CP) and Kansas City Southern (KCS) Recreated Summary of CP/KCS Claimed Efficiencies

Exhibit B-XI: Canadian Pacific Railway (CP) and Kansas City Southern (KCS) Recreated Pro-Forma Consolidated Income Statement Including the Effects of the Claimed Efficiencies

Exhibit B-XII: Canadian Pacific Railway (CP) and Kansas City Southern (KCS) Recreated Pro-Forma Consolidated Balance Sheet Including the Effects of the Claimed Efficiencies

Exhibit B-XIII: Canadian Pacific Railway (CP) and Kansas City Southern (KCS) Recreated Pro-Forma Consolidated Statement of Cash Flows Including the Effects of the Claimed Efficiencies

I. INTRODUCTION AND CONCLUSIONS

1. My name is Mark E. Zmijewski. I specialize in the areas of accounting, economics, and finance as they relate to financial analysis, valuation, and securities analysis, or more generally, financial economics. I am Professor Emeritus at The University of Chicago Booth School of Business. I am also a Senior Consultant to Charles River Associates. In my practice, I have consulted in matters related to assessment of the valuation, financial performance, capital structure/financial leverage, and financial health of companies and in merger and acquisition transactions. I have also taught courses on these topics as part of my academic career (financial accounting, mergers and acquisition accounting, financial analysis, corporate valuation, and financial strategy). I discuss my qualifications and present my curriculum vitae in Appendix A.

2. This matter arises from the acquisition of Kansas City Southern ("KCS") by Canadian Pacific Railway Limited ("CP") (collectively, the "Merging Parties") on December 14, 2021.[1] As of the close of the acquisition, CP owned KCS via a voting trust, "which ensures KCS will operate independently of CP, [and which] will remain in effect until the U.S. Surface Transportation Board ('STB') issues its decision on the companies' joint railroad control application."[2] In October 2021, CP and KCS submitted an application ("CP/KCS Application")[3] to the STB, which seeks permission from the STB to dissolve the voting trust structure: "The STB's approval of CP's control of KCS would create

[1] Kansas City Southern, Form 8-K, dated December 14, 2021.

[2] Kansas City Southern, Form 8-K, dated December 14, 2021.

[3] Before the Surface Transportation Board, Finance Docket No. 36500, Railroad Control Application, October 29, 2021, vol. 1-4.

Canadian Pacific Kansas City Limited ('CPKC'), the only single-line railroad linking the United States, Mexico and Canada."[4]

3. As part of the CP/KCS Application, Dean Vargas, a Managing Director of Revenue Planning for CP, submitted a verified statement ("Vargas VS") dated October 28, 2021.[5] In that verified statement, Mr. Vargas stated that he prepared pro forma financial statements for CP that "show the financial impact of the Transaction on a forward-looking basis over the three-year period during which the Transaction will be implemented and in a normal post-implementation year."[6] These forecasts include Base Year financial statements for the standalone CP and KCS ("Base Year CP" and "Base Year KCS"), and pro forma financial statements for CPKC on a consolidated basis ("Pro Forma Exhibits"), including the potential transaction benefits claimed by CP ("Claimed Efficiencies").[7, 8] Based on the forecasts in the Vargas VS, I developed an alternative set of forecasts that exclude the effects of the Claimed Efficiencies ("Conservative Forecasts").

4. CP also submitted a verified statement of Chris De Bruyn, Managing Director – Investor Relations and Treasury for CP ("De Bruyn VS"), which claims to "explain: (a) the

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[4] Kansas City Southern, Form 8-K, dated December 14, 2021.

[5] Verified Statement of Dean Vargas before the Surface Transportation Board, dated October 28, 2021. Finance Docket No. 36500.

[6] Vargas VS, ¶22.

[7] Vargas VS. The Pro Forma Exhibits include Income Statements, Balance Sheets, and Cash Flow Statements for each of the companies. See, CP/KCS Application, vol. 1, Appendix E (Exhibit 16), Appendix F (Exhibit 17), and Appendix G (Exhibit 18).

[8] The potential revenue and cost benefits in a merger and acquisition transaction are called synergies or efficiencies. I use the *Horizontal Merger Guidelines* issued by the U.S. Department of Justice & Federal Trade Commission to analyze the potential revenue and cost benefits claimed by the Merging Parties in this transaction and I refer to those potential benefits as "Claimed Efficiencies," which is consistent with the term used in the *Horizontal Merger Guidelines*. See, U.S. Department of Justice & Federal Trade Commission's *Horizontal Merger Guidelines*, dated Aug. 19, 2010, Section 10.

financial terms of CP's proposed acquisition of control of Kansas City Southern ('KCS'); (b) CP's ability to repay transaction-related debt while simultaneously increasing its network investment; and (c) the fairness of the consideration to be paid by CP to KCS from the financial perspective of CP's shareholders."[9]

5. Notably, the CP/KCS Application does not include a verified statement from Nadeem Velani, CP's Chief Financial Officer ("CFO"), even though previously, on June 28, 2021, Mr. Velani submitted a verified statement[10] that analyzed the proposal by Canadian National Railway Company ("CN") to acquire KCS ("Velani VS on CN's Acquisition of KCS"). The Velani VS on CN's Acquisition of KCS concluded, "CN's proposal to acquire KCS is fraught with risk to a wide range of stakeholders"[11] and "CN's targeted rate of return will not be achieved based on the synergies CN forecasts, which will place pressure on CN to boost returns in other ways, such as through cost-cutting, or – more plausibly – reaping the benefits of reduced competition ...."[12] The De Bruyn VS did not conduct the same analyses or apply the same standards to CP's acquisition of KCS that were used in the Velani VS on CN's Acquisition of KCS to evaluate CN's proposed acquisition of KCS. Yet, as I show in this verified statement, the criticisms of CN's proposed acquisition of KCS in the Velani VS on CN's Acquisition of KCS equally apply to, and are equally valid for, CP's acquisition of KCS.

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[9] Verified Statement of Chris De Bruyn before the Surface Transportation Board, dated October 28, 2021. Finance Docket No. 36500.

[10] On June 28, 2021, CP filed a Reply to CN and KCS's Motion For Approval of Voting Trust, including a Verified Statement by CP's Chief Financial Officer Nadeem Velani attached as Exhibit 2 to CP Reply. See, Canadian Pacific's Reply to CN and KCS Joint Motion For Approval of Voting Trust, STB Finance Docket No. 36514, filed June 28, 2021 by Canadian Pacific Railway.

[11] Velani VS on CN's Acquisition of KCS, p. 2.

[12] Velani VS on CN's Acquisition of KCS, p. 11.

6. I have been asked by Sidley Austin LLP to address two aspects of the acquisition of KCS by CP:

   a. Analyze the financial effects of CP's acquisition of KCS on CP, including an analysis of the De Bruyn VS, and conducting the analyses and applying the standards previously used by CP to evaluate the proposed acquisition of KCS by CN;[13] and

   b. Assess the verifiability of CP's Claimed Efficiencies from the perspective of the *Horizontal Merger Guidelines* ("*Merger Guidelines*")[14] provided by the U.S. Department of Justice ("DOJ") and Federal Trade Commission ("FTC").[15]

7. In this verified statement I show the following regarding the De Bruyn VS:

   a. None of the analyses in the De Bruyn VS is based on the Pro Forma Exhibits, but, instead, the De Bruyn VS uses more optimistic forecasts: "CP and KCS as they are today and with ongoing economic growth moving forward."[16]

   b. The estimated 3.8x 2021 pro forma leverage ratio for CP in the De Bruyn VS does not represent the leverage ratio that CP would ever report in 2021 because the De Bruyn VS calculated the pro forma leverage ratio by combining CP and KCS, when, in fact, in 2021 and for some time afterwards, KCS will be held in a trust and operate independently. That leverage ratio without combining KCS in 2021 using the data used in the De Bruyn VS is 4.5x versus the 3.8x estimated pro forma leverage ratio for 2021 in the De Bruyn VS.

   c. The estimated 2021 pro forma leverage ratio for CP in the De Bruyn VS is substantially lower than CP's actual pro forma leverage ratio for 2021 (3.8x in the De

[13] Although I do not agree with the usefulness or economic foundation of certain analyses, standards, and conclusions in the Velani VS on CN's Acquisition of KCS, I nonetheless, utilize these analyses and standards to analyze CP's acquisition of KCS; and I show that the key criticisms in the Velani VS on CN's Acquisition of KCs equally apply to, and are equally valid for, CP's acquisition of KCS.

[14] U.S. Department of Justice & Federal Trade Commission's *Horizontal Merger Guidelines*, dated Aug. 19, 2010.

[15] I understand that the *Merger Guidelines* are not legally applicable to the Transaction, but they nevertheless provide a reasonable and appropriate framework to analyze the Claimed Efficiencies from the perspective of a financial economist.

[16] De Bruyn VS, p. 6. Although the De Bruyn VS does not provide a source of the forecasts used, the forecasts appear to be the same forecasts that were disclosed in the CP/KCS November 3, 2021 Proxy Statement/Prospectus, p. 101, which was filed with the U.S. SEC by both companies as KCS Schedule 14A ("Proxy Statement") and CP Form 424B3 ("Prospectus"). The forecasts for CP and KCS on a standalone basis are referred to in the Proxy Statement/Prospectus as "KCS management unaudited CPRL projections" and "KCS management unaudited KCS projections," respectively. These forecasts are used in the BMO Transaction Model (CP-HC-00007073.xlsx) that also incorporates the Claimed Efficiencies into the forecasts. I refer to the forecasts underlying the BMO Transaction Model as "Proxy/Transaction Model Forecasts." De Bruyn VS appears to use the Proxy/Transaction Model Forecasts.

Bruyn VS versus CP's actual pro forma leverage ratio, 4.0x), indicating that CP's forecast for 2021 was optimistic.

d. Using the data in the De Bruyn VS, CP's estimated 2021 leverage ratio (without combining KCS), which is the leverage ratio CP would report based on its actual financial statements, is 4.5x. Based on its actual financial results for 2021,[17] CP's actual 2021 leverage ratio is 4.8x not 4.5x, again, indicating that CP's forecast for 2021 was optimistic.

e. The De Bruyn VS claims that CP will attain its target leverage ratio of 2.5x within four years. Had the De Bruyn VS used either CP's Pro Forma Exhibits or the Conservative Forecasts, CP would not attain its target leverage ratio within four years.

f. The De Bruyn VS conducted no analysis of CP's post-acquisition ROIC, which was a primary criticism that the Velani VS made about a potential CN-KCS transaction. Based on CP's actual financial results for 2021, or either CP's Pro Forma Exhibits or the Conservative Forecasts, CP's ROIC for 2021 and the following four years is substantially below – less than one-half – of its historical and target ROIC of 15% in every year. (See ¶9.a - ¶9.b.)

g. Based on credit rating thresholds used in the De Bruyn VS, CP's credit rating is likely to fall below investment grade if CP experiences a substantial downturn in its financial performance.

8. The Velani VS on CN's Acquisition of KCS concluded that "CN Will Take on a Very High Level of Debt,"[18] and "CN's proposal to acquire KCS is fraught with risk to a wide range of stakeholders."[19] In this verified statement, when I apply the leverage analyses and standards used in the Velani VS on CN's Acquisition of KCS to CP's acquisition of KCS, I show that:

a. CP took on a high level of debt that will substantially increase CP's leverage and, thus, its financial risk.

b. Based on either CP's Pro Forma Exhibits or the Conservative Forecasts, CP would not attain its target leverage ratio within four years. Based on CP's Pro Forma

[17] CP 2021 SEC Form 10-K, p. 79.

[18] Velani VS on CN's Acquisition of KCS, p. 6.

[19] Velani VS on CN's Acquisition of KCS, p. 2.

Exhibits, CP would only attain a leverage ratio of 2.8x in four years; and based on the Conservative Forecasts, CP would only attain a leverage ratio of 3.8x in four years.

c. Based on the analysis in the Velani VS on CN's Acquisition of KCS, CP's leverage will be "materially higher" than that of any other Class I railroad over the last decade. "As of 2020, the highest leverage amongst other Class I railroads is 3.0 times Adjusted Debt / EBITDA,"[20] which is substantially lower than 4.8x Adjusted Debt / EBITDA for CP in 2021.

d. Based on CP's Pro Forma Exhibits, CP has no margin of error in its forecasts so that it can repay its debt over the next four years, and based on the Conservative Forecasts, CP will have a cash flow deficit of over $2 billion over the next four years.

9. Based on an analysis of CN's post-acquisition ROIC, the Velani VS on CN's Acquisition of KCS concluded that CN's post-acquisition ROIC would be substantially lower than CN's historical ROIC and target ROIC. In this verified statement, I conduct that same analysis of CP's post-acquisition ROIC and show that CP's post-acquisition ROIC will be substantially lower than CP's historical ROIC and target ROIC in the 15% range:

a. Based on its actual financial results for 2021, CP's actual ROIC for 2021 is 8.2%,[21] which is substantially below its historical and target ROIC of 15%.

b. Based on CP's Pro Forma Exhibits, CP's ROIC for the next four years has a range of 7.0% to 7.3%; and based on CP's Conservative Forecasts, CP's ROIC for the next four years has a range of 5.7% to 6.3%, which, again, are substantially below – less than one-half – of its historical and target ROIC of 15% in every year.

10. Lastly, in this verified statement, my assessment of the verifiability of CP's Claimed Efficiencies from the perspective of the *Merger Guidelines* shows that most of the Claimed Efficiencies are not verifiable and many are not merger-specific; and thus, the majority of the Claimed Efficiencies would not meet the standards to be cognizable based on the *Merger Guidelines*.

[20] Velani VS on CN's Acquisition of KCS, pp. 8 – 9.

[21] CP 2021 SEC Form 10-K, p. 75.

11. The remainder of this verified statement is organized as follows. In Section II, I discuss my analysis of the financial effects of CP's acquisition of KCS on CP, including an analysis of the De Bruyn VS and an analysis of the CP acquisition of KCS by applying the same analyses and standards previously used by CP to evaluate the proposed acquisition of KCS by CN. In Section III, I assess the verifiability of CP's Claimed Efficiencies from the perspective of the *Merger Guidelines*. In Appendix A, I provide my curriculum vitae; and in Appendix B, I present CP's Pro Forma Exhibits.

II. ANALYSIS OF THE FINANCIAL EFFECTS OF CP'S ACQUISITION OF KCS ON CP

12. In this section, I first describe CP's Pro Forma Exhibits and the Conservative Forecasts. Then, in the remainder of this section, I analyze the financial effects of CP's acquisition of KCS on CP, including an analysis of the De Bruyn VS. I conduct the same analyses and apply the same standards previously used by CP to evaluate the proposed acquisition of KCS by CN.

A. CP's Forecasts Submitted to the STB and the Alternative More Conservative Forecasts

13. As I noted in the introduction, the Pro Forma Exhibits in the CP/KCS Application included forecasts of CPKC (CP and KCS combined) and the potential efficiencies claimed by CP.[22] As I explain later in this section, I adjusted the Pro Forma Exhibits to develop more conservative forecasts of CP's acquisition of KCS (Conservative Forecasts). In this section, I describe these two sets of forecasts.

[22] Vargas VS, ¶22. See, CP/KCS Application, vol. 1, Appendix E (Exhibit 16), Appendix F (Exhibit 17), and Appendix G (Exhibit 18).

1. CP's Pro Forma Exhibits

14. The Vargas VS stated that CP's Pro Forma Exhibits were prepared to "show the financial impact of the Transaction on a forward-looking basis over the three-year period during which the Transaction will be implemented and in a normal post-implementation year. All impacts are shown relative to the base year pro forma financial statements of CPKC for 2019."[23] In other words, each year in the Pro Forma Exhibits is based on CP's adjusted 2019 reported financial statements plus the Claimed Efficiencies, which are assumed to be realized during the three-year period (one-third realized each year). I replicated these forecasts and present them in Appendix B, Exhibits B-I through B-XIII.[24]

15. CP's Pro Forma Exhibits include a 2019 Base-Year forecast, forecasts for Year 1 through Year 3, and a forecast for a Normal Year beyond Year 3 (four years of forecasts). The 2019 Base-Year forecast for CP does not include CP's acquisition of KCS. I adjusted the 2019 Base-Year forecast for CP's acquisition of KCS to create a CP Unconsolidated Base-Year Forecast, which is how CP will report its acquisition of KCS in the years KCS is held in the trust and operates independently.[25] In the following table, I present various financial items derived from the forecasted income statement (Revenues, EBITDA,[26] and

[23] Vargas VS, ¶22.

[24] See, CP/KCS Application, vol. 1, Appendix E (Exhibit 16), Appendix F (Exhibit 17), and Appendix G (Exhibit 18).

[25] I assume that: (1) KCS will pay CP a dividend; (2) CP will incur debt to finance the KCS acquisition and pay interest on that debt; (3) CP will not repurchase any shares but rather use that cash to repay its debt; (4) CP's common shares (and the dividend paid on those shares) include the amount of shares issued to finance the KCS acquisition; and (5) CP will record purchase accounting adjustments to its assets and liabilities following the KCS acquisition similar to those that CP recorded in December 2021. All adjustment amounts used are from the Forecasts Submitted to the STB.

[26] EBITDA is equal to earnings before interest, taxes, depreciation and amortization.

Interest Expense), the balance sheet (Total Debt and Invested Capital[27]), and the cash flow statement (Cash Flow from Operations, Capital Expenditures, and Unlevered Free Cash Flows[28]). The table presents five years of information, the CP Unconsolidated Base-Year ("CP Unconsol"), Year 1 through Year 3 forecasts ("Year 1," "Year 2," and "Year 3," respectively), and the Normal Year ("Year 4"); the table also presents the compound average growth rate ("CAGR") over Years 1 to 4 in the last column of the table.

Table 1
Pro Forma Exhibits
Selected Financial Statement Measures

	CP Unconsol	Year 1	Year 2	Year 3	Year 4	Yr 1-Yr 4 Total	Yr 1 - Yr 4 CAGR
Panel A: Income Statement							
TOTAL REVENUES	$5,999	$9,283	$9,592	$9,887	$9,887	$38,649	*2.1%*
EBITDA	$3,383	$5,064	$5,311	$5,534	$5,534	$21,443	*3.0%*
NET INTEREST EXPENSE	536	652	637	607	575	$2,471	
Panel B: Balance Sheet							
TOTAL DEBT	$15,416	$18,669	$17,366	$15,843	$14,267		
TOTAL INVESTED CAPITAL	$36,240	$44,601	$45,497	$46,319	$47,078		
Panel C: Cash Flow Statement							
CASH PROVIDED BY OPERATING ACTIVITIES	$2,303	$3,506	$3,804	$4,016	$4,059	$15,385	
CASH USED IN INVESTING ACTIVITIES	($1,254)	($1,946)	($1,950)	($1,942)	($1,930)	($7,768)	
UNLEVERED FREE CASH FLOWS	$1,459	$2,046	$2,329	$2,526	$2,557	$9,458	*7.7%*

Sources: CP/KCS Application, vol. 1, Appendix E (Exhibit 16), pp. 3-4; Appendix F (Exhibit 17), pp. 1-2; Appendix G (Exhibit 18), pp. 1-2; CRA calculations.

16. As seen from the above table, the CAGR over Years 1 through 4 (the period when the parties expect to realize their Claimed Efficiencies) for the consolidated revenue,

[27] Invested Capital is equal to Total Debt plus Shareholders Equity plus Non-Controlling Interest. Total Debt equals Long-Term Debt plus Current Maturities of Long-Term Debt.

[28] Unlevered Free Cash Flows is equal to Cash Flow from Operating Activities plus After-Tax Interest Expense minus Capital Expenditures.

EBITDA and Unlevered Free Cash Flows are 2.1%, 3.0% and 7.7%, respectively. Over that period the consolidated CPKC is projected to generate approximately $38.6 billion in Revenue, $21.4 billion in EBITDA, and S15.4 billion in Operating Cash Flows, of which $7.8 billion are expected to be reinvested as capital expenditures. The Merged Company[29] also expects to generate about $9.5 billion of Unlevered Free Cash Flows and use that cash to pay dividends and reduce its debt from roughly $19 billion in Year 1 to $14 billion in Year 4.

2. Conservative Forecasts

17. The Velani VS on CN's Acquisition of KCS criticized the analyses submitted by CN to the STB related to CN's proposed acquisition of KCS. One criticism was not "stress testing" the forecasts used: "The biggest flaw in Mr. Houle's analysis is that he performs no stress testing of financial performance."[30] In response, I was asked by counsel for CN to "stress test" CN's proposed acquisition of KCS. To that end, I submitted a verified statement to the STB using a set of pessimistic forecasts ("Zmijewski VS on CN's Acquisition of KCS").[31] Based on the framework I developed in my previous verified statement, in this verified statement, I adjust the forecasts CP submitted to the STB for CP's acquisition of KCS and create a more conservative set of forecasts ("Conservative Forecasts").

18. The Conservative Forecasts assume that the 2019 Base-Year forecasts continue for the next four years, which excludes the Claimed Efficiencies from the forecasts CP submitted

[29] I use the term "Merged Company" to refer to an integrated CP and KCS, that is CPKC.

[30] Velani VS on CN's Acquisition of KCS, p. 18.

[31] Verified Statement of Mark E. Zmijewski before the Surface Transportation Board, dated July 6, 2021. Finance Docket No. 36514.

to the STB. The Conservative Forecasts are more conservative than the forecasts CP submitted to the STB and thus can "stress test" CP's acquisition of KCS. I note that the Conservative Forecasts are more optimistic forecasts than the pessimistic forecasts I used to "stress test" CN's proposed acquisition of KCS.[32] I present a summary of these forecasts in the following table (presenting the same financial measures as in the above table).

[32] I described the pessimistic forecasts I used in the Zmijewski VS on CN's Proposed Acquisition of KCS as follows (p. 15):

> In my analyses I used pessimistic forecasts (stress test) for both CN and KCS ("Pessimistic Forecasts"). The Pessimistic Forecasts:
>
> a. are based on the actual financial performance of CN and KCS in 2020, which, as is widely known, included the effects of a substantial downturn in the economy resulting from the COVID-19 pandemic;
>
> b. are adjusted to include the change in operating working capital of $0 (instead of being positive and a source of cash) and an increase in investment in capital expenditures at its pre-COVID-19 (pre-2020) levels;
>
> c. do not include the cash flows generated by CN or KCS while KCS is held in the Voting Trust, which could be used by CN to repay its debt and which will increase KCS's value while it is held in the Voting Trust; and
>
> d. do not include the realization of any synergies expected to result from the Merger.
>
> Thus, my analyses based on the Pessimistic Forecasts are conservative and provide a stress test of the Merger because they assume a continuation of the substantial economic downturn that occurred in 2020; they ignore the consensus forecast that the economy is expected to grow substantially over the next few years; they are adjusted for an increase in investments in capital expenditures; they do not include the cash flows generated by either company while KCS is held in the Voting Trust; and, if the Merger is ultimately approved by the STB, they ignore that CN and KCS, as well as financial analysts, expect the realization of substantial synergies to result from the Merger.

Table 2
Conservative Forecast
Selected Financial Statement Measures

	CP Unconsol	Year 1	Year 2	Year 3	Year 4	Yr 1-Yr 4 Total	Yr 1 - Yr 4 CAGR
Panel A: Income Statement							
TOTAL REVENUES	$5,999	$8,865	$8,865	$8,865	$8,865	$35,460	*0.0%*
EBITDA	$3,383	$4,646	$4,646	$4,646	$4,646	$18,584	*0.0%*
NET INTEREST EXPENSE	536	652	643	626	610	$2,531	
Panel B: Balance Sheet							
TOTAL DEBT	$15,416	$18,949	$18,167	$17,360	$16,530		
TOTAL INVESTED CAPITAL	$36,239	$44,612	$45,532	$46,401	$47,219		
Panel C: Cash Flow Statement							
CASH PROVIDED BY OPERATING ACTIVITIES	$2,302	$3,210	$3,263	$3,288	$3,313	$13,074	
CASH USED IN INVESTING ACTIVITIES	($1,254)	($1,930)	($1,930)	($1,930)	($1,930)	($7,720)	
UNLEVERED FREE CASH FLOWS	$1,458	$1,766	$1,812	$1,824	$1,837	$7,240	*1.7%*

Sources: CP/KCS Application, vol. 1, Appendix E (Exhibit 16), pp. 3-4; Appendix F (Exhibit 17), pp. 1-2; Appendix G (Exhibit 18), pp. 1-2; CRA calculations.

19. As seen from the above table, in Years 1 through 4, absent the Claimed Efficiencies, the parties' consolidated Revenue, EBITDA and Unlevered Free Cash Flows are essentially flat (with minimal increase in the Unlevered Free Cash Flows due to tax advantages of increased depreciation). Over that period the consolidated CPKC will generate approximately $35.5 billion in Revenue, $18.6 billion in EBITDA, and $13.1 billion in Operating Cash Flows of which $7.7 billion will be reinvested as capital expenditures. The consolidated company will generate about $7.2 billion of Unlevered Free Cash Flows and use that cash to pay dividends and reduce its debt from roughly $19 billion in Year 1 to $16.5 billion in Year 4. Thus, if none of the Claimed Efficiencies are realized,

CP will generate about $2.2 billion less of Unlevered Free Cash Flows and pay off about $2.2 billion less of debt.[33]

B. Analysis of CP's Post Acquisition Financial Risk (Debt Burden)

20. In this section, I analyze CP's post-acquisition financial risks based on the analyses of the company's leverage ratio and free cash flow used in the Velani VS on CN's Acquisition of KCS. Based on these analyses, the Velani VS on CN's Acquisition of KCS concluded that "CN Will Take on a Very High Level of Debt,"[34] "[t]he proposed transaction will increase CN's leverage to levels that CN has not incurred in the recent past,"[35] and "CN's leverage will be materially higher than that of any other Class 1 railroad over the last decade."[36] My analyses show that the criticisms by Mr. Velani about CN's proposed acquisition of KCS equally apply to, and are equally valid for, CP's acquisition of KCS. Namely, that CP is taking on a high level of debt that will substantially increase CP's leverage and, thus, its financial risk. I also conduct a credit rating analysis of CP post acquisition and find that the results of that analysis further corroborate the conclusion of substantially increased financial risk.

1. Comparison of the De Bruyn VS 2021 Estimated CP Leverage Ratio to CP's Actual 2021 Leverage Ratio

21. The De Bruyn VS presents a comparison of CP's historical leverage ratios (Adjusted Net Debt to Adjusted EBITDA) from 2011 through 2020 and CP's estimated leverage ratios

[33] Year 4 debt of $14.3 billion in the Pro Forma Exhibits versus Year 4 debt of $16.5 billion in the Conservative Forecasts. See Tables 1 and 2.

[34] Velani VS on CN's Acquisition of KCS, p. 6.

[35] Velani VS on CN's Acquisition of KCS, p. 8.

[36] Velani VS on CN's Acquisition of KCS, p. 8.

in 2021 through 2024, assuming CP's acquisition of KCS occurred in the Q4 2021.[37] For 2021, the De Bruyn VS calculates CP's leverage ratio on a "pro forma" basis, which assumes CP and KCS are combined. However, if CP's acquisition of KCS occurred in Q4 2021, CP would not combine (and did not combine) KCS because KCS would be held in a trust and operate independently from CP. Thus, De Bruyn's "pro forma" leverage ratio for CP in 2021 is not what CP would report in 2021 because KCS would be held in a trust.

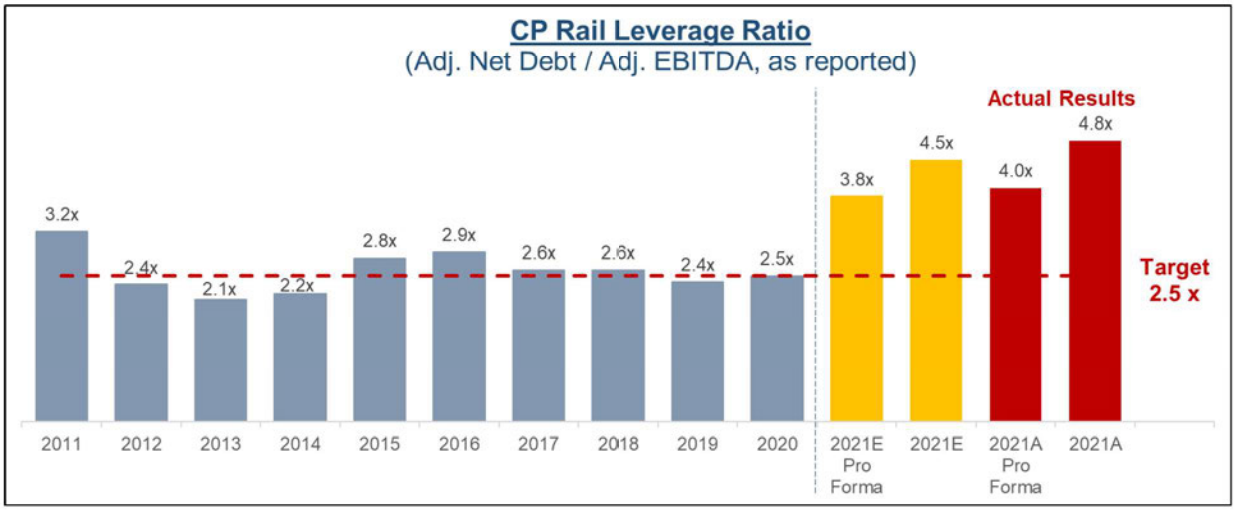
22. In the following figure, I reproduce CP's leverage ratios from the De Bruyn VS through 2021. The 2011-2020 ratios (blue-gray bars) are as reported by CP in the company's Form 10-K filings with the U.S. SEC. The De Bruyn VS presents CP's expected 2021 leverage ratio (orange bar, 3.8x) on a pro forma basis (CP and KCS combined). In the same figure, I also show CP's expected 2021 leverage ratio (orange bar, 4.5x) based on the financial statements CP would report (that is, KCS is not consolidated but reported as an equity investment because it is held in a trust and operates independently). The two red bars show CP's actual leverage ratios: (i) CP's actual 2021 leverage ratio (red bar, 4.8x) based on CP's 2021 actual financial statements;[38] and (ii) CP's actual pro forma 2021 leverage ratio (red bar, 4.0x).[39]

[37] De Bruyn VS, Figure 1, p. 5.

[38] CP 2021 SEC Form 10-K, p. 79.

[39] CP's actual pro forma 2021 leverage ratio is calculated using debt and EBITDA figures for KCS as reported in the company's 2021 Form 10-K filed with the U.S. SEC (see KCS Form 10-K for the period ended December 31, 2021).

Figure 1
De Bruyn VS 2021 Estimated CP Leverage Ratio
Compared to CP's Actual 2021 Leverage Ratio



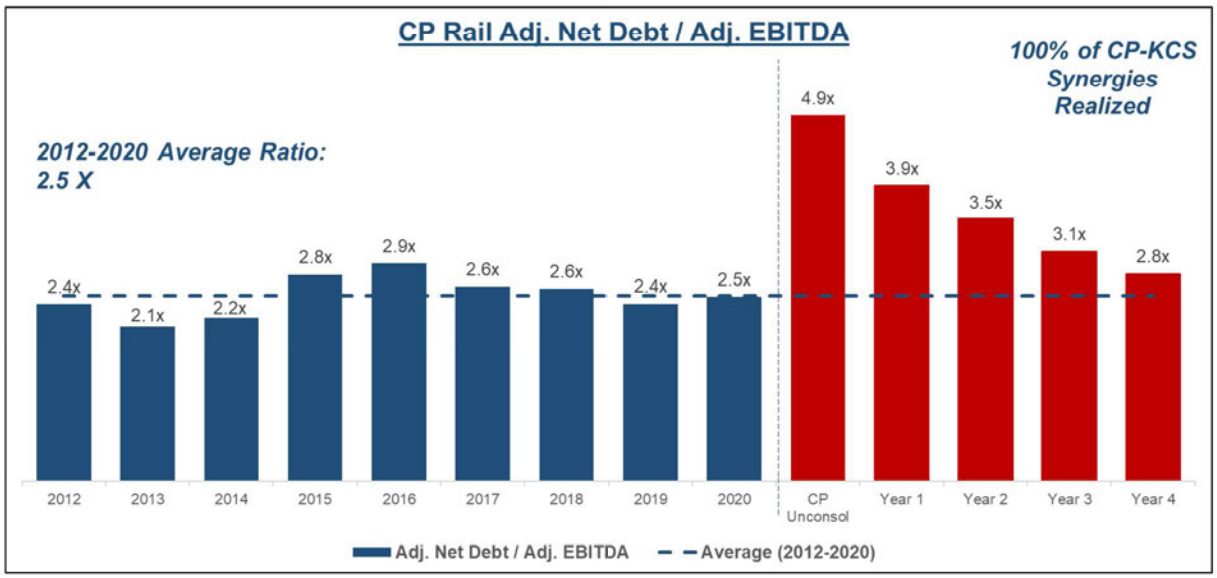
Sources: CP 2013-2021 SEC Forms 10-K; De Bruyn VS, Figure 1; CRA calculations.

23. As is seen from the above figure, the estimated 2021 CP leverage ratio in the De Bruyn VS was 3.8x on a pro-forma basis while its actual leverage ratio was 4.0x on a pro-forma basis, which is about 5% higher than the estimate in the De Bruyn VS. I also note that CP's 2021 leverage ratio on a standalone basis was 4.8x which is more than 90% higher than CP's 2020 standalone leverage ratio of 2.5x and CP's target leverage ratio of 2.5x. These results show not only that CP's leverage ratios are higher than its historical leverage ratios, but also that CP's forecasts for 2021 were optimistic.

2. CP's Post-Acquisition Leverage Ratios

24. In the following figure, I present CP's leverage ratios (Adjusted Net Debt to Adjusted EBITDA)[40] pre-acquisition from 2012 through 2020 (blue bars) and post-acquisition (red bars: CP Unconsol, Year 1, …, Year 4) based on the Pro Forma Exhibits.

Figure 2
CP's Leverage Ratios Based on the Pro Forma Exhibits



Sources: CP 2013-2020 SEC Forms 10-K; De Bruyn VS, Figure 1; CP/KCS Application, vol. 1, Appendix E (Exhibit 16), pp. 3-4; Appendix F (Exhibit 17), pp. 1-2; Appendix G (Exhibit 18), pp. 1-2; CRA calculations.

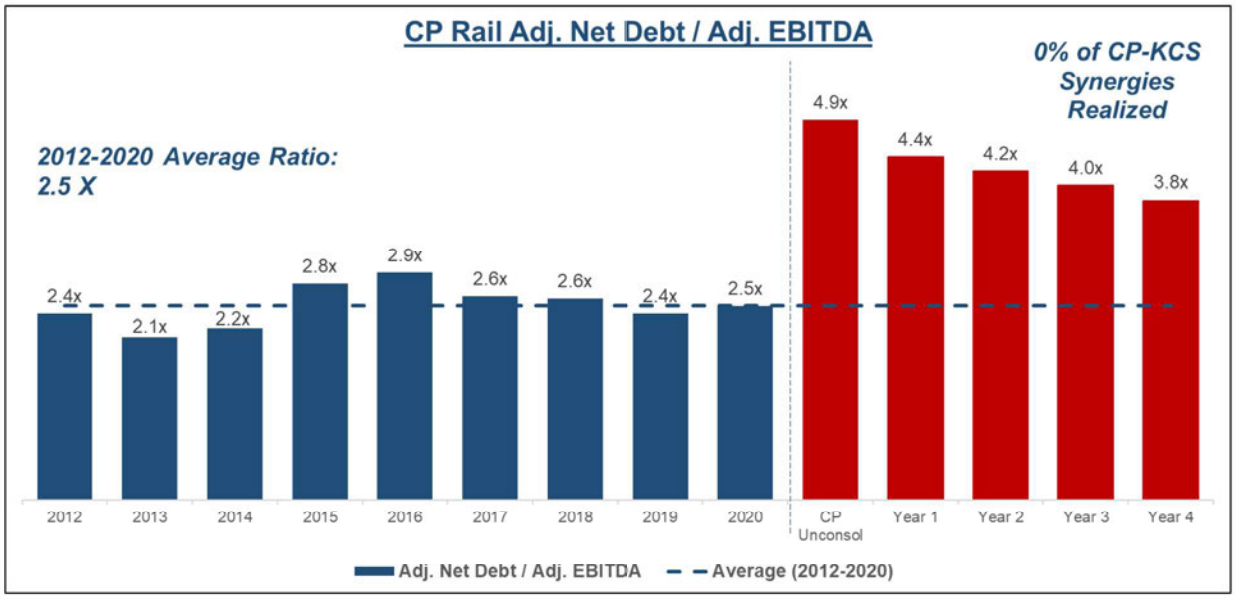
25. As is seen from the above figure, CP's leverage ratio ranged between 2.1x and 2.9x over the 2012-2020 period and averaged about 2.5x (which is also CP's Target Leverage Ratio). Following the KCS acquisition and while KCS is held in trust, CP's leverage ratio increases to 4.9x mostly due to the increased debt incurred to finance the acquisition. In Years 1 to 4 when CP expects STB to approve the KCS acquisition and

[40] For definitions of Adjusted Net Debt and Adjusted EBITDA, see, for example, 2020 CP Form 10-K, pp. 68-69. Adjusted Net Debt is defined as Long-term debt including long-term debt maturing within one year + Pension plan deficit + Operating lease liabilities – Cash and cash equivalents. Adjusted EBITDA is defined as Adjusted EBIT + Operating lease expense + Depreciation and amortization – Other components of net periodic benefit recovery. I assume that Pension plan deficit, Operating lease liabilities, Operating lease expense, and Other components of net periodic benefit recovery in Years 1 to 4 are as reported by CP in the Base Year (2019).

KCS will be consolidated with CP, the leverage ratio declines from 3.9x in Year 1 to 2.8x in Year 4. Thus, CP does not attain its 2.5x target leverage ratio within four years after the merger.

26. In the figure below, I also present CP's leverage ratios (CP Rail Adjusted Net Debt to CP Adjusted EBITDA) pre-acquisition from 2012 through 2020 (blue bars) and post-acquisition (red bars: CP Unconsol, Year 1, …, Year 4) based on the Conservative Forecasts.

Figure 3
CP's Leverage Ratios Based on the Conservative Forecasts



Sources: CP 2013-2020 Forms 10-K; De Bruyn VS, Figure 1; CP/KCS Application, vol. 1, Appendix E (Exhibit 16), pp. 3-4; Appendix F (Exhibit 17), pp. 1-2; Appendix G (Exhibit 18), pp. 1-2; CRA calculations.

27. As is seen from the above figure, in Years 1 to 4 when CP expects the STB to approve the KCS acquisition and KCS will be consolidated with CP, the leverage ratio declines from 4.4x in Year 1 to 3.8x in Year 4. Thus, CP does not attain its 2.5x target leverage ratio within four years after the merger.

28. The Velani VS on CN's Acquisition of KCS criticized CN stating, "Further, CN's leverage will be materially higher than that of any other Class I railroad over the last decade. As of 2020, the highest leverage amongst other Class I railroads is 3.0 times Adj. Debt / EBITDA, materially lower than the contemplated 4.8 times Adj. Debt / EBITDA for CN."[41] As seen from the above figures, the CP Unconsol leverage ratios are as high as CN's leverage ratios, and based on both sets of forecasts, CP's leverage ratios are higher than the Target Leverage Ratio of 2.5x.[42] Thus, my analyses show that the criticisms by Mr. Velani about CN's proposed acquisition of KCS equally apply to, and are equally valid for, CP's acquisition of KCS.

3. All of CP's Free Cash Flow Will be Used to De-Lever the Company Post Acquisition

29. The Velani VS on CN's Acquisition of KCS criticized CN for the use of its excess cash flow to service the company's debt in a manner that Mr. Velani argued "leaves no margin for error."[43] The Velani VS on CN's Acquisition of KCS demonstrated that "the comparison between (a) projected total free cash flow (calculated as cash from operations, less capital expenditures and investing activities) generated by both CN and KCS … inclusive of some synergies … and (b) cash flow required to pay CN's dividend and repay the amount of CN's debt required to achieve its target Leverage Ratio … [implies that] CN is pursuing a strategy that leaves itself very little margin of error."[44]

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[41] Velani VS on CN's Acquisition of KCS, pp. 8 – 9.

[42] I note that using the Proxy/Transaction Model Forecasts, CP's post-acquisition leverage ratios in 2022-2025 are {{ }}, respectively (see also De Bruyn VS, Figure 1). Using the Proxy/Transaction Model Forecasts and assuming none of the Claimed Efficiencies is realized, CP's post-acquisition leverage ratios in 2022-2025 are {{ }}, respectively.

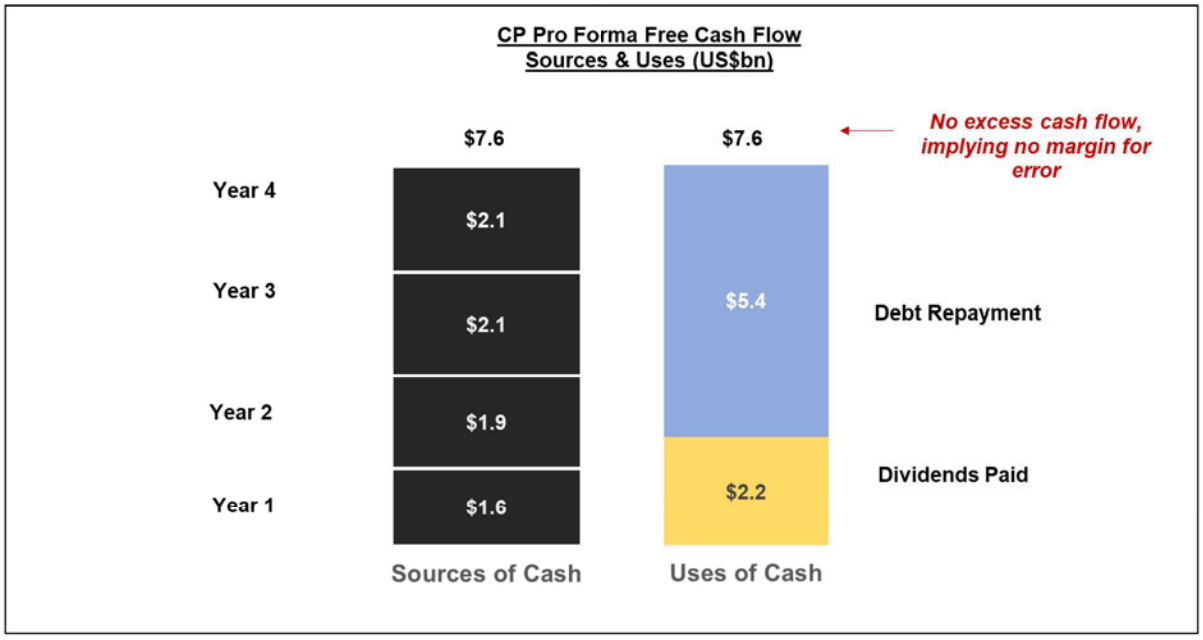
[43] Velani VS on CN's Acquisition of KCS, p. 10.

[44] Velani VS on CN's Acquisition of KCS, pp. 10-11 and Figure 6.

30. I conduct the same analysis for the CP acquisition of KCS and compare the sources and uses of CP's Free Cash Flows; or stated alternatively I compare "(a) projected total free cash flow (calculated as cash from operations, less capital expenditures and investing activities) … [and] …(b) cash flow required to pay … dividend and repay the amount of … debt."[45]

31. In the following figure, I present CP's sources and uses of Free Cash Flow based on the Pro Forma Exhibits.

Figure 4
CP's Post Acquisition Sources and Uses of Free Cash Flow
Based on the Pro Forma Exhibits



Sources: Velani VS on CN's Acquisition of KCS, Figure 6; CP/KCS Application, vol. 1, Appendix E (Exhibit 16), pp. 3-4; Appendix F (Exhibit 17), pp. 1-2; Appendix G (Exhibit 18), pp. 1-2; CRA calculations.

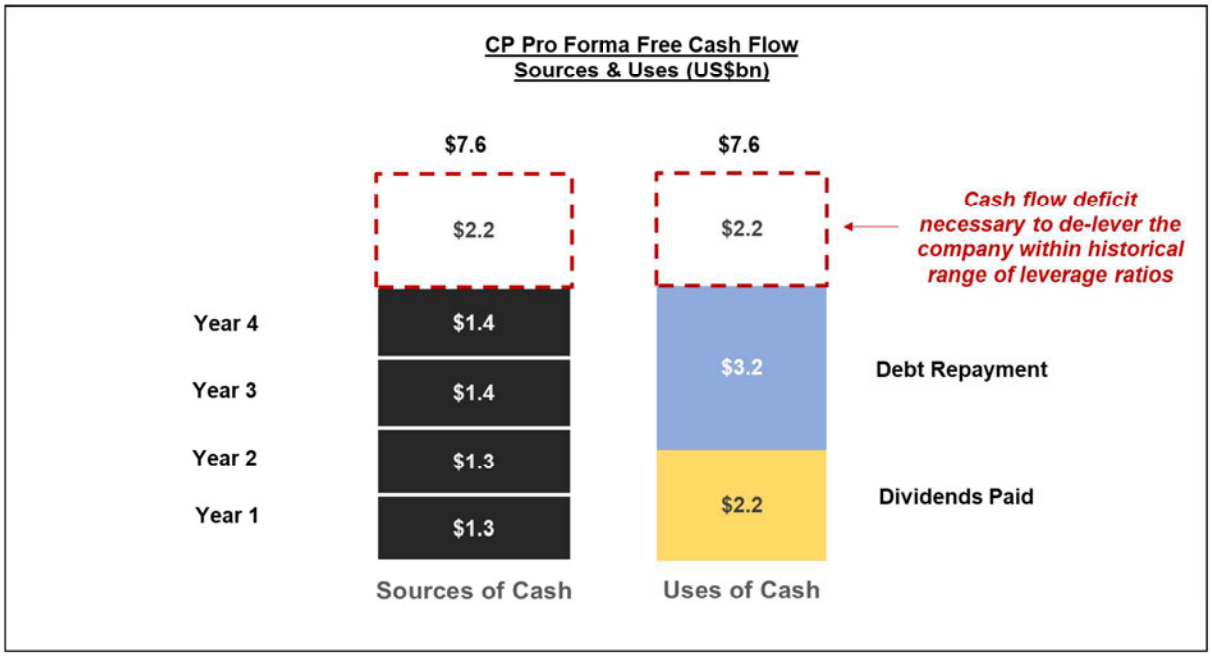
32. As is seen from the above figure, in order to de-lever the company by Year 4 and achieve leverage ratio of 2.8x, which is still above its 2.5x target leverage ratio (see Figure 2), CP uses all of the $7.6 billion Free Cash Flows that the company is expected to generate

[45] Velani VS on CN's Acquisition of KCS, pp. 10-11 and Figure 6.

from Year 1 to Year 4 to pay dividends ($2.2 billion) and repay debt ($5.4 billion), thus, according to the Velani VS on CN's Acquisition of KCS, CP has no margin for error.

33. In the following figure, I present CP's sources and uses of Free Cash Flow based on the Conservative Forecasts.

Figure 5
CP's Post Acquisition Sources and Uses of Free Cash Flow
Based on the Conservative Forecasts



Sources: Velani VS on CN's Acquisition of KCS, Figure 6; CP/KCS Application, vol. 1, Appendix E (Exhibit 16), pp. 3-4; Appendix F (Exhibit 17), pp. 1-2; Appendix G (Exhibit 18), pp. 1-2; CRA calculations.

34. As is seen from the above figure, if none of the Claimed Efficiencies is realized, CP will generate about $5.4 billion free cash flows from Year 1 through 4, an amount sufficient to pay the $2.2 billion dividend and repay only $3.2 billion of debt. Thus, CP would be $2.2 billion short of the free cash flow that is necessary to de-lever the company by Year 4 to a level consistent with CP's historical leverage.[46]

[46] I note that using the Proxy/Transaction Model Forecasts, CP is projected to generate post-closing approximately $3.8 billion excess cash flows ($12.3 billion free cash flows less $8.5 billion of dividend and debt payments)

4. CP's Post-Acquisition Credit Rating

35. Although the Velani VS on CN's Acquisition of KCS raised various criticisms of the amount of debt that CN would have issued in the acquisition of KCS, it failed to acknowledge that CN's post-acquisition credit rating was expected to be investment grade and close to CP's pre-acquisition credit rating.[47] Moreover, CP's post-acquisition credit rating Baa2/BBB+[48] is the same as CN's expected post-acquisition credit rating had CN acquired KCS. I illustrate the effect of CP's acquisition of KCS on its credit rating using the De Bruyn VS credit rating thresholds, which are based on CP's leverage ratio.[49] Typically, a credit rating below Baa3/BBB- is considered non-investment grade.[50]

36. In the following figure, I present CP's post-acquisition leverage ratios as measured by the Debt to EBITDA ratio (CP Unconsol, Year 1, …, Year 4) relative to the credit rating thresholds for the various investment grade credit ratings using the Pro Forma Exhibits.

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between 2022 and 2025. Using the Proxy/Transaction Model Forecasts and assuming none of the Claimed Efficiencies is realized, CP is projected to generate post-closing approximately $2.5 billion excess cash flows ($11.0 billion free cash flows less $8.5 billion of dividend and debt payments) between 2022 and 2025.

[47] See Zmijewski VS on CN's Acquisition of KCS, pp 11 – 13.

[48] Moody's and S&P Global.

[49] The De Bruyn VS support workpapers, FD 36500 – Work Paper – HC – Debruyn - Excel Back-up.xlsx, Tab "23.2" (Rating Agency - Credit Rating Summary Matrix) indicates that credit ratings Baa1/BBB+, Baa2/BBB, and Baa3/BBB- are associated with Debt/EBITDA ratios below {{ }}, respectively.

[50] See Zmijewski VS on CN's Acquisition of KCS, pp 11 – 13. See also Charles Schwab *Guide to Sub-Investment Grade/High Yield Bonds,* p. 2, "Sub-investment grade/high yield bonds are bonds with a credit rating below investment grade (Baa3 or BBB-), as judged by the bond ratings assigned by one of the major rating agencies: Moody's Investors Service (Moody's) and Standard & Poor's. The ratings are the opinion of the agency. They are not a guarantee of credit quality, probability of default, or recommendation to buy or sell." Available at https://www.schwab.com/public/file/p-4635483/.

Figure 6
Illustration of CP's Credit Ratings
Based on the Pro Forma Exhibits

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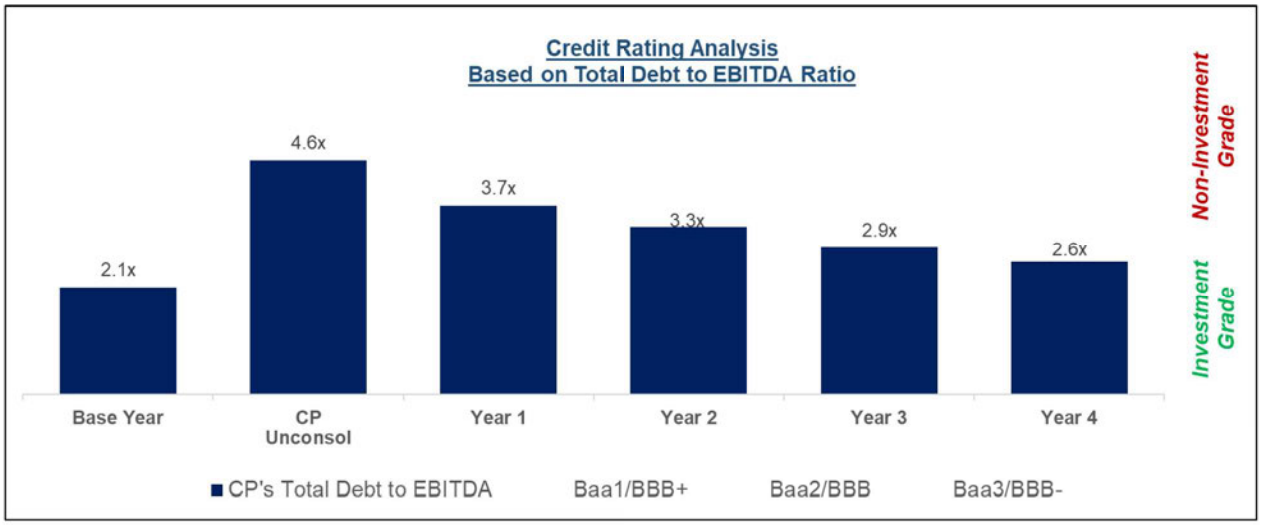

Sources: FD 36500 – Work Paper – HC – Debruyn - Excel Back-up.xlsx, Tabs "21.2" and "23.2"; CP/KCS Application, vol. 1, Appendix E (Exhibit 16), pp. 3-4; Appendix F (Exhibit 17), pp. 1-2; Appendix G (Exhibit 18), pp. 1-2; CRA calculations.

}}

37. The above figure illustrates how the addition of $8.2 billion acquisition debt to the company's balance sheet pushes the leverage ratio above the thresholds associated with investment grade credit rating. This evidence is consistent with an increased financial risk for CP following the KCS acquisition. The ability to successfully manage that risk depends on CP's ability to de-lever the company by Year 4 by aggressively repaying its debt. A strategy that in the CP CFO's own words "leaves no margin for error."[51]

38. In the following figure, I present CP's post-acquisition leverage as measured by the Debt to EBITDA ratio (CP Unconsol, Year 1, …, Year 4) relative to the credit rating

[51] Velani VS on CN's Acquisition of KCS, p. 10.

thresholds for the various investment grade credit ratings based on the Conservative Forecasts.

Figure 7
Illustration of CP's Credit Ratings
Based on the Conservative Forecasts

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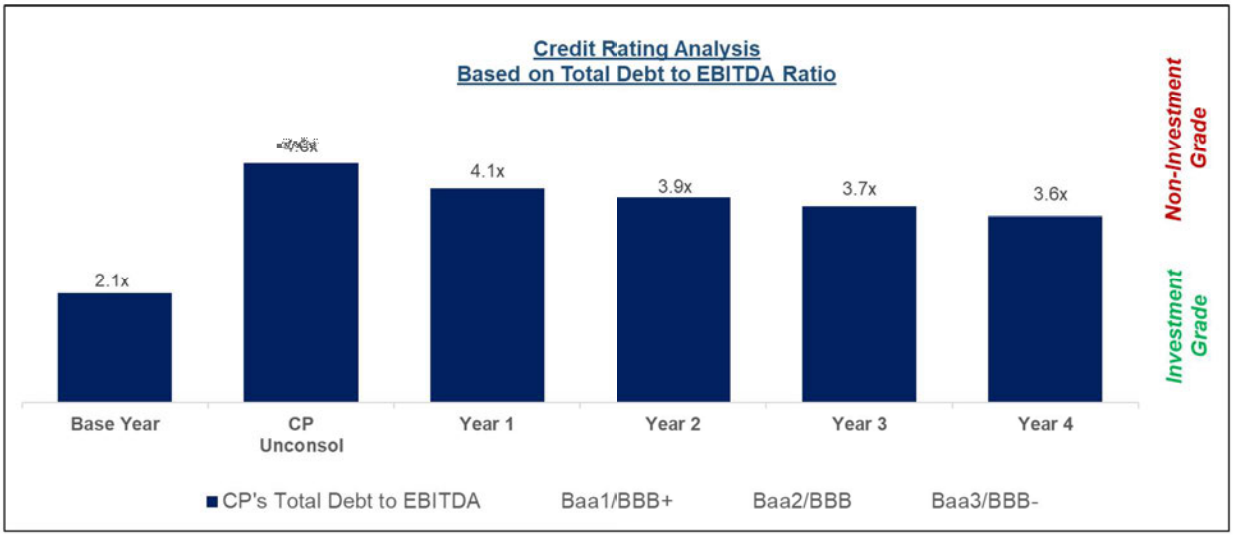

Sources: FD 36500 – Work Paper – HC – Debruyn - Excel Back-up.xlsx, Tabs "21.2" and "23.2"; CP/KCS Application, vol. 1, Appendix E (Exhibit 16), pp. 3-4; Appendix F (Exhibit 17), pp. 1-2; Appendix G (Exhibit 18), pp. 1-2; CRA calculations.

}}

39. As discussed earlier, CP generates about $2.2 billion less of free cash flows under the Conservative Forecasts and repays about $2.2 billion less of debt, thus, the company's leverage remains higher relative to the leverage under the Conservative Forecasts. This implies higher debt burden and more pressure on the company's investment grade credit rating. The above figure illustrates that if CP experiences a substantial downturn in its

financial performance, CP's debt levels remain relatively high even by Year 4 and its credit rating is likely to fall below investment grade.[52]

C. Analysis of CP's Return on Invested Capital (ROIC)

40. Based on an analysis of CN's post-acquisition ROIC, the Velani VS on CN's Acquisition of KCS concluded that CN's post-acquisition ROIC would be substantially lower than CN's historical ROIC and target ROIC.[53] In this section, I conduct that same analysis of CP's post-acquisition ROIC and show it will be substantially lower than CP's historical ROIC and target ROIC of roughly 15%.

41. In the remainder of this section, I first discuss the lack of ROIC analysis in the De Bruyn VS. I then follow the approach in the Velani VS on CN's Acquisition of KCS that identified CN's target ROIC based on CN's historical ROICs, management compensation, and statements by CN's Chief Financial Officer Ghislain Houle.[54, 55] Lastly, I show CP's 2021 reported ROIC and calculate CP's ROIC based on the forecasts in the Pro Forma Exhibits and the Conservative Forecasts.

1. The De Bruyn VS Did Not Analyze ROIC

42. CP states that its adjusted ROIC is also an important measure of the company's financial performance: "Adjusted ROIC is a performance measure that measures how productively the Company uses its long-term capital investments, representing critical indicators of

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[52] I note that using the Proxy/Transaction Model Forecasts, CP's post-acquisition Debt/EBITDA ratios in 2022-2025 are {{ }}, respectively. Assuming none of the Claimed Efficiencies are realized, CP's post-acquisition Debt/EBITDA ratios in 2022-2025 are {{ }}, respectively.

[53] Velani VS on CN's Acquisition of KCS, Section IV, pp. 15 – 16.

[54] Velani VS on CN's Acquisition of KCS, Section IV, pp. 11 – 18.

[55] I note that Mr. Houle responded to the allegations of Mr. Velani and explained how Mr. Velani mischaracterized his statements. See Verified Statement of Ghislain Houle before the Surface Transportation Board, dated July 6, 2021. Finance Docket No. 36514, pp. 7-9.

good operating and investment decisions made by management, and is an important performance criteria in determining certain elements of the Company's long-term incentive plan."[56] Tellingly, even though Adjusted ROIC is an important measure of financial performance used by CP, and even though the Velani VS on CN's Acquisition of KCS analyzed and made conclusions about CN's proposed acquisition of KCS, the De Bruyn VS conducts no analysis and provides no discussion of the effect of the KCS acquisition on CP's post-acquisition ROIC.

2. CP's Target ROIC Has Been in the 15.3% and 15.5% Range (Roughly 15%)

43. CP explains Adjusted ROIC as:

> Adjusted ROIC is calculated as Adjusted return divided by Adjusted average invested capital. Adjusted return is defined as Net income adjusted for interest expense, tax effected at the Company's adjusted annualized effective tax rate, and significant items in the Company's Consolidated Financial Statements, tax effected at the applicable tax rate. Adjusted average invested capital is defined as the sum of total Shareholders' equity, Long-term debt, and Long-term debt maturing within one year, as presented in the Company's Consolidated Financial Statements, each averaged between the beginning and ending balance over a rolling 12-month period, adjusted for the impact of significant items, tax effected at the applicable tax rate, on closing balances as part of this average ….[57]

44. In the following figure, I present CP's historical ROIC from 2016 through 2020, which I extracted from CP's 2020 SEC Form 10-K filing.[58]

[56] CP 2021 SEC Form 10-K, p. 73.

[57] CP 2020 SEC Form 10-K, p. 64.

[58] CP 2020 SEC Form 10-K, p. 66.

Figure 8
CP's Historical ROIC (2016 – 2020)

(in millions of Canadian dollars, except for percentages)	For the year ended December 31				
	2020	2019	2018	2017	2016
Adjusted return	**$ 2,748**	$ 2,626	$ 2,421	$ 2,013	$ 1,896
Adjusted average invested capital	**$ 16,443**	$ 15,547	$ 14,953	$ 13,672	$ 13,541
Adjusted ROIC	**16.7 %**	16.9 %	16.2 %	14.7 %	14.0 %

45. As is seen from the above figure, between 2016 and 2020, CP earned an ROIC in the range of 14.0% to 16.9%.

46. In the next figure, I present the target ROIC for Management's Performance Share Units ("PSUs").[59]

[59] In CP's annual report for the 2020 fiscal year, it stated (p. 118):

> During 2020, the Company issued 97,998 PSUs with a grant date fair value of approximately $ 34 million and 10,029 PDSUs with a grant date fair value, including value of expected future matching units, of approximately $ 4 million. PSUs and PDSUs attract dividend equivalents in the form of additional units, based on dividends paid on the Company's Common Shares, and vest approximately three years after the grant date contingent upon CP's performance ("performance factor"). The fair value of these PSUs and PDSUs is measured periodically until settlement using closing share price on the date of measurement. The fair value of units that are probable of vesting based on forecasted performance factors over the three-year performance period is recognized as expense in the Consolidated Statements of Income. Vested PSUs are settled in cash. Vested PDSUs are settled in cash pursuant to the DSU plan and are eligible for a 25 % match if the holder has not exceeded their share ownership requirements, and are paid out only when the holder ceases their employment with CP.
>
> The performance period for PSUs and PDSUs issued in 2020 is January 1, 2020 to December 31, 2022, and the performance factors are Return on Invested Capital ("ROIC"), Total Shareholder Return ("TSR") compared to the S&P/TSX 60 Index, and TSR compared to Class I railways.

Figure 9
CP's Target ROIC for Management Performance Share Units[60]

2019 PSU performance measures	Why the measure is important	Threshold (50%)	Target (100%)	Exceptional (200%)	Weighting
PSU three-year average return on invested capital (ROIC) Net operating profit after tax divided by average invested capital	Focuses executives on the effective use of capital as we grow Ensures shareholders' capital is employed in a value-accretive manner	15.3%	16%	16.4%	70%
Total shareholder return Measured over three years. The percentile ranking of CP's TSX Compound Annual Growth Rate (CAGR) relative to the companies that make up the S&P/TSX 60	Compares our TSR on the TSX to the broader S&P/TSX60 to reflect our progress relative to the Canadian market Aligns long-term incentive compensation with long-term shareholder interests	25th percentile	50th percentile	75th percentile	15%
Total shareholder return Measured over three years. The ordinal ranking of CP's NYSE CAGR relative to the Class 1 Railroads	Compares our TSR on the NYSE to the publicly traded Class 1 Railroads to ensure we are competitive against our primary competitors. Aligns long-term incentive compensation with long-term shareholder interests	4th	3rd	1st	15%

2020 MANAGEMENT PROXY CIRCULAR 39

47. CP awards PSUs to its executives to "focus executives on achieving medium-term goals within a three-year performance period."[61] As is seen from the above figure, ROIC is an important metric that is used to evaluate management performance because it represents about 70% weight in the overall score. The minimum threshold for ROIC is 15.3%.

48. Lastly, I show an excerpt from CP's internal management presentation to the company's Board of Directors in the following figure.

[60] CP 2020 Management Proxy Circular, p. 39.

[61] CP 2020 Management Proxy Circular, p. 39.

Figure 10
CP's ROIC in Internal Management Presentation to the Board of Directors[62]

{{

}}

49. As is seen from the above figure, the CP management envisioned about {{ }}% average ROIC in the 2021-2024 period based on the company's standalone multiyear 2022-2024 Plan.

50. Based on my review of these documents, I conclude that CP's Target ROIC has been in the 15.3% and {{ }}% range (roughly 15%).

3. CP's Actual 2021 Post-Acquisition ROIC

51. In the following figure, I present CP's reported 2021 ROIC disclosed in its SEC Form 10-K filing.[63]

[62] CP Standalone Multi Year Plan 2022 – 2024, Board of Directors Presentation, September 2021, p. 2 (17.2.32 CP-HC-00007424).

[63] CP 2021 SEC Form 10-K, p. 75.

Figure 11
CP's Actual 2021 Post-Acquisition ROIC

Calculation of Adjusted ROIC

(in millions of Canadian dollars, except for percentages)	For the year ended December 31 2021	2020	2019
Adjusted return	$ **2,899**	$ 2,748	$ 2,626
Adjusted average invested capital	$ **35,383**	$ 16,443	$ 15,547
Adjusted ROIC	**8.2 %**	16.7 %	16.9 %

52. As is seen from the above figure, CP achieved 16.9% ROIC in 2019, 16.7% ROIC in 2020, and 8.2% in 2021 following the KCS acquisition.

4. CP's Post-Acquisition ROIC Based on the Forecasts

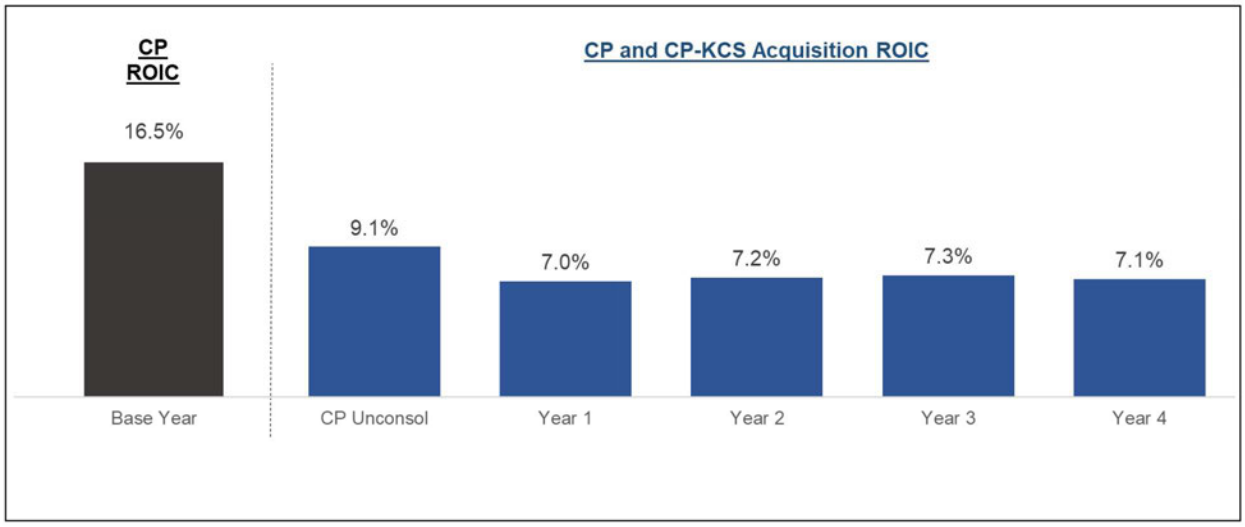
53. The Velani VS on CN's Acquisition of KCS conducted an ROIC analysis of CN post acquisition and found that "[e]ven after factoring in the $1 billion in annual synergies that CN forecasts for the KCS combination, it appears that CN's return on invested capital for this transaction will fall well short of … target range."[64]

54. I conduct similar ROIC analysis using both the Pro Forma Exhibits (with the full amount of Claimed Efficiencies) and the Conservative Forecasts (with no Claimed Efficiencies).

55. In the following figure, I present CP's ROIC post acquisition (CP Unconsol, Year 1, …, Year 4) based on the Pro Forma Exhibits.

[64] Velani VS on CN's Acquisition of KCS, Section IV, p. 15.

Figure 12
CP's Post-Acquisition ROIC Based on the Pro Forma Exhibits

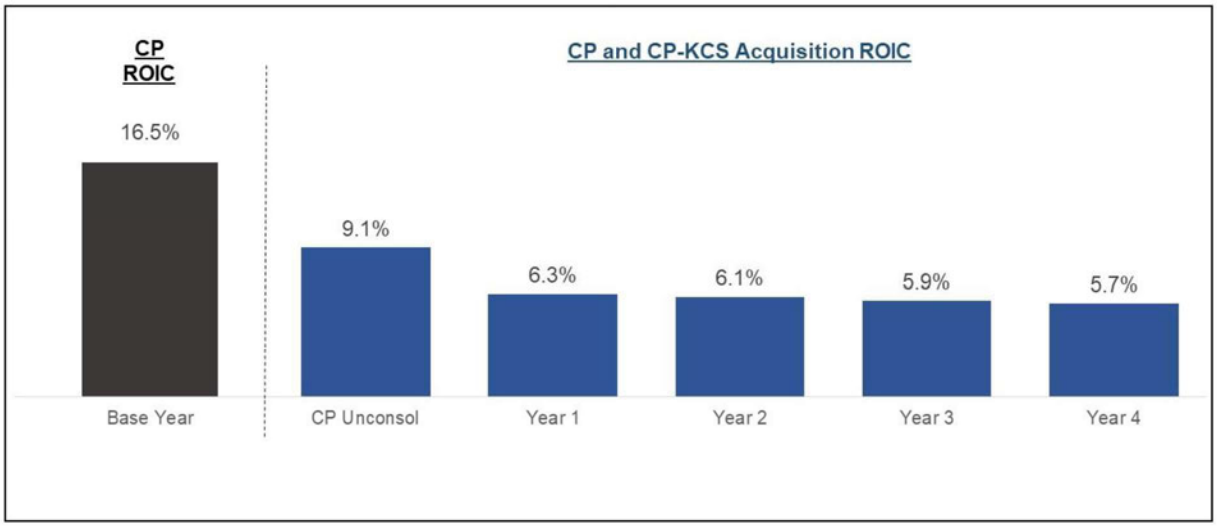


Sources: Velani VS on CN's Acquisition of KCS, Figure 9; CP/KCS Application, vol. 1, Appendix E (Exhibit 16), pp. 3-4; Appendix F (Exhibit 17), pp. 1-2; Appendix G (Exhibit 18), pp. 1-2; CRA calculations.

56. As is seen from the above figure, the expected ROIC in the post-acquisition period ranges between 7.0% and 9.1% and is well below CP's 15% target ROIC even with a full credit of the Claimed Efficiencies. The expected ROIC is about 7.0% to 7.3% in Year 1 to 4 when CP claims that it will realize the Claimed Efficiencies. Thus, in order to achieve an ROIC close to its target, holding its invested capital (ROIC denominator) constant, CP will have to more than double its unlevered earnings.

57. In the following figure, I present CP's ROIC post acquisition (CP Unconsol, Year 1, …, Year 4) based on the Conservative Forecasts.

Figure 13
CP's Post-Acquisition ROIC Based on the Conservative Forecasts



Sources: Velani VS on CN's Acquisition of KCS, Figure 9; CP 2013-2020 Forms 10-K; CP/KCS Application, vol. 1, Appendix E (Exhibit 16), pp. 3-4; Appendix F (Exhibit 17), pp. 1-2; Appendix G (Exhibit 18), pp. 1-2; CRA calculations.

58. As is seen from the above figure, again, the expected ROIC in the post-acquisition period, Years 1 to 4, falls even lower, to the 5.7% to 6.3% range, in the absence of the Claimed Efficiencies.[65]

5. Conclusions – CP's Post-Acquisition ROIC

59. The Velani VS on CN's Acquisition of KCS concluded, for example, "[m]y analysis in Section IV demonstrates that the implicit ROIC for CN's huge investment in KCS does not meet CN's own stated ROIC targets based on the $1 billion in transaction synergies CN has estimated. This means that CN must have based its investment decision on some unstated set of strategic benefits CN expects to realize. The most plausible explanation is that CN's investment is justified by CN's anticipated increase in market power –giving it

[65] I note that using the Proxy/Transaction Model Forecasts, CP's post-acquisition ROIC in 2022-2025 are {{ }}, respectively. Using the Proxy/Transaction Model Forecasts and assuming none of the Claimed Efficiencies are realized, CP's post-acquisition ROIC in 2022-2025 are {{ }}, respectively.

greater pricing power …."[66] My analyses show that the criticisms by Mr. Velani about CN's proposed acquisition of KCS equally apply to, and are equally valid for, CP's acquisition of KCS.

III. ASSESSMENT OF CP'S CLAIMED EFFICIENCIES

60. In this section, I assess the verifiability of the CP's Claimed Efficiencies from the perspective of the DOJ/FTC *Merger Guidelines*. My analysis of CP's Claimed Efficiencies shows that most of the Claimed Efficiencies are not verifiable, and many are not merger-specific; thus, the overwhelming majority of the Claimed Efficiencies would not meet the standards to be cognizable based on the *Merger Guidelines*.

61. While I understand that the *Merger Guidelines* are not legally applicable to CP's acquisition of KCS, the *Merger Guidelines* nevertheless provide a reasonable and appropriate framework to analyze the Claimed Efficiencies from the perspective of a financial economist. Based on the *Merger Guidelines*, assessing whether the efficiencies claimed by the Merging Parties are cognizable requires assessing whether they are: (1) merger-specific, (2) verifiable, and (3) not the result of anticompetitive reductions in output or service.[67] I summarize my conclusions in the following table, which I also present as Exhibit III-1.

[66] Velani VS on CN's Proposed Acquisition of KCS, pp. 26 – 27.

[67] *Merger Guidelines*, § 10 at 30. I note that I have not been asked to comment on whether the Claimed Efficiencies are the result of anticompetitive reductions in output or service.

Table 3
Summary of the Assessment of CP's Claimed Efficiencies

SUMMARY OF BENEFITS	Assessment of Verification	Assessment of Merger Specificity
Benefit Component		
OPERATING REVENUE GAINS		
Revenue Increase from Traffic Gains		
Rail-to-Rail Diversions (Brown/Zebrowski)	Not verified	Merger specific
Truck-to-Rail Diversions (Mutan)	Not verified	Merger specific
Attract New Rail Traffic (Wahba/Naatz)	Not verified	Partially merger-specific
Cost of Handling Added Traffic:		
Engineering - Maintenance of Way	Not verified	Merger specific
Mechanical	Not verified	Merger specific
Transportation	Not verified	Partially merger-specific
Equipment Requirements & Utilization	Not verified	Merger specific
Intermodal Operations	Not verified	Merger specific
OPERATING BENEFITS		
Mechanical	Not verified	Not merger-specific
Transportation	Not verified	Partially merger-specific
Equipment Requirements	Not verified	Partially merger-specific
Purchasing (Procurement)	Not verified	Partially merger-specific
G&A Savings		
Personnel Savings	Not verified	Merger specific
Non-Personnel Savings		
Non-Personnel Expenditures	Not verified	Merger specific
IT (Licensing/Subscriptions/Contract Services)	Not verified	Merger specific
Facilities	Verified	Merger specific
Audit & Listing Fees	Partially verified	Merger specific

Source: CP/KCS Application, Vol I, p. 74 (Appendix B - Summary of Benefits Exhibit)

62. Regarding the Revenue Increase from Traffic Gains component, none of the categories within this component is verifiable . Most, but not all, of these revenue increases are merger-specific. Regarding the Cost of Handling Added Traffic, none of the categories within this component is verifiable but these costs are merger-specific. CP's Claimed Operating Benefits efficiency has five components: 1) Mechanical; 2) Transportation; 3)

Equipment Requirements & Utilization; 4) Purchasing (Procurement); and 5) General and Administrative (G&A).

a. None of the claimed Mechanical Operating Benefits is verifiable and they are not merger-specific.
b. None of the claimed Transportation Operating Benefits is verifiable and they are only partially merger-specific.
c. None of the claimed Equipment Requirements Operating Benefits are verifiable and they are only partially merger-specific.
d. None of the claimed Procurement Operating Benefits are verifiable and they are only partially merger-specific.
e. One of the five categories of General and Administrative Benefits is verifiable and one category is partially verifiable; all categories are merger-specific.

63. In sum, in this verified statement, my assessment of the verifiability of CP's Claimed Efficiencies from the perspective of the *Merger Guidelines* shows that most of the Claimed Efficiencies are not verifiable and many are not merger-specific; and thus, the majority of the Claimed Efficiencies would not meet the standards to be cognizable based on the *Merger Guidelines*.

64. In what follows, I describe the framework and methodology I use in my assessment of CP's Claimed Efficiencies based on the *Merger Guidelines*, I describe each of the categories of CP's Claimed Efficiencies, and I provide my analysis of each of the categories of CP's Claimed Efficiencies to assess whether they are cognizable.

A. Framework and Methodology to Assess Merger Efficiencies

65. In this section, I analyze CP's Claimed Efficiencies. More specifically, I assess whether CP's Claimed Efficiencies are cognizable from the perspective of the *Merger*

Guidelines[68] provided by the DOJ and FTC. I understand that the *Merger Guidelines* are not legally applicable to CP's acquisition of KCS, but the *Merger Guidelines* nevertheless provide a reasonable and appropriate framework to analyze the Claimed Efficiencies from the perspective of a financial economist.

66. The DOJ and the FTC ("Agencies") issued updated *Merger Guidelines* on August 19, 2010.[69] The *Merger Guidelines* outline how the Agencies view efficiencies that result from a merger and set forth criteria of whether Claimed Efficiencies will be deemed cognizable. The *Merger Guidelines* state, "[c]ognizable efficiencies are merger-specific efficiencies that have been verified and do not arise from anticompetitive reductions in output or service. Cognizable efficiencies are assessed net of costs produced by the merger or incurred in achieving those efficiencies."[70]

67. The *Merger Guidelines* state that the Agencies assess whether cognizable efficiencies will reverse the potential anticompetitive effects of a proposed merger in the relevant market:[71]

> The Agencies will not challenge a merger if cognizable efficiencies are of a character and magnitude such that the merger is not likely to be anticompetitive in any relevant market. To make the requisite determination, the Agencies consider whether cognizable efficiencies likely would be sufficient to reverse the merger's potential to harm customers in the relevant market, e.g., by preventing price increases in that market ... In adhering to this approach, the Agencies are mindful that the antitrust laws give competition, not internal operational efficiency, primacy in protecting customers.

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[68] *Merger Guidelines*.

[69] *Merger Guidelines*.

[70] *Merger Guidelines*, § 10 at 30.

[71] *Merger Guidelines*, § 10 at 30-31 (footnotes omitted).

68. The analysis of the cognizable efficiencies claimed by the Merging Parties in the *Merger Guidelines* requires assessing whether they are: (1) merger-specific, (2) verifiable, and (3) not the result of anticompetitive reductions in output or service (collectively, "*Merger Guidelines Efficiencies Criteria*").[72] I note, however, that I have not been asked to comment on whether the Claimed Efficiencies are the result of anticompetitive reductions in output or service and I do not discuss this consideration further.

1. Methodology for Verifying Efficiencies

69. The *Merger Guidelines* state, "[e]fficiency claims will not be considered if they are vague, speculative, or otherwise cannot be verified by reasonable means."[73] The *Merger Guidelines* also state:[74]

> Efficiencies are difficult to verify and quantify, in part because much of the information relating to efficiencies is uniquely in the possession of the merging firms. Moreover, efficiencies projected reasonably and in good faith by the merging firms may not be realized. Therefore, it is incumbent upon the merging firms to substantiate efficiency claims so that the Agencies can verify by reasonable means the likelihood and magnitude of each asserted efficiency, how and when each would be achieved (and any costs of doing so) ...

70. While the *Merger Guidelines* do not prescribe specific standards, methods, or tests that should be used to verify efficiency claims, the 2006 *Commentary on the Horizontal Merger Guidelines*[75] ("Commentary on the Horizontal Merger Guidelines") provides

[72] *l Merger Guidelines*, § 10 at 30.

[73] *Merger Guidelines*, § 10 at 30.

[74] *Merger Guidelines*, § 10 at 30.

[75] U.S. Department of Justice & Federal Trade Commission's *Commentary on the Horizontal Merger Guidelines*, dated Mar. 2006.

guidance on the documentation the DOJ and FTC look for to substantiate efficiency claims, and the process they use to verify those claims.

71. The *Commentary on the Horizontal Merger Guidelines* notes that, "[t]he best way to substantiate an efficiency claim is to demonstrate that similar efficiencies were achieved in the recent past from similar actions. Documentation must be based on appropriate methods and realistic assumptions, and ideally would be grounded on actual experience."[76] It naturally follows that in order for an extrapolation of the cost savings experienced from a previous merger to form the basis of cognizable efficiencies in a subsequent merger, the cost savings from the previous merger must also be cognizable (verifiable, and merger-specific, and not the result of anticompetitive reductions in output or service).[77]

72. The *Commentary on the Horizontal Merger Guidelines* also describes the verification process, stating:[78]

> After the parties have presented substantiation for their claimed merger-specific efficiencies, the Agencies attempt to verify those claims. The verification process usually includes, among other things, an assessment of the parties' analytical methods, including the accuracy of their data collection and measurement, an evaluation of the reasonableness of assumptions in the analysis, and scrutiny into how well the parties' conclusions stand up to modifications in any assumptions (i.e., the "robustness" of the parties' analysis).

[76] U.S. Department of Justice & Federal Trade Commission's *Commentary on the Horizontal Merger Guidelines*, dated Mar. 2006, § 4 at 53.

[77] *See generally Merger Guidelines*, § 10 at 30.

[78] U.S. Department of Justice & Federal Trade Commission's *Commentary on the Horizontal Merger Guidelines*, dated Mar. 2006, § 4 at 52.

73. Consistent with the *Merger Guidelines*, the *Commentary on the Horizontal Merger Guidelines* summarized above, and the basic principles in accounting, economics, and finance, I assess whether the Claimed Efficiencies can be verified by analyzing whether the Merging Parties have:

a. Provided adequate documentation to support and explain each of the Claimed Efficiencies;

b. Used standard, widely accepted and reliable principles, methods, and analyses to measure the Claimed Efficiencies and employed them appropriately; and

c. Used facts and data, the foundation of any economic analyses, to support the inputs and assumptions used in these analyses.

74. This framework and methodology are consistent with the *Merger Guidelines*, the *Commentary on the Horizontal Merger Guidelines*, and basic principles in accounting, economics, and finance.

2. Assessing Merger-Specificity of Efficiencies

75. The *Merger Guidelines* define "merger-specific efficiencies" as "those efficiencies likely to be accomplished with the proposed merger and unlikely to be accomplished in the absence of either the proposed merger or another means having comparable anticompetitive effects."[79] As discussed in the *Commentary on the Horizontal Merger Guidelines*, an efficiency may be "merger-specific," even if it theoretically could be achieved without a merger, if for example, the other means were not practically feasible or would impose substantial transaction costs.[80] The *Merger Guidelines* further explain

[79] *Merger Guidelines*, § 10 at 30.

[80] U.S. Department of Justice & Federal Trade Commission's *Commentary on the Horizontal Merger Guidelines*, dated Mar. 2006, § 4. Specifically, the *Commentary on the Horizontal Merger Guidelines* states, "[t]hat an efficiency theoretically could be achieved without a merger—for example, through a joint venture or contract—does not disqualify it from consideration in the analysis. Many joint venture agreements or contracts may not be practically feasible or may impose substantial transaction costs (including monitoring costs). In their assessment of

that, "[t]he Agencies will not deem efficiencies to be merger-specific if they could be attained by practical alternatives that mitigate competitive concerns, such as divestiture or licensing. If a merger affects not whether but only when an efficiency would be achieved, only the timing advantage is a merger-specific efficiency."[81]

76. The *Commentary on the Horizontal Merger Guidelines* further states: [82]

> [T]he parties may believe that they can reduce costs by adopting each other's "best practices" or by modernizing outdated equipment. But, in many cases, these efficiencies can be achieved without the proposed merger. The presence of other firms in the industry unilaterally adopting similar "best practices" would suggest that such cost savings are not merger-specific. By contrast, if a "best practice" is protected by intellectual property rights, then it could be the basis for a merger-specific efficiency claim.

In other words, the "best practices" portion of an efficiency that could be practically achievable through other means and is not protected by intellectual property rights is generally not merger-specific.[83]

77. This framework and methodology are consistent with the *Merger Guidelines*, the *Commentary on the Horizontal Merger Guidelines*, and basic principles in accounting, economics, and finance.

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proffered efficiency claims, the Agencies accord appropriate weight to evidence that alternatives to the merger are likely to be impractical or relatively costly." (U.S. Department of Justice & Federal Trade Commission's *Commentary on the Horizontal Merger Guidelines*, dated Mar. 2006, § 4 at 50).

[81] *Merger Guidelines*, § 10 at 30 n.13.

[82] U.S. Department of Justice & Federal Trade Commission's *Commentary on the Horizontal Merger Guidelines*, dated Mar. 2006, § 4 at 50-51.

[83] I note that if a merger can speed the adoption of best practices by the merging parties, then best practices may be a cognizable efficiency, but only for the limited time period until the merging parties could have developed best practices independently.

3. Concluding Comments on the Framework and Methodology

78. As I stated above, the analysis of the cognizable efficiencies claimed by the Merging Parties in the *Merger Guidelines* requires assessing whether the Claimed Efficiencies are: (1) merger-specific, (2) verifiable, and (3) not the result of anticompetitive reductions in output or service.[84] It is widely accepted that accounting, economic, financial analysis, and valuation experts analyze efficiencies claimed in mergers to assist the trier of fact in assessing whether efficiencies are cognizable based on these criteria.[85]

79. Lastly, I note that a finding that a claimed efficiency is not verifiable does not mean that the claimed efficiency does not exist (has a $0 value); rather, it means that the merging parties have not provided sufficient foundation to substantiate the magnitude of the claimed efficiency or to assess the likelihood that a meaningful efficiency will be realized. Said differently, the information provided by the merging parties does not allow a third party to distinguish the magnitude of the claimed efficiency from, for example, 0% or 1% of the amount claimed and 200% or 300% of the amount claimed.

B. Summary of CP's Claimed Efficiencies

80. In this section, I provide a summary of the CP Claimed Efficiencies. CP presented a summary of the Claimed Efficiencies in Appendix B ("Summary of Benefits Exhibit") of Volume 1 of the CP/KCS Application (Total Merger Benefits in the CP/KCS Application). The Summary of Benefits Exhibit partitions the Claimed Efficiencies into two main components: (i) Operating Revenue Gains; and (ii) Operating Benefits. In

[84] *Merger Guidelines*, § 10 at 30. I note that I have not been asked to comment on whether the Claimed Efficiencies are the result of anticompetitive reductions in output or service at this time.

[85] I note that the *Merger Guidelines* state, "[t]he Commentary on the Horizontal Merger Guidelines issued by the Agencies in 2006 remains a valuable supplement to these Guidelines." *Merger Guidelines*, § 1 at 1 n.1.

Exhibit III-2 and presented in the table below, I provide a summary of the Summary of Benefits Exhibit presented by the CP.

Table 4
Summary of Benefits (CP's Claimed Efficiencies)

USD million

SUMMARY OF BENEFITS	NORMAL YEAR
Benefit Component	
OPERATING REVENUE GAINS	
Revenue Increase from Traffic Gains	1,021.9
Cost of Handling Added Traffic:	(306.3)
Net Revenue Gains	**715.6**
OPERATING BENEFITS	
Mechanical	19.9
Transportation	62.5
Equipment Requirements	12.8
Purchasing (Procurement)	20.5
Subtotal	115.7
Support Functions (G&A)	57.1
Total Operating Benefits	172.8
Employee Separation/Relocation	-
Total Merger Benefits	**888.4**

Source: CP/KCS Application Vol I, p. 74 (Appendix B - Summary of Benefits Exhibit)

81. I discuss each of these components below.

1. Operating Revenue Gains

82. In this section, I summarize the Claimed Efficiencies related to the Operating Revenue Gains.

i. Revenue Increase from Traffic Gains

83. The first component of the Operating Revenue Gains is the assumed estimated increase in revenue from traffic gains ("Revenue Increase from Traffic Gains"). CP claims it will achieve $1.0 billion of additional revenue from traffic gains in a "Normal Year."[86] The $1.0 billion Revenue Increase from Traffic Gains is made up of three components of additional revenue: (i) $513.1 million from rail-to-rail diversions; (ii) $98.2 million from truck-to-rail diversions; and (iii) $411.4 million from attracting new rail traffic.

84. The $513.1 million of additional revenue from rail-to-rail diversions is addressed and estimated in the Verified Statement of Richard Brown, a consultant in the Network Industry Strategies practice at FTI, and Nathaniel S. Zebrowski, managing director in the Network Industry Strategies practice at FTI ("Brown and Zebrowski VS").[87] The Brown and Zebrowski VS explains, "[a]s part of the assessment of the market impacts of Canadian Pacific Railway's ('CP') proposed acquisition of control of Kansas City Southern ('KCS'), we have been asked by CP to estimate the amount of railroad traffic that would shift from movement on other railroads to the combined CP/KCS system as a result of the new service offerings, more efficient single-line services, and other changes

[86] STB, Volume I, p. 74 (Summary of Benefits Exhibit).

[87] Verified Statement of Richard W. Brown and Nathaniel S. Zebrowski before the Surface Transportation Board, dated October 28, 2021. Finance Docket No. 36500.

resulting from the Transaction. Such traffic shifts are commonly referred to as rail-to-rail diversions."[88]

85. The $98.2 million of additional revenue from truck-to-rail diversions is addressed and estimated in the Verified Statement of Bengt Muten, Consulting Principal at IHS Markit, ("Muten VS").[89] The Muten VS explains that he was asked "to estimate the expected diversions of current truck traffic to intermodal services the combined Canadian Pacific ('CP') and KCS system will offer."[90]

86. The $411.4 million of additional revenue from attracting new rail traffic is addressed and estimated in the Verified Statement of Jonathan Wahba, Vice President of Commercial Integration at CP, and Michael J. Naatz, Executive Vice President and Chief Marketing Officer at KCS ("Wahba and Naatz VS").[91] The Wahba and Naatz VS explains, "[i]n this statement, we drill down to describe in more detail – and on a commodity-by commodity basis – some of the key opportunities CPKC intends to pursue to bring the benefits of the Transaction to customers across North America."[92]

ii. Costs of Handling Added Traffic

87. CP claims that there will be additional costs related to the Revenue Increase from Traffic Gains in the amount of $306.3 million ("Costs of Handling Added Traffic").[93] The Costs

[88] Brown and Zebrowski VS, p. 4.

[89] Verified Statement of Bengt Mutén before the Surface Transportation Board, dated October 28, 2021. Finance Docket No. 36500.

[90] Muten VS, pp. 2-3.

[91] Verified Statement of Jonathan Wahba and Michael J. Naatz before the Surface Transportation Board, dated October 29, 2021. Finance Docket No. 36500.

[92] Wahba and Naatz VS, p. 4.

[93] STB, Volume I, p. 74 (Summary of Benefits Exhibit).

of Handling Added Traffic are discussed and estimated in the Verified Statement of Michael Baranowski, Sr. Managing Director at FTI, ("Baranowski VS"),[94] which "develop[s] the total dollar value of the operating savings resulting from the Canadian Pacific ('CP')/Kansas City Southern ('KCS') combination, as quantified in the Operating Plan (Exhibit 13 to the Application) and … estimate[s] the additional costs, revenues, and net revenues that would be associated with the additional traffic the CP/KCS system would attract as a result of the merger through extended hauls, rail-to-rail diversions, and truck-to-rail diversions."[95]

88. The Costs of Handling Added Traffic have the following components and amounts:[96]

a. Engineering – Maintenance of Way: $38.8 million
b. Mechanical: $23.4 million
c. Transportation: $204.8 million
d. Equipment Requirements & Utilization: $13.6 million
e. Intermodal Operations: $25.7 million

89. These costs are calculated by multiplying the number of diverted units by the applicable costs for those units (for example, the number of diverted automotive units times the mechanical cost per additional unit).[97]

2. Operating Benefits

90. The Operating Benefits ("Claimed Operating Benefits") include Mechanical, Transportation, Equipment Requirement & Utilization, Purchasing Claimed Efficiencies, which total $115.7 million, which are addressed and estimated in the Baranowski VS.

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[94] Verified Statement of Michael R. Baranowski before the Surface Transportation Board, dated October 28, 2021. Finance Docket No. 36500.

[95] Baranowski VS, p. 3 (footnotes omitted).

[96] Baranowski VS, p. 26.

[97] See FD 36500 – Work Paper – HC – URCS Phase III Calculation For Growth Traffic.

The remainder of the Claimed Operating Benefits consist of general & administrative ("G&A") savings of $57.1 million and are primarily addressed in the Verified Statement of Dean Vargas, the Managing Director of Revenue Planning at CP, ("Vargas VS").[98] I discuss each of these components below.

i. Mechanical

91. The Baranowski VS calculates mechanical savings ("Claimed Mechanical Savings") by calculating claimed operating metrics savings of $52.6 million[99] and allocating a portion of those claimed savings to mechanical operations.[100] The Baranowski VS calculates the claimed operating metrics savings by multiplying the reduction in each operating metric which it identifies (train miles, locomotive unit miles, locomotive gross ton miles, and I&I switches) by "the dollar savings attributable to the operating metric reductions … [based] upon relevant unit costs from the URCS [Uniform Rail Costing System]."[101] Of the total $52.6 million of claimed operating metrics savings, the total Claimed Mechanical Savings are $19.9 million.

ii. Transportation

92. The Baranowski VS calculates transportation savings ("Claimed Transportation Savings") by adding together claimed fuel savings and the claimed operating metrics

[98] Vargas VS.

[99] Baranowski VS, p. 6.

[100] The remaining claimed operating metrics savings are allocated to transportation operations, which I discuss in the next section.

[101] Baranowski VS, p. 5.

savings that were not allocated to the Claimed Mechanical Savings.[102] To calculate the claimed fuel savings, the Baranowski VS states, "I calculated the difference between the number of gallons that would have been consumed … at the base year consumption rate for KCSR and KCSM, and the gallons at the revised consumption rates at each year's projected volumes. I then multiplied the KCS difference by an average price per gallon of $2.04 … and the KCSM difference by an average price of $3.08."[103] The claimed fuel savings are $29.8 million, and the total Claimed Transportation Savings are $62.5 million.

iii. Equipment Requirements & Utilization

93. The Baranowski VS estimates $12.8 million of claimed equipment requirements & utilization costs savings ("Claimed Equipment Savings"), which is equal to the expected savings from the claimed locomotive depreciation and lease annual expense plus the claimed freight cars expense. The Baranowski VS explains the process by which the claimed locomotive depreciation and lease annual expense was calculated:[104]

> The reduction in locomotive unit miles between the base and optimized operating plan will achieve savings for locomotive depreciation and lease costs. I calculated these savings by applying the URCS locomotive depreciation and lease costs per locomotive unit mile and per gross ton mile to the locomotive unit miles saved between the base and the optimized operating plan and the equivalent affected gross ton miles.

[102] While the Baranowski VS calculates the components that make up the Claimed Transportation Savings, the Baranowski VS never specifically identifies the Claimed Transportation Savings; rather, the Claimed Transportation Savings is identified in the Summary of Benefits Exhibit (Appendix B to the CP/KCS Application).

[103] Baranowski VS, p. 7.

[104] Baranowski VS, p. 8.

94. The Baranowski VS also explains the process by which the claimed freight cars expense was calculated:[105]

> CP personnel identified specific reductions in locomotive and freight car counts for the combined system before any extended hauls or traffic diversions … Applicants have determined that full service lease costs for the types of freight cars identified … average $4,800 annually. Based on this number, I calculated the cumulative cost savings attributable to freight cars.

iv. Purchasing (Procurement)

95. The Baranowski VS estimates $20.5 million of claimed procurement savings ("Claimed Procurement Savings"). The Baranowski VS explains the process by which the Claimed Procurement Savings were determined: [106]

> CP identified the total spend by major expense category for which prices are negotiated routinely as part of the procurement process. For each category, CP reviewed the scope of the combined CP/KCS spend and identified opportunities for savings. These opportunities range from increased overall purchase volumes that allow for negotiation of lower rates to the extension of existing favorable terms or best practices to the other carrier. CP then determined the estimated percentage savings from 2019 spend levels that could be achieved in future negotiations by the combined CP/KCS.

v. General & Administrative

96. The Vargas VS summarized "the general and administrative ('G&A') cost savings that CP/KCS expects to realize from the Transaction and describe how these savings were developed."[107] The Vargas VS estimates G&A savings of $57.1 million, which is

[105] Baranowski VS, pp. 9-10.

[106] Baranowski VS, p. 10.

[107] Vargas VS, p. 2.

comprised of personnel savings of $43.7 million and non-personnel savings of $13.4 million ("Claimed G&A Savings").[108]

97. The headcount reductions upon which the personnel savings of $43.7 million are based are addressed in the verified statement of Chad Rolstad, the Vice President of Human Resources and Chief Culture Officer of CP, ("Rolstad VS"),[109] which "explain[s] the steps CP anticipates taking to manage the small number of changes in the non-agreement labor force that will result from implementing the proposed combination of CP and KCS under CP control."[110]

98. The non-personnel savings of $13.4 million estimated in the Vargas VS are comprised of the following components:

- Non-personnel expenditures ($2.0 million): "non-personnel expenditures that will decrease with a reduction in personnel levels, such as business travel and meals, training, and mobile communication."[111]
- IT (Licensing/Subscriptions/Contract Services) ($8.1 million): "These saving [*sic*] will be achieved through … rationalizing IT software licensing and subscription fees, and insourcing of outsourced IT contract services."[112]
- Facilities ($1.4 million): "These saving will be achieved through consolidating the CP and KCS U.S. operating headquarters in Kansas City, eliminating a duplicative IT data center in Minneapolis."[113]
- Audit and listing fees ($1.8 million): "... from eliminating duplicative fees and expenses related to reporting as a publicly traded company, given that the two

[108] Vargas VS, pp. 5-6.

[109] Verified Statement of Chad Rolstad before the Surface Transportation Board, dated October 28, 2021. Finance Docket No. 36500.

[110] Rolstad VS, p. 2.

[111] Vargas VS, p. 6.

[112] Vargas VS, pp. 6-7.

[113] Vargas VS, pp. 6-7.

railroads will report financial results as a single consolidated company. Examples of these duplicative costs include audit and stock exchange listing fees."[114]

C. Analysis of Claimed Efficiencies

99. In this section, I provide my assessment of whether the Claimed Efficiencies are cognizable (verifiable and merger-specific). In my analysis and assessment of the Claimed Efficiencies, I rely on several of the verified statements prepared by experts from Oliver Wyman, a global management consulting firm, that was asked to review certain of the Claimed Efficiencies. Specifically, I have reviewed and rely upon the following verified statements:

- Verified Statement of David T. Hunt related to the expected revenues achievable by the Merged Company ("Hunt VS");[115]
- Verified Statement of Hugh Randall related to the operating costs on the incremental revenue and the forecasted capital expenditures ("Randall VS");[116] and
- Verified Statement of Carl Van Dyke related to the operating plan of CP and KCS ("Van Dyke VS").[117]

1. Revenue Increase from Traffic Gains

100. In this section, I assess the verifiability of claimed revenue efficiencies. I understand that the Hunt VS has also analyzed CP's claimed revenue efficiencies from the perspective of a railroad industry expert, and "review[ed] and comment[ed] on Applicants' testimony regarding the traffic diversions and associated revenues that are

[114] Vargas VS, pp. 6-7.

[115] Verified Statement of David T. Hunt before the Surface Transportation Board, dated February 28, 2022. Finance Docket No. 36500.

[116] Verified Statement of Hugh Randall before the Surface Transportation Board, dated February 28, 2022. Finance Docket No. 36500.

[117] Verified Statement of Carl Van Dyke before the Surface Transportation Board, dated February 28, 2022. Finance Docket No. 36500.

likely to be achieved by the merged CPKC as a result of the proposed transaction."[118] I review the Hunt VS and provide additional analysis interpreting its findings from the perspective of a financial economist and the *Merger Guidelines*.

i. The Baseline Forecasted Market Share that the Merged Company Will Achieve from Rail-to-Rail Diversions Is Not Verifiable

101. The Brown and Zebrowski VS explains the methodology it used to estimate rail-to-rail diversions: "We applied the starting point diversion percentages shown in Table 7 below to project the amount of traffic that will divert to CP/KCS, but as noted below our diversion estimates considered further individualized factors that led us to apply adjustments."[119] As shown in Table 7 of the Brown and Zebrowski VS, the "starting point diversion percentages" are 25% for "[t]raffic moves via single-line option via other carriers," 50% for "[t]raffic moves via interline service via other carriers," 50% or 75% for "CP or KCS participates in traffic via interline service with other carriers," and 75% for "[t]raffic moves in interline service via two interchanges, with CP and KCS at origin or destination and a third bridge carrier."[120]

102. I am not aware of any quantitative analysis or foundation substantiating these baseline diversion percentages. Therefore, given the lack of foundation to support the inputs and assumptions used in this analysis, while it is likely that the Merged Company may achieve some diversions, these claimed diversion percentages cannot be verified.

103. I understand that the Hunt VS has also analyzed the expected incremental revenue per unit from the perspective of a railroad industry expert. The Hunt VS states: "Witnesses

[118] Hunt VS, Section 2.

[119] Brown and Zebrowski VS, p. 22.

[120] Brown and Zebrowski VS, p. 22.

Brown and Zebrowski apply fixed diversion percentages of 25, 50, or even 75 percent that are unsupported by any credible rationale."[121] The Hunt VS's conclusion that the diversion percentages are "unsupported by any credible rationale" provides additional evidence that the revenue per incremental unit of rail-to-rail diversions is not verifiable.

ii. The Forecasted Revenue per Diverted Rail-to-Rail Carload Is Not Verifiable

104. The Brown and Zebrowski VS explains how it estimates incremental revenue per unit: "In light of the factors noted above, and the incentives that incumbent carriers will have to seek to retain the traffic in which they currently participate, we considered it appropriate to assume that CP/KCS would be required to offer rate reductions averaging five percent in order to attract traffic away from existing single-line service to CP/KCS single-line service."[122] I am not aware of any quantitative analysis or foundation that substantiates this 5% reduction in rates is sufficient to realize the forecasted diversions. Therefore, these rates cannot be verified.

105. I understand that the Hunt VS has also analyzed the expected incremental revenue per unit from the perspective of a railroad industry expert. The Hunt VS concluded that "Revenue for post-merger diverted traffic is overstated by $47.4 million due to errors."[123] Specifically, the Hunt VS explains that "the revenue gain for CPKC from diverted traffic should logically reflect the approximate revenue that would be lost by the railroads that currently haul that traffic"[124] and notes that the Brown and Zebrowski VS "considered it

[121] Hunt VS, Section 3.

[122] Brown and Zebrowski VS, p. 21.

[123] Hunt VS, Section 4.2.

[124] Hunt VS, Section 4.2.

appropriate to assume that CP/KCS would be *required to offer rate reductions averaging five percent in order to attract traffic away* from existing single-line service."[125] However, the Hunt VS shows that, due to errors in the Brown and Zebrowski VS's analysis, "the incremental revenue per diverted carload claimed by witnesses Brown and Zebrowski in many cases exceeds the rates currently charged by the incumbent carrier."[126] The Hunt VS concludes that "[i]f Brown and Zebrowski's revenue estimates are accurate, it is hard to see how Applicants can claim that diverting this traffic will be beneficial to shippers, who (according to Brown and Zebrowski's revenue assumptions) would be charged significantly more than the current 'going rate' to move those shipments over longer, more circuitous routes."[127] Thus, these errors identified in the Hunt VS provide additional evidence that the revenue per incremental unit of rail-to-rail diversions is not verifiable.

iii. The Additional Rail-to-Rail Diversions are not Verifiable

106. Additional rail-to-rail diversions are also not verifiable.

Grains

107. Regarding grains, the Wahba and Naatz VS states: "Given our knowledge of the market and our customers, we expect the Transaction to lead to at least a five percent increase in the CP/KCS share of all grains exported from the United States to Mexico."[128] The

[125] Brown and Zebrowski VS, p. 21, ¶32 (emphasis added).

[126] Hunt VS, Section 4.2.

[127] Hunt VS, Section 4.2.

[128] Wahba and Naatz VS, p. 11.

Brown and Zebrowski VS corroborates this claim with its own professional judgement.[129] I am not aware of any quantitative analysis or foundation, however, that substantiates this 5% increase in market share. Therefore, while it is likely that the Merged Company may achieve some increase in market share, this increase in market share cannot be verified.

108. I understand that the Hunt VS has also analyzed the expected increase in market share from the perspective of a railroad industry expert. The Hunt VS states: "This (unexplained) assumption, which increases total revenues from diverted grain shipments in the Brown and Zebrowski diversion model by more than 340 percent, does not appear to be based on any movement-specific analysis … There is no justification or evidentiary support for … this arbitrary increase in CPKC's post-merger grain traffic."[130] This provides additional evidence that the increase in market share is not verifiable.

Lumber

109. Regarding lumber, the Brown and Zebrowski VS states: "In addition to CP/KCS's increased ability to attract Canadian lumber traffic that CP currently hands off to other U.S. carriers, CP/KCS's new single-line routes will also enable it to originate a larger share of lumber from Canadian mills served by both CP and CN (and where CN dominates). We estimate this additional traffic by identifying lumber mills CP can access in Alberta, British Columbia, Ontario, and Quebec, and assuming CP increases its share by five percentage points and moves that traffic to destinations in Dallas and other destinations to either displace existing supply or accommodate future growth."[131] I am

[129] Brown and Zebrowski VS, pp. 25-27.

[130] Hunt VS, Section 4.3.

[131] Brown and Zebrowski VS, p. 44.

not aware of any quantitative analysis or foundation, however, that substantiates this 5% increase in market share. Therefore, while it is likely that the Merged Company may achieve some increase in market share, this increase in market share cannot be verified.

110. I understand that the Hunt VS has also analyzed the expected increase in market share from the perspective of a railroad industry expert. The Hunt VS states: "Witnesses Brown and Zebrowski provide no analysis or calculations to support these market share and growth assumptions. In total, these adjustments account for 2,038 additional carloads, or 56 percent of all incremental revenue from lumber diversions."[132] This provides additional evidence that the increase in market share is not verifiable.

iv. Additional Incremental Revenues Forecasted by the Wahba and Naatz VS Are Not Verifiable

111. The Wahba and Naatz VS identifies additional incremental revenues beyond those identified in the Brown and Zebrowski VS and the Mutén VS. These additional incremental revenues are calculated by identifying the average revenues per car at 2019 levels for certain routes and multiplying that revenue by an estimate of fully phased in units.[133] The Wahba and Naatz VS does not provide an explanation of how almost all of the additional fully phased in units are calculated. With one exception,[134] the values of fully phased in units are either hardcoded[135] or come from calculations that are based on

[132] Hunt VS, Section 4.3.

[133] FD 36500 – Work Paper – HC – Growth Initiative Calculations.xlsx.

[134] FD 36500 – Work Paper – HC – Growth Initiative Calculations.xlsx, cell E23. The one exception is the domestic perishables from Michoacan/Veracruz to Chicago/Twin Cities/Kansas City-2. With regards to perishables, the Hunt VS states, "Applicants do not explain why these shipments are divertible, or why witness Mutén (who clearly was aware of the movements) did not judge them to be divertible." (Hunt VS, Section 5.3).

[135] See, for example, FD 36500 – Work Paper – HC – Growth Initiative Calculations.xlsx, cells E6, E9, and E21.

hardcoded and/or unexplained values.[136] Therefore, while it is possible that the Merged Company may achieve some additional incremental revenues, the total additional incremental revenues forecasted by the Wahba and Naatz VS are not verifiable.

112. I understand that the Hunt VS has also analyzed the expected additional incremental revenues forecasted by the Wahba and Naatz VS from the perspective of a railroad industry expert. The Hunt VS states, "These additional traffic volumes and revenues – which account for $411 million or 40 percent of the total incremental revenue gains set forth in the Application – are based on unrealistic assumptions and unsupported claims."[137] The Hunt VS additionally states: "witnesses Wahba and Naatz are claiming [LPG] traffic that does not currently exist."[138] The Hunt VS's conclusion that the claimed additional incremental revenues lack foundation provides additional evidence that the additional incremental revenues forecasted by the Wahba and Naatz VS are not verifiable.

v. Additional Incremental Revenues Forecasted by the Wahba and Naatz VS Are Not Merger-specific

113. Additional rail-to-rail diversions forecasted by the Wahba and Naatz VS are not merger-specific.

Crude oil

114. Regarding crude oil, the Wahba and Naatz VS states: "The new single-line service unlocked by the CP/KCS Transaction will support the investments needed to accelerate

[136] See, for example, FD 36500 – Work Paper – HC – Growth Initiative Calculations.xlsx, cells E4, E5, and E12.

[137] Hunt VS, Section 3.

[138] Hunt VS, Section 5.3.

the transition away from traditional crude-by-rail and towards the movement of Alberta crude in private cars in non-hazardous DRUbit form."[139] I understand from the Hunt VS, however, that "a crude oil movement from Hardisty, AB to Port Arthur, TX … was made public by the shipper, Gibson Energy, in December 2019" and therefore "this rail movement clearly predates the merger."[140] If incremental revenues can be realized without a merger, then it logically follows that a merger is unnecessary to realize these specific benefits. The incremental revenues from crude oil are not merger-specific and are not cognizable.

Diversions that exclusively utilize the KCS network

115. I understand from the Hunt VS that the Wahba and Naatz VS "attribute[s] $21.1 million … in merger-related benefits to Lazaro Cardenas – Kansas City diversions and another $22.9 million to Lazaro Cardenas-Dallas diversions, routes where KCS could provide single-line service on a stand-alone basis today."[141] I am aware of no reason that has been provided as to why KCS could not realize these diversions as an independent company, and therefore, based on the conclusions presented in the Hunt VS, these diversions are not merger-specific.

2. Cost of Handling Added Traffic

116. In this section, I assess the verifiability of the Claimed Cost of Handling Added Traffic. I understand that the Randall VS has analyzed CP's Claimed Cost of Handling Added Traffic from the perspective of a railroad industry expert, and that it "review[ed] and

[139] Wahba and Naatz VS, p. 43.

[140] Hunt VS, Section 5.1.

[141] Hunt VS, Section 5.2.

comment[ed] on … Applicants' projected post-merger operating expenses."[142] The Randall VS concludes that "Applicants' projected operating expenses for the first three post-merger years are understated by approximately $2.47 billion when compared to the operating expenses actually incurred by CP US and KCS US during the 2015-2019 period."[143]

117. Below, I provide an analysis of the Costs of Handling Added Traffic, which interprets the related verified statements from the perspective of a financial economist and the *Merger Guidelines*.[144]

i. The Cost for Diverted Units Is Not Verifiable

118. The Baranowski VS explains that it calculates the incremental cost per diverted unit by "develop[ing] a model that replicates certain of the relevant URCS costing procedures for the cost components that are affected directly by the traffic shifts that are not accounted for in other analyses undertaken by CP."[145] The Randall VS explains, however, that "Applicants did not base their estimate of incremental operating expenses on the analyses or outputs of their operating plan or system model. Instead, Applicants based their estimate solely on a table of incremental operating expenses that is hard-coded into an

[142] Randall VS, Section 2. The Randall VS explains, "Solely for purposes of this Verified Statement, I have assumed that the envisioned merged railroad, CPKC, will achieve the traffic increases projected in the Application" (Randall VS, Section 2).

[143] Randall VS, Section 4.

[144] I note that the Randall VS "review[s] and comment[s] on … Applicants' estimate of the capacity improvements and other capital expenditures that would be required to handle the additional traffic volumes projected by Applicants safely and efficiently" and concludes that "Applicants' [c]apital [e]xpenses [a]re [s]ignificantly [u]nderstated" (Randall VS, Sections 2-3). I note that to the extent that the Randall VS is correct that the Merged Company underestimates its required capital expenditures, that is further evidence that the costs of revenue efficiencies are understated and not verifiable.

[145] Baranowski VS, p. 15.

unsourced spreadsheet in Applicants' work papers"[146] and that "operating expenses reflected in the Application are nothing more than assumptions that are unsupported by documentation or analysis."[147] Consistent with the finding presented in the Randall VS, I am aware of no facts, calculations, or detailed methodology for the Baranowski VS's calculation of the incremental cost per diverted unit. Therefore, given the lack of sufficient documentation and foundation underlying these assumptions and consistent with the *Merger Guidelines*, I find that the cost per diverted unit is not verifiable.

119. The Baranowski VS calculates the total cost for diverted units by multiplying the incremental cost per diverted unit by the total number of diverted units of each type.[148] As I discussed in Section III.C.1, however, the total number of diverted units is not verifiable. Therefore, neither the cost per unit, nor the number of units, is verifiable and the total cost for diverted units is also not verifiable.

3. Operating Benefits

120. In this section, I assess the claimed Operating Benefits of the Transaction.[149] Those claimed Operating Benefits are divided into Claimed Mechanical Savings, Claimed

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[146] Randall VS, Section 4.

[147] Randall VS, Section 4. In addition, I understand that the Randall VS opines that certain categories of costs were inappropriately excluded from the calculations of the cost of handling additional traffic (Randall VS, Section 4.2).

[148] FD 36500 – Work Paper – HC – URCS Phase III Calculation For Growth Traffic.xlsm, tab Incremental Costs by Category.

[149] I note that the Randall VS has analyzed the speed at which the Claimed Operating Benefits will be realized. The Randall VS states: "Since CP cannot begin to physically integrate its network with KCS or influence KCS operations until the merger is approved, it is unlikely that Applicants would be able to implement all of the operating changes required to generate virtually all of the achievable operating expense savings in the first post-merger year" (Randall VS, Section 4). This provides additional evidence that the rate at which certain claimed cost efficiencies will be realized is not verifiable, further reducing the extent to which these efficiencies are cognizable. See also the *Merger Guidelines*, which explain that "Delayed benefits from efficiencies (due to delay in the achievement of, or the realization of customer benefits from, the efficiencies) will be given less weight because they are less proximate and more difficult to predict" (*Merger Guidelines*, § 10 at 31 n.15).

Transportation Savings, Claimed Equipment Savings, Claimed Procurement Savings, and Claimed G&A Savings.[150]

i. Mechanical

121. As I discussed in Section III.B.2.i, the Claimed Mechanical Savings are equal to a portion of the total claimed operating metrics savings calculated by the Baranowski VS. The Baranowski VS explains that its calculations of the claimed operating metrics savings "reflect[] the operations of a consolidated CP/KCS network … It does this in two phases: first, by identifying the operational efficiencies that arise from operating a larger, fully integrated and optimized network that *adopts the best practices of both railroads*, and second, by planning for and assessing the operations (including capacity additions) that would accommodate the increased traffic the combined system will attract."[151] As I explained Section III.A.2, savings from "best practices" are not merger-specific and thus would not be considered cognizable efficiencies. Therefore, to the extent that the Claimed Mechanical Savings are expected to be realized via adoptions of best practices, they are not cognizable efficiencies, or, at best, cognizable for a limited time period.[152]

122. In addition, I understand that some or all of the Claimed Mechanical Savings are due to implementation of precision scheduled railroading ("PSR").[153] However, the Randall VS

[150] I do not discuss claimed savings from Engineering – Maintenance of Way or Intermodal Operations because they do not have benefits in the Normal Year.

[151] Baranowski VS, pp. 4-5 (emphasis added).

[152] As I explained above when I discussed the framework and methodology to assess merger efficiencies, I note that if a merger can speed the adoption of best practices by the merging parties, then best practices may be a cognizable efficiency, but only for the limited time period until the merging parties could have developed best practices independently.

[153] Specifically, the Randall VS explains that "Without identifying what specific expense reduction measures would be implemented in Year 1, witness Baranowski assumes that CPKC will realize this extremely high percentage of total projected operating expense savings during the first year of the merger, (supposedly) by implementing CP's precision scheduled railroading (PSR) on KCS" (Randall VS, Section 4.3).

explains that "a significant portion of the implementation of PSR has already been realized by KCS without the merger. Beginning in January 2019, KCS commenced an aggressive initiative to implement PSR, which helped to reduce its operating ratio from 69.1 percent in 2019 to 62.2 percent in 2020."[154] Therefore, based on the criteria found in the *Merger Guidelines*, these claimed cost reductions are not merger-specific[155] and thus are not considered cognizable efficiencies.

123. Finally, I note that the expected reduction of train miles per day for KCS's US and Mexican railroads, which is the core input that allows the Merging Parties to realize the Claimed Mechanical Savings, are hardcoded values that are calculated by "{{ }}"[156] I have not seen any explanation for this calculation, and given the lack of foundation to support the inputs and assumptions used in these analyses, the Claimed Mechanical Savings are not verifiable.[157]

ii. Transportation

124. As I discussed in Section III.B.2.i, the Claimed Transportation Savings are equal to a portion of the claimed operating metrics savings calculated by the Baranowski VS plus the claimed fuel savings. I already discussed the reasons that the claimed operating

[154] Randall VS, Section 4.3.

[155] *Merger Guidelines*, § 10 at 30 ("… those efficiencies likely to be accomplished with the proposed merger and unlikely to be accomplished in the absence of either the proposed merger or another means having comparable anticompetitive effects").

[156] FD 36500 – Work Paper – HC – CP Operating Plan Output Cost Metrics Model.xlsx, tab Model, cells C33 and C49.

[157] I note that the reduction in I&I switches is a hardcoded value that cannot be tied directly to FD 36500 – Work Paper – HC – CP Operating Plan Output Cost Metrics Model.xlsx, despite being sourced to this file (see FD 36500 – Work Paper – HC – Base to Optimized Operating Plan Savings.xlsx, tab Base to Optimized Metrics). Therefore, even if the reduction in I&I switches is not related to PSR, it is unexplained and therefore not verifiable.

metrics savings are not cognizable (not verifiable and not merger specific) in the previous section, Section III.C.3.i, and I do not repeat myself here. The Claimed Transportation Savings related to the claimed fuel savings are calculated by applying a "regression of horsepower per ton and gross ton-miles [for CP to the] forecast of Years 1 through 3 gross ton-miles and extrapolat[ing] the results to forecasts of KCSR and KCSM."[158] While a regression is a reasonable process to calculate an efficiency, the forecasts of gross ton-miles are closely linked to the forecasts of incremental revenues, which as I explained in Section III.C.1 are not verifiable. Therefore, the claimed fuel savings are not verifiable.

iii. Equipment Requirements

125. I understand that some or all of the Claimed Equipment Savings, other than the reduction in the claimed freight car expense, are due to implementation of PSR.[159] I already discussed the reasons that the claimed savings related to PSR are not cognizable (not verifiable and not merger specific) in Section III.C.3.i, and I do not repeat myself here. The Claimed Equipment Savings related to the claimed freight car expense is calculated with hardcoded inputs sourced from the Operating Plan.[160] The Van Dyke Verified Statement, however, explains that the Operating Plan is "incomplete and deeply flawed" and "cannot be relied upon in evaluating the impact of the proposed merger on CP-KCS operations, the operations of other railroads, or other stakeholders, such as shippers and

[158] Baranowski VS, p 7.

[159] Specifically, the Randall VS explains that "Without identifying what specific expense reduction measures would be implemented in Year 1, witness Baranowski assumes that CPKC will realize this extremely high percentage of total projected operating expense savings during the first year of the merger, (supposedly) by implementing CP's precision scheduled railroading (PSR) on KCS" (Randall VS, Section 4.3).

[160] FD 36500 – Work Paper – HC – Freight Car Savings.xlsx.

communities."[161] Therefore, the Claimed Equipment Savings related to the reduction in total freight cars is therefore not verifiable.

iv. Purchasing (Procurement)

126. The Baranowski VS calculates the Claimed Procurement Savings by multiplying different categories of costs by assumed savings percentages, which range from {{ }}% to {{ }}%, and which are all hard-coded values that include no additional support or foundation and thus cannot be verified.[162]

127. In addition, as the Baranowski VS explains, some of the savings are expected to result "… from increased overall purchase volumes that allow for negotiation of lower rates to the extension of existing favorable terms or *best practices* to the other carrier."[163] As I explained above, savings from "best practices" are not merger-specific and thus would not be considered cognizable efficiencies or, at best, cognizable for a limited time period.[164] In addition, while savings achieved via pooling purchasing volumes and realizing bulk purchasing discounts are merger-specific, to the extent any expected savings are due to simply realizing another party's more favorable purchasing terms for similar orders, that expected savings is not merger-specific and is therefore not cognizable.

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[161] Van Dyke VS, Section 2.

[162] FD 36500 – Workpaper – HC – CPKCS Procurement Synergies Study.xlsx.

[163] Baranowski VS, p. 10 (emphasis added).

[164] As I explained above when I discussed the framework and methodology to assess merger efficiencies, I note that if a merger can speed the adoption of best practices by the merging parties, then best practices may be a cognizable efficiency, but only for the limited time period until the merging parties could have developed best practices independently.

v. General & Administrative

128. In this section, I assess the Claimed G&A Savings of the Transaction. Those claimed savings are divided into personnel savings and several categories of non-personnel savings: non-personnel expenditures, information technology ("IT") expenditures, facilities, and audit & listing fees.

Personnel Savings

129. The claimed personnel savings are calculated by determining the total cost per employee at each title and division at CP and KCS (for example, the cost of an executive in corporate risk at KCS) and multiplying that total cost for each of those employees by the number of employees terminated at that level in that division from that railroad. These savings are then summed to determine total personnel savings.[165]

130. In Exhibit III-3, I present an example of the calculation of a portion of the claimed personnel savings. Specifically, I show the calculation of the claimed personnel savings related to the elimination of executives in corporate risk from KCS. First, I show the calculation of the total corporate risk executive salary per employee at KCS. This is equal to the KCS corporate risk executive salary plus expected incentive compensation and expected fringe rates compensation. Incentive compensation is equal to {{ }}% of base salary and fringe rates compensation is equal to {{ }}% of base salary. The sum of these three values is the total KCS corporate risk executive compensation per employee of ${{ }} per year. This salary is then multiplied by the total number of KCS corporate risk executive employees to be terminated: {{ }}.

[165] FD 36500 – Work Paper – HC – summary of benefits SG&A.xlsx, tabs Summary, Comp & headcount.

Therefore, the total claimed savings per year are ${{ }}. In order to calculate the total claimed personnel savings efficiency, the Baranowski VS then conducts a similar calculation for each different class of employees (divided by title and division) at each of CP and KCS. The total savings are then summed and represent the total claimed personnel efficiency.

131. While it is likely that the Merged Company may achieve some personnel savings, the personnel savings are not verifiable because CP (and the Vargas VS and the Rolstad VS) rely on unfounded and unsupported assumptions and use business judgment for the headcount reduction assumptions underpinning this claimed efficiency. I have seen no calculations or underlying foundation that provides substantiation of the headcount reductions at each company or the total amount of reduced headcount.

Non-Personnel Expenditures

132. The Vargas VS explains that the claimed non-personnel expenditures savings will be realized because "non-personnel expenditures … will decrease with a reduction in personnel levels."[166] As examples of these expenditures, the Vargas VS lists "business travel and meals, training, and mobile communication."[167] In Exhibit III-4, I show the calculation of the claimed non-personnel expenditures savings. As shown in this exhibit, the Baranowski VS calculates non-personnel expenditures savings for KCS and CP separately. For each railroad, non-personnel expenditures savings are equal to variable G&A per employee times the expected headcount reduction. The total expected savings are ${{ }} and ${{ }} for KCS and CP, respectively. The

[166] Vargas VS, p. 6.

[167] Vargas VS, p. 6.

total expected savings for the Merged Company is the sum of these values, ${{

}}.

133. However, given that this calculation relies upon the expected headcount reduction that, as I discussed above, is not verifiable, this claimed amount of savings is not verifiable either.

IT Expenditures

134. The Vargas VS explains that claimed IT expenditures savings "will be achieved through consolidating the CP and KCS U.S. operating headquarters in Kansas City, eliminating a duplicative IT data center in Minneapolis, rationalizing IT software licensing and subscription fees, and insourcing of outsourced IT contract services."[168]

135. In Exhibit III-5, I show the calculation of this claimed efficiency. The claimed efficiency is equal to the sum of seven categories of claimed IT savings, each of which is a hardcoded value.[169] The savings for each of these categories involves professional or business judgement, however, and each category of savings is calculated by applying estimated, rounded percentages to determine increased demand on IT resources (for licensing and network costs) or net IT savings (for other categories of IT costs).[170]

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[168] Vargas VS, p. 6.

[169] Each of these values is hardcoded in terms of CAD, which is then transformed into a USD value by applying an exchange rate conversion to the expected CAD costs savings (FD 36500 – Work Paper – HC – summary of benefits SG&A.xlsx, tab Non – comp).

[170] Infrastructure licensing and network costs savings are calculated "{{ }}" and "{{ }}" "{{ }}" "{{ }}" "{{ }}" "{{ }}" "{{ }}" "{{ }}"

Therefore, there are no rigorous calculations or underlying foundation that provides substantiation of the inputs to this efficiency, and while it is likely that the Merged Company may achieve some IT expenditures savings, this efficiency is unverified.

Facilities

136. The claimed facilities costs savings is based on the assumption that "{{

}}"[171] These costs are factual and are verified.

Audit & Listing Fees

137. The claimed audit & listing fees costs savings is calculated "from eliminating duplicative fees and expenses related to reporting as a publicly traded company, given that the two railroads will report financial results as a single consolidated company. Examples of these duplicative costs include audit and stock exchange listing fees."[172] In Exhibit III-6, I show the calculation of this claimed efficiency. As shown in this exhibit, the claimed efficiency is equal to the sum of avoided listing fees of $ {{ }} and auditor fees of $ {{ }}.

}}" (FD 36500 – Work Paper – HC – summary of benefits SG&A.xlsx, tabs Summary, Non – comp.)

[171] FD 36500 – Work Paper – HC – summary of benefits SG&A.xlsx, tabs Summary, Non – comp.

[172] Vargas VS, p. 6.

138. Professional or business judgement was used to assume that audit fees would be reduced by "{{ }}"[173] Therefore, because the only foundation for this assumption is business judgement, while it is likely that the Merged Company may achieve some savings related to audit fees, the savings cannot be verified.[174]

4. The Operating Ratio of the Merged Company Provides Additional Evidence that the Claimed Efficiencies Are Not Verifiable

139. The Randall VS provides additional evidence that the Claimed Efficiencies are not verifiable by comparing the forecasted cost for the Merged Company to benchmarks. The Randall VS states that "the projected operating expense per GTM for CPKC of $0.0126 during the first three post-merger years is well below historical benchmarks."[175] The Randall VS also states that the "changes in operating expense per GTM for all of the Class I railroads between 2009 and 2019 … strongly suggest[] that Applicants have significantly underestimated the operating expense per GTM that the combined CPKC system is likely to experience."[176] Furthermore, the Randall VS states that "the implied operating ratio for CPKC's post-merger incremental traffic (based on the incremental revenues and operating expenses set forth in the Application) is far below the historic norms for the US operations of Applicants themselves, and for the US Class I railroads as a group."[177] The *Merger Guidelines* note that Claimed Efficiencies ideally "would be

[173] FD 36500 – Work Paper – HC – summary of benefits SG&A.xlsx, tabs Summary, Non – comp.

[174] The cost savings from the avoided listing fees, $798 thousand, is factual and is verified.

[175] Randall VS, Section 4.4.

[176] Randall VS, Section 4.4.

[177] Randall VS, Section 4.4.

grounded on actual experience."[178] In this instance, the "actual experience" provides evidence that the Merged Company will have greater costs than CP claims. Therefore, this is economic evidence that the expected cost for the Merged Company is not verifiable and may be understated.

[178] "The best way to substantiate an efficiency claim is to demonstrate that similar efficiencies were achieved in the recent past from similar actions. Documentation must be based on appropriate methods and realistic assumptions, and ideally would be grounded on actual experience … If the parties cannot point to similar efficiencies achieved in the recent past, they should use the best information available to substantiate their efficiency claims. For example, the parties might do an internal study and analysis of expected efficiencies using recent cost records and other pertinent objective data" (U.S. Department of Justice & Federal Trade Commission's *Commentary on the Horizontal Merger Guidelines*, dated Mar. 2006, § 4 at 53-54).

VERIFICATION

I, Mark E. Zmijewski, declare under penalty of perjury under the laws of the United States that the foregoing information is true and correct. Further, I certify that I am qualified and authorized to file this statement.

Executed on this 28th day of February, 2022.

Mark E. Zmijewski

Exhibit III-1
Assessment of Claimed Efficiencies

SUMMARY OF BENEFITS	Assessment of Verification	Assessment of Merger Specificity
Benefit Component		
OPERATING REVENUE GAINS		
Revenue Increase from Traffic Gains		
Rail-to-Rail Diversions (Brown/Zebrowski)	Not verified	Merger specific
Truck-to-Rail Diversions (Mutan)	Not verified	Merger specific
Attract New Rail Traffic (Wahba/Naatz)	Not verified	Partially merger-specific
Cost of Handling Added Traffic:		
Engineering - Maintenance of Way	Not verified	Merger specific
Mechanical	Not verified	Merger specific
Transportation	Not verified	Partially merger-specific
Equipment Requirements & Utilization	Not verified	Merger specific
Intermodal Operations	Not verified	Merger specific
OPERATING BENEFITS		
Mechanical	Not verified	Not merger-specific
Transportation	Not verified	Partially merger-specific
Equipment Requirements	Not verified	Partially merger-specific
Purchasing (Procurement)	Not verified	Partially merger-specific
G&A Savings		
Personnel Savings	Not verified	Merger specific
Non-Personnel Savings		
Non-Personnel Expenditures	Not verified	Merger specific
IT (Licensing/Subscriptions/Contract Services)	Not verified	Merger specific
Facilities	Verified	Merger specific
Audit & Listing Fees	Partially verified	Merger specific

Source: CP/KCS Application, Vol I, p. 74 (Appendix B - Summary of Benefits Exhibit)

Exhibit III-2
Summary of Benefits ("Claimed Efficiencies")

USD million

SUMMARY OF BENEFITS	NORMAL YEAR
Benefit Component	
OPERATING REVENUE GAINS	
Revenue Increase from Traffic Gains	1,021.9
Cost of Handling Added Traffic:	(306.3)
Net Revenue Gains	**715.6**
OPERATING BENEFITS	
Mechanical	19.9
Transportation	62.5
Equipment Requirements	12.8
Purchasing (Procurement)	20.5
Subtotal	115.7
Support Functions (G&A)	57.1
Total Operating Benefits	172.8
Employee Separation/Relocation	-
Total Merger Benefits	**888.4**

Source: CP/KCS Application Vol I, p. 74 (Appendix B - Summary of Benefits Exhibit)

Exhibit III-3
Claimed Personnel Savings
KCS Corporate Risk Executives

USD thousands

Description	Formula	Run Rate	Source	Verifiability
KCS corporate risk executive salary	[a]	{{ }}	FD 36500 – Work Paper – HC – summary of benefits SG&A.xlsx	Verifiable
Incentive compensation multiplier	[b]	{{ }}	FD 36500 – Work Paper – HC – summary of benefits SG&A.xlsx	Verifiable
Expected incentive compensation	[c] = [a] x [b]	{{ }}	Calculation	Verifiable
Fringe rates multiplier	[d]	{{ }}	FD 36500 – Work Paper – HC – summary of benefits SG&A.xlsx	Verifiable
Expected fringe rates compensation	[e] = [a] x [d]	{{ }}	Calculation	Verifiable
Total KCS corporate risk executive compensation per employee	[f] = [a] + [c] + [e]	{{ }}	Calculation	Verifiable
Number of KCS corporate risk executive employees terminated	[g]	{{ }}	FD 36500 – Work Paper – HC – summary of benefits SG&A.xlsx	Not verifiable
KCS corporate risk executive savings	[h] = [f] x [g]	{{ }}	Calculation	Not verifiable
Magnitude of verifiable run-rate savings	**n/a**	**-**	**Not verifiable**	

Notes and sources:
Source: FD 36500 – Work Paper – HC – summary of benefits SG&A.xlsx

Exhibit III-4
Claimed Non-Personnel Expenditures Savings

USD thousands

Description	Formula	Run Rate	Source	Verifiability
Variable KCS G&A per employee	[a]	{{ }}	FD 36500 – Work Paper – HC – summary of benefits SG&A.xlsx	Verifiable
KCS headcount reduction	[b]	{{ }}	FD 36500 – Work Paper – HC – summary of benefits SG&A.xlsx	Not verifiable
KCS non-personnel expenditures savings	[c] = [a] x [b]	{{ }}	Calculation	Not verifiable
Variable CP G&A per employee	[d]	{{ }}	FD 36500 – Work Paper – HC – summary of benefits SG&A.xlsx	Verifiable
CP headcount reduction	[e]	{{ }}	FD 36500 – Work Paper – HC – summary of benefits SG&A.xlsx	Not verifiable
CP non-personnel expenditures savings	[f] = [d] x [e]	{{ }}	Calculation	Not verifiable
Total non-personnel expenditures savings	[g] = [c] + [f]	{{ }}	Calculation	Not verifiable
Magnitude of verifiable run-rate savings	**n/a**	**-**	**Not verifiable**	

Notes and sources:
Source: FD 36500 – Work Paper – HC – summary of benefits SG&A.xlsx

Exhibit III-5
Claimed IT Savings

USD thousands

Description	Formula	Run Rate	Source	Verifiability
Infrastructure licensing	[a]	{{ }}	FD 36500 – Work Paper – HC – summary of benefits SG&A.xlsx	Not verifiable
Network	[b]	{{ }}	FD 36500 – Work Paper – HC – summary of benefits SG&A.xlsx	Not verifiable
SAP Licensing/maintenance rationalization and renegotiate	[c]	{{ }}	FD 36500 – Work Paper – HC – summary of benefits SG&A.xlsx	Not verifiable
Microsoft licensing rationalization and renegotiate	[d]	{{ }}	FD 36500 – Work Paper – HC – summary of benefits SG&A.xlsx	Not verifiable
ServiceNow licensing rationalization and renegotiate	[e]	{{ }}	FD 36500 – Work Paper – HC – summary of benefits SG&A.xlsx	Not verifiable
License rationalization and renegotiation of remainder of licenses not identified above	[f]	{{ }}	FD 36500 – Work Paper – HC – summary of benefits SG&A.xlsx	Not verifiable
Transition managed services to Insource	[g]	{{ }}	FD 36500 – Work Paper – HC – summary of benefits SG&A.xlsx	Not verifiable
IT Savings	[h] = [a] + [b] + [c] + [d] + [e] + [f] + [g]	{{ }}	Calculation	Not verifiable
Magnitude of verifiable run-rate savings	**n/a**	**-**	**Not verifiable**	

Notes and sources:
Source: FD 36500 – Work Paper – HC – summary of benefits SG&A.xlsx

Exhibit III-6
Claimed Audit and Listing Fees Savings

USD thousands

Description	Formula	Run Rate	Source	Verifiability
Listing fees	[a]	{{ }}	FD 36500 – Work Paper – HC – summary of benefits SG&A.xlsx	Verifiable
Auditor fees	[b]	{{ }}	FD 36500 – Work Paper – HC – summary of benefits SG&A.xlsx	Not verifiable
Audit & Listing Fees	[c] = [a] + [b]	{{ }}	Calculation	Not verifiable
Magnitude of verifiable run-rate savings	**[a]**	{{ }}	**Verifiable**	

Notes and sources:
Source: FD 36500 – Work Paper – HC – summary of benefits SG&A.xlsx

APPENDIX A – QUALIFICATIONS

1. I specialize in the areas of accounting, economics, and finance as they relate to valuation, financial analysis, and security analysis, or more generally, financial economics. I am Professor Emeritus at The University of Chicago Booth School of Business, and previously held the Charles T. Horngren Professorship and the Leon Carroll Marshall Professorship in my 30-year career at Chicago Booth. In addition to my faculty duties, I also held the positions of Deputy Dean and the PhD Program faculty director at Chicago Booth. I was also the faculty director of the University of Chicago's Center for Research in Security Prices, which is widely recognized for its expertise in building and maintaining historical, academic, research-quality stock market databases.

2. I earned my BS in 1976, MBA in 1981, and PhD (PhD with major in accounting and minors in economics and finance) in 1983, all from the State University of New York at Buffalo. In addition to The University of Chicago, I have taught at the State University of New York at Buffalo and at York University in Toronto, Canada. I have taught various courses in accounting (financial accounting, managerial accounting, and advanced accounting/mergers and acquisitions), finance (corporate finance, financial strategy and corporate transactions, financial analysis, and valuation of companies and corporate transactions), and entrepreneurship.

3. My research focuses on firm valuation, the pricing of securities, including publicly traded securities, and the ways in which various capital market participants use information to value securities. I have taught courses in financial and managerial accounting, mergers and acquisition accounting, financial analysis, corporate valuation, and financial strategy. I have published articles in academic journals in the areas of accounting and financial economics and also co-authored a textbook (with Professor Robert Holthausen of The

Wharton School of the University of Pennsylvania) on how to value companies, parts of companies, and the securities issued by companies, titled *Corporate Valuation: Theory, Evidence and Practice*. I have been an Associate Editor of *The Accounting Review* and have been on the Editorial Boards of both the *Journal of Accounting Research* and *The Accounting Review*.

4. I am a Senior Consultant to Charles River Associates, a consulting firm that provides economic, financial, and management consulting services. I am also a member of the Investment Committee at Patron Capital Partners (Funds IV and V), a private equity investment company with a focus on real estate related investments. I was a founding partner of Chicago Partners, LLC, which was acquired by Navigant Consulting. I am a former managing director of Navigant Economics (a subsidiary of Navigant Consulting) and a former member of the corporate executive committee of Navigant Consulting.

5. I have worked as a consultant or expert in litigation matters in U.S. state and federal courts, in the Supreme Court of Victoria in Australia, and in U.S. and international arbitrations. The issues on which I have worked include: business valuation and securities valuation (valuation of corporate transactions, companies, and parts of companies, intangible assets and intellectual property, and securities); securities litigation (Rule 10b-5, Section 11, Section 12, ERISA, Martin Act, effect of disclosures, analysis of how markets work, and insider trading); mergers and acquisitions (appraisals and price disputes, analyzing merger synergies, material adverse changes, corporate transactions, and the process of purchasing and selling companies); solvency and ability to pay (fraudulent conveyance, solvency assessment, and ability to pay government fines, analysis of debt covenants, renegotiation of terms of debt agreements, and debt

refinancing); antitrust litigation (analysis of merger efficiencies, failing firm defense, and financial analyses of alleged anticompetitive behavior); commercial and stockholder disputes (damages, accounting analyses, and economic assessment of transactions); accounting issues (measuring and analyzing revenue, cost structures, profitability, rates of return, interest rates, and other financial metrics and concepts); and creating and evaluating business plans. The frameworks and tools I use in my work are generally applicable to all industries, and I have applied my expertise in a broad range of sectors, including airline, auto, financial services, chemical, computer hardware and software, credit card and credit card security, energy, entertainment, for-profit education, health care, insurance, heavy and light manufacturing, pharmaceutical, retail, real estate investment funds, technology, telecommunications, transportation, investment companies/funds, investment advisory and brokerage companies, and others. My curriculum vitae, which is attached to this verified statement in Appendix A, details my qualifications, including my publications and testimonial experience within the last five years.

CRA Charles River Associates

Mark E. Zmijewski (Zme – yev' -ski) Bio

Professor Zmijewski specializes in the areas of accounting, economics, and finance as they relate to valuation, financial analysis, and security analysis, or more generally, financial economics. He is Professor Emeritus at The University of Chicago Booth School of Business, and previously held the Charles T. Horngren Professorship and the Leon Carroll Marshall Professorship in his 30-year career at the Booth. In addition to his research and teaching activities, Professor Zmijewski also held the positions of Deputy Dean, Associate Dean for PhD Studies, and the Faculty Director of the Center for Research in Security Prices (CRSP), all at the Booth School of Business. Professor Zmijewski is a Senior Consultant to Charles River Associates, a consulting firm that provides economic, financial, and management consulting services. He is also a Senior Advisor to, and a member of, the Investment Committee at Patron Capital Partners (Funds IV and V), a private equity investment company with a focus on real estate related investments. Professor Zmijewski was a Founding Partner of Chicago Partners, LLC, which was acquired by Navigant Consulting. He is the former Managing Director of Navigant Economics (a subsidiary of Navigant Consulting) and a former member of the Corporate Executive Committee of Navigant Consulting.

Professor Zmijewski earned his BS in 1976, MBA in 1981, and PhD with a major in accounting and minors in economics and finance in 1983, all from the State University of New York at Buffalo. In addition to The University of Chicago, he has taught at the State University of New York at Buffalo and at York University in Toronto, Canada. He has taught various courses in accounting (financial accounting, managerial accounting, and advanced accounting/mergers and acquisitions), finance (corporate finance, financial strategy and corporate transactions, financial analysis, and valuation of companies and corporate transactions), and entrepreneurship. Professor Zmijewski's research has focused on firm valuation and the ways in which various capital market participants use information to value securities. He has published articles in academic journals in the areas of accounting and financial economics and has co-authored a textbook (with Professor Robert Holthausen of The Wharton School of the University of Pennsylvania) on how to value companies, parts of companies, and the securities issued by companies, titled "Corporate Valuation: Theory, Evidence and Practice." He has been an Associate Editor of *The Accounting Review*, and has been on the Editorial Boards of both the *Journal of Accounting Research* and *The Accounting Review*.

Professor Zmijewski has worked as a consultant or expert in litigation matters in US state and federal courts, in the Ontario Superior Court of Justice in Canada, in the Supreme Court of Victoria in Australia, and in US and international arbitrations. The issues on which he has consulted include: business valuation and securities valuation (valuation of corporate transactions, companies, and parts of companies, intangible assets and intellectual property, and securities); securities litigation (10b-5, section 11, section 12, ERISA, Martin Act, and insider trading); material adverse changes; mergers and acquisitions (appraisals and price disputes, analyzing merger synergies, corporate transactions, and the process of purchasing and selling companies); solvency and ability to pay (fraudulent conveyance, solvency assessment, and ability to pay government fines); antitrust litigation (analysis of merger efficiencies, failing firm defense, and financial analyses of alleged anticompetitive behavior); commercial and stockholder disputes (measurement of damages, accounting analyses, and economic assessment of transactions); accounting issues (measuring and analyzing revenue, cost structures, profitability, rates of return, interest rates, and other financial metrics and concepts); and creating and evaluating business plans.

The frameworks and tools used in his work are generally applicable to all industries, and he has applied his expertise in a broad range of sectors, including the airline, auto, chemical, computer hardware and software, credit card, energy, entertainment, financial services, for-profit education, health care, insurance, heavy and light manufacturing, pharmaceutical, retail, real estate investment fund, technology, telecommunications, and transportation industries, among others.

CRA Charles River Associates

Mark E. Zmijewski (Zme-yev'-ski)

Senior Consultant

PhD, Accounting
State University of New York
at Buffalo

MBA, Accounting
State University of New York
at Buffalo

BA, Accounting
State University of New York
at Buffalo

Academic employment

1984–Present	The University of Chicago Booth School of Business
	Professor Emeritus (2018–Present)
	Charles T. Horngren Professor of Accounting (2015–2018)
	Leon Carroll Marshall Professor of Accounting (1999–2015)
	Deputy Dean (1996–2011)
	Professor of Accounting (1992–1999)
	Associate Dean for PhD Studies (1995–1996)
	Executive Director, Center for Research in Securities Prices (CRSP) (1992–1998)
	Associate Professor of Accounting (1988–1992)
	Assistant Professor of Accounting (1984–1988)
1980–1984	*Assistant Professor of Accounting*, State University of New York at Buffalo
1979–1982	*Course Director*, York University, Toronto Canada
1977–1980	*Teaching Assistant*, State University of New York at Buffalo

Honors and awards

Business Information Professional of the Year—Education, Beta Alpha Psi, 2007.

Hillel J. Einhorn Excellence in Teaching Award, The Executive MBA Program, The University of Chicago Graduate School of Business, 1999.

Emory Williams Award for Excellence in Teaching, The University of Chicago, 1988

Competitive Manuscript Award, American Accounting Association, 1984.

Beta Alpha Psi, Honorary Accounting Society, 1981.

Beta Gamma Sigma, Honorary Business Society, 1980.

Grants

Research Grant, SEC and Financial Reporting Institute, 1985.

University Fellowship, State University of New York at Buffalo, 1979.

Graduate Fellowship, State University of New York at Buffalo, 1976–1978.

Publications

Corporate Valuation: Theory, Evidence and Practice (textbook). With Robert W. Holthausen, Cambridge Business Publishers, LLC, 1st Edition, 2014; 2nd edition, 2020.

"Valuation with Market Multiples: How to Avoid Pitfalls When Identifying and Using Comparable Companies." With R. Holthausen. *Journal of Applied Corporate Finance*, Summer 2012.

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Comments on "Earnings Forecasting Research: Its Implications for Capital Markets Research." *International Journal of Forecasting*.

Dissertation committees

Sandip Madan, The University of Chicago, 1999, Member

Keith Bockus, The University of Chicago, 1998, Co-Chairperson

Beverly Walther, The University of Chicago, 1995, Member

Howard Bunsis, The University of Chicago, 1993, Co-Chairperson

Phillip Berger, The University of Chicago, 1992, Member

Stuart Essig, The University of Chicago, 1991, Member

Sherri Jarrell, The University of Chicago, 1991, Member

Andrew Alford, The University of Chicago, 1990, Chairperson

Mark Lang, The University of Chicago, 1990, Member

Laureen Maines, The University of Chicago, 1990, Member

Walter Teets, The University of Chicago, 1988, Member

Siew Teoh, The University of Chicago, 1988, Member

Kirsten Ely, The University of Chicago, 1988, Member

M. Daniel Beneish, The University of Chicago, 1987, Member

Pat O'Brien, The University of Chicago, 1986, Member

W. Forbes Cavanagh, State University of New York at Buffalo, 1985, Member

University activities

Accounting Advisory Counsel, State University of New York at Buffalo, 1993–1995.

Faculty Facilitator, Leadership, Education, and Development (LEAD) Program, The University of Chicago, Graduate School of Business, 1989, 1991.

Dean's Advisory Committee on MBA Students and Curriculum, The University of Chicago, 1988.

Executive Director, Management Development Council, State University of New York at Buffalo, 1981–1984.

Advisor, Center for Management Development, State University of New York at Buffalo, 1979–1980.

Editorial service and boards

Associate Editor, *The Accounting Review*, 1993–1997.

Editorial Board, *Journal of Accounting Research*, 1988–1993.

Editorial Board, *The Accounting Review*, 1985–1987.

Ad hoc referee

Journal of Accounting, Auditing, and Finance

The Accounting Review

Contemporary Accounting Research

The Financial Review

Journal of Accounting and Economics

Journal of Accounting Research

Journal of Banking and Finance

Journal of Business

Journal of Forecasting

International Journal of Forecasting

Management Science

Professional organizations

American Accounting Association

The American Finance Association

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Norman Leslie Wills and Jane Anne Danaher (as Trustees for the Minty Tin Superannuation Fund), v. Woolworths Group Ltd (formerly Woolworths Ltd), Respondent. In the Federal Court of Australia Victoria Registry, Case No. VID 1131/2018. Expert Report February 17, 2020, Expert Rebuttal Report October 30, 2020.

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APPENDIX B – CP'S PRO FORMA EXHIBITS

Exhibit B-I
Canadian Pacific Railway (CP)
Recreated Pro-Forma Income Statement

($ in Millions)	CP HISTORICAL 2019 AS REPORTED US GAAP $CDN (1)	ADJUSTMENTS $CDN (2)	CP BASE YEAR $CDN (3)	CP BASE YEAR $USD (4)
TOTAL REVENUES	$ 7,792	$ -	$ 7,792	$ 5,999
OPERATING EXPENSES	*3,962*	-	*3,962*	*3,050*
DEPRECIATION & AMORTIZATION	*706*	-	*706*	*544*
TOTAL OPERATING EXPENSES	4,668	-	4,668	3,594
OPERATING INCOME	$ 3,124	$ -	$ 3,124	$ 2,405
LESS: OTHER (INCOME) EXPENSES	(470)	94	(376)	(290)
INCOME BEFORE INTEREST AND INCOME TAXES	$ 3,594	$ (94)	$ 3,500	$ 2,695
EARNINGS BEFORE INTEREST, TAXES, DEPRECIATION & AMORTIZATION	*$ 4,300*	*$ (94)*	*$ 4,206*	*$ 3,239*
NET INTEREST EXPENSE	448	-	448	345
INCOME BEFORE INCOME TAX EXPENSE	3,146	(94)	3,052	2,350
INCOME TAX EXPENSE	706	56	762	587
LESS: NET INCOME ATTRIBUTABLE TO NONCONTROLLING INTEREST	-	-	-	-
NET INCOME	$ 2,440	$ (150)	$ 2,290	$ 1,763

NOTES TO PRO FORMA INCOME STATEMENT
CP
BASE YEAR

1. CP HISTORICAL 2019 AS REPORTED: Represents CP's 2019 income statement as reported under US GAAP in its 2019 Annual Report on Form 10-K.

2. ADJUSTMENTS: Represents adjustments made to eliminate effects on CP's income statement of the following non-recurring transactions as reported in 2019:
(1) a deferred tax expense of $24 million as a result of a provision for an uncertain tax item of a prior period;
(2) a deferred tax recovery of $88 million due to the change in the Alberta provincial corporate income tax rate;
(3) a net non-cash gain of $94 million ($86 million after $8 million deferred tax) due to foreign exchange translation of debt and lease liabilities.

3. CP BASE YEAR: Represents CP's 2019 income statement as reported in the 2019 Annual Report on Form 10-K revised to include the adjustments indicated in 2.

4. CP BASE YEAR $USD: Represents the CP Base Year stated in $CDN (3. above) converted to $USD using a conversion factor of $CDN 1 equals 0.7699, which was the exchange rate as of December 31, 2019 from the Bank of Canada.

Bank of Canada December 31, 2019 Exchange Rate		
	Canadian$/US$	1.2988
	US$/Canadian$	0.7699

Source: CP/KCS Application, vol. 1, Appendix F (Exhibit 17), pp. 1-2.

Exhibit B-II
Canadian Pacific Railway (CP)
Recreated Pro-Forma Balance Sheet

($ in Millions)	CP HISTORICAL 2019 AS REPORTED US GAAP $CDN (1)	ADJUSTMENTS $CDN (2)	CP BASE YEAR $CDN (3)	CP BASE YEAR $USD (4)
ASSETS				
CURRENT ASSETS				
CASH AND CASH EQUIVALENTS	$ 133	$ 909	$ 1,042	$ 802
ACCOUNTS RECEIVABLE, NET	805	-	805	620
MATERIALS AND SUPPLIES	182	-	182	140
OTHER CURRENT ASSETS	90	-	90	69
TOTAL CURRENT ASSETS	1,210	909	2,119	1,631
GROSS PROPERTIES	*27,255*	-	*27,255*	*20,985*
ACCUMULATED DEPRECIATION	*(8,099)*	-	*(8,099)*	*(6,236)*
PROPERTIES, NET	19,156	-	19,156	14,749
OTHER ASSETS	2,001	-	2,001	1,541
TOTAL ASSETS	$ 22,367	$ 909	$ 23,276	$ 17,921
LIABILITIES AND SHAREHOLDERS' EQUITY				
CURRENT LIABILITIES				
ACCOUNTS PAYABLE AND ACCRUED LIABILITIES	$ 1,693	$ -	$ 1,693	$ 1,304
LONG-TERM DEBT MATURING WITHIN ONE YEAR	599	-	599	461
TOTAL CURRENT LIABILITIES	2,292	-	2,292	1,765
LONG-TERM DEBT	8,158	-	8,158	6,281
DEFERRED INCOME TAXES	3,501	-	3,501	2,695
OTHER LONG-TERM LIABILITIES	1,347	-	1,347	1,037
TOTAL LIABILITIES	15,298	-	15,298	11,778
SHAREHOLDERS' EQUITY				
SHARE CAPITAL	1,993	-	1,993	1,535
ADDITIONAL PAID-IN CAPITAL	48	-	48	37
ACCUMULATED OTHER COMPREHENSIVE LOSS	(2,522)	-	(2,522)	(1,942)
RETAINED EARNINGS	7,550	909	8,459	6,513
TOTAL SHAREHOLDERS' EQUITY	7,069	909	7,978	6,143
NONCONTROLLING INTEREST	-	-	-	-
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	$ 22,367	$ 909	$ 23,276	$ 17,921

NOTES TO PRO FORMA BALANCE SHEET
CP
BASE YEAR

1. CP HISTORICAL 2019 AS REPORTED: Represents CP's 2019 balance sheet as reported under US GAAP in its 2019 Annual Report on Form 10-K.

2. ADJUSTMENTS: Represents $US 700 million merger termination fee paid to CP in Q2 2021.

3. CP BASE YEAR: Represents CP's 2019 balance sheet as reported in the 2019 Annual Report on Form 10-K.

4. CP BASE YEAR $USD: Represents the CP Base Year stated in $CDN (3. above) converted to $USD using a conversion factor of $CDN 1 equals 0.7699, which was the exchange rate as of December 31, 2019 from the Bank of Canada.

Bank of Canada December 31, 2019 Exchange Rate	Canadian$/US$	1.2988
	US$/Canadian$	0.7699

Source: CP/KCS Application, vol. 1, Appendix E (Exhibit 16), pp. 1-2.

Exhibit B-III
Canadian Pacific Railway (CP)
Recreated Pro-Forma Statement of Cash Flows

($ in Millions)	CP HISTORICAL 2019 AS REPORTED US GAAP $CDN (1)	ADJUSTMENTS $CDN (2)	CP BASE YEAR $CDN (3)	CP BASE YEAR $USD (4)
OPERATING ACTIVITIES				
NET INCOME	$ 2,440	$ (150)	$ 2,290	$ 1,763
RECONCILIATION OF NET INCOME TO CASH PROVIDED BY OPERATING ACTIVITIES:				
DEPRECIATION AND AMORTIZATION	706		706	544
DEFERRED INCOME TAX	181	56	237	182
OTHER OPERATING ACTIVITIES, NET	(311)	94	(217)	(167)
CHANGE IN NON-CASH WORKING CAPITAL BALANCES RELATED TO OPERAT	(26)	-	(26)	(20)
CASH PROVIDED BY OPERATING ACTIVITIES	2,990	-	2,990	2,302
INVESTING ACTIVITIES				
ADDITIONS TO PROPERTIES	(1,647)	-	(1,647)	(1,268)
OTHER INVESTING ACTIVITIES	(156)	174	18	14
CASH USED IN INVESTING ACTIVITIES	(1,803)	174	(1,629)	(1,254)
FINANCING ACTIVITIES				
DIVIDENDS PAID	(412)	-	(412)	(317)
ISSUANCE OF COMMON SHARES	26	-	26	20
PURCHASE OF COMMON SHARES	(1,134)	-	(1,134)	(873)
ISSUANCE OF LONG-TERM DEBT (EXCLUDING COMMERCIAL PAPER)	397	-	397	306
REPAYMENT OF LONG-TERM DEBT (EXCLUDING COMMERCIAL PAPER)	(500)	-	(500)	(385)
NET ISSUANCE OF SHORT-TERM DEBT AND COMMERCIAL PAPER	524	-	524	403
OTHER FINANCING ACTIVITIES	(12)	-	(12)	(9)
CASH USED IN FINANCING ACTIVITIES	(1,111)	-	(1,111)	(855)
EFFECT OF FOREIGN CURRENCY FLUCTUATIONS ON FOREIGN-DENOMINATED CASH AND CASH EQUIVALENTS	(4)	-	(4)	(4)
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	$ 72	$ 174	$ 246	$ 189

NOTES TO PRO FORMA SOURCES AND APPLICATION OF FUNDS (STATEMENT OF CASH FLOWS)
CP
BASE YEAR

1. CP HISTORICAL 2019 AS REPORTED: Represents CP's 2019 sources and applications of funds as reported under US GAAP in its 2019 Annual Report on Form 10-K.
2. ADJUSTMENTS: Represents adjustments made to eliminate effects on CP's sources and applications of funds of the following non-recurring transactions as reported in 2019:
(1) a deferred tax expense of $24 million as a result of a provision for an uncertain tax item of a prior period;
(2) a deferred tax recovery of $88 million due to the change in the Alberta provincial corporate income tax rate;
(3) a net non-cash gain of $94 million ($86 million after $8 million deferred tax expense) due to foreign exchange translation of debt and lease liabilities;
(4) on December 30, 2019 CP invested $174 million towards the purchase of 100% of Central Maine & Quebec Railway.
3. CP BASE YEAR: Represents CP's 2019 sources and applications of funds as reported in the 2019 Annual Report on Form 10-K revised to include the adjustments indicated in 2.
4. CP BASE YEAR $USD: Represents the CP Base Year stated in $CDN (3. above) converted to $USD using a conversion factor of $CDN 1 equals 0.7699, which was the exchange rate as of December 31, 2019 from the Bank of Canada.

Bank of Canada December 31, 2019 Exchange Rate	Canadian$/US$	1.2988
	US$/Canadian$	0.7699

Source: CP/KCS Application, vol. 1, Appendix G (Exhibit 18), pp. 1-2.

Exhibit B-IV
Kansas City Southern (KCS)
Recreated Pro-Forma Income Statement

($US in Millions)	KCS HISTORICAL 2019 AS REPORTED US GAAP (1)	ADJUSTMENTS (2)	KCS BASE YEAR (3)
TOTAL REVENUES	$ 2,866	$ -	$ 2,866
OPERATING EXPENSES	*1,629*	*(169)*	*1,460*
DEPRECIATION & AMORTIZATION	*351*	-	*351*
TOTAL OPERATING EXPENSES	1,980	(169)	1,811
OPERATING INCOME	$ 886	$ 169	$ 1,055
LESS: OTHER (INCOME) EXPENSES	(18)	17	(1)
INCOME BEFORE INTEREST AND INCOME TAXES	$ 904	$ 152	$ 1,056
EARNINGS BEFORE INTEREST, TAXES, DEPRECIATION & AMORTIZATION	*$ 1,255*	*$ 152*	*$ 1,407*
NET INTEREST EXPENSE	116	-	116
INCOME BEFORE INCOME TAX EXPENSE	788	152	940
INCOME TAX EXPENSE	247	3	250
LESS: NET INCOME ATTRIBUTABLE TO NONCONTROLLING INTEREST	2	-	2
NET INCOME	$ 539	$ 149	$ 688

NOTES TO PRO FORMA INCOME STATEMENT
KCS
BASE YEAR

1. KCS HISTORICAL 2019 AS REPORTED: Represents KCS's 2019 income statement as reported under US GAAP in its 2019 Annual Report on Form 10-K.
2. ADJUSTMENTS: Represents adjustments made to eliminate effects on KCS's income statement of the following non-recurring transactions as reported in 2019:
   (1) restructuring charges: $169 million ($125 million after $44 million tax expense);
   (2) foreign exchange gain: $17 million ($12 million after $5 million tax expense);
   (3) foreign exchange component of income taxes: $36 million expense.
3. KCS BASE YEAR: Represents KCS's 2019 income statement as reported in the 2019 Annual Report on Form 10-K revised to include the adjustments indicated in 2.

Source: CP/KCS Application, vol. 1, Appendix F (Exhibit 17), pp. 3-4.

Exhibit B-V
Kansas City Southern (KCS)
Recreated Pro-Forma Balance Sheet

($US in Millions)	KCS HISTORICAL 2019 AS REPORTED US GAAP (1)	ADJUSTMENTS (2)	KCS BASE YEAR (3)
ASSETS			
CURRENT ASSETS			
CASH AND CASH EQUIVALENTS	$ 149	$ -	$ 149
ACCOUNTS RECEIVABLE, NET	274	-	274
MATERIALS AND SUPPLIES	151	-	151
OTHER CURRENT ASSETS	155	-	155
TOTAL CURRENT ASSETS	729	-	729
GROSS PROPERTIES	*11,496*	-	*11,496*
ACCUMULATED DEPRECIATION	*(2,690)*	-	*(2,690)*
PROPERTIES, NET	8,806	-	8,806
OTHER ASSETS	252	-	252
TOTAL ASSETS	$ 9,787	$ -	$ 9,787
LIABILITIES AND SHAREHOLDERS' EQUITY			
CURRENT LIABILITIES			
ACCOUNTS PAYABLE AND ACCRUED LIABILITIES	$ 473	$ -	$ 473
LONG-TERM DEBT MATURING WITHIN ONE YEAR	18	-	18
TOTAL CURRENT LIABILITIES	491	-	491
LONG-TERM DEBT	3,228	-	3,228
DEFERRED INCOME TAXES	1,128	-	1,128
OTHER LONG-TERM LIABILITIES	194	-	194
TOTAL LIABILITIES	5,041	-	5,041
SHAREHOLDERS' EQUITY			
SHARE CAPITAL	7	-	7
ADDITIONAL PAID-IN CAPITAL	844	-	844
ACCUMULATED OTHER COMPREHENSIVE LOSS	(29)	-	(29)
RETAINED EARNINGS	3,601	-	3,601
TOTAL SHAREHOLDERS' EQUITY	4,423	-	4,423
NONCONTROLLING INTEREST	323	-	323
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	$ 9,787	$ -	$ 9,787

NOTES TO PRO FORMA BALANCE SHEET
KCS
BASE YEAR

1. KCS HISTORICAL 2019 AS REPORTED: Represents KCS's 2019 balance sheet as reported under US GAAP in its 2019. Annual Report on Form 10-K.
2. ADJUSTMENTS: No adjustments were necessary to represent KCS's base year balance sheet.
3. KCS BASE YEAR: Represents KCS's 2019 balance sheet as reported in the 2019 Annual Report on Form 10-K.

Source: CP/KCS Application, vol. 1, Appendix E (Exhibit 16), pp. 3-4.

Exhibit B-VI
Kansas City Southern (KCS)
Recreated Pro-Forma Statement of Cash Flows

($US in Millions)	KCS HISTORICAL 2019 AS REPORTED US GAAP (1)	ADJUSTMENTS (2)	KCS BASE YEAR (3)
OPERATING ACTIVITIES			
NET INCOME	$ 541	$ 149	$ 690
RECONCILIATION OF NET INCOME TO CASH PROVIDED BY OPERATING ACTIVITIES:			
DEPRECIATION AND AMORTIZATION	351	-	351
DEFERRED INCOME TAX	53	3	56
OTHER OPERATING ACTIVITIES, NET	168	(120)	48
CHANGE IN NON-CASH WORKING CAPITAL BALANCES RELATED TO OPERATIONS	(10)	-	(10)
CASH PROVIDED BY OPERATING ACTIVITIES	1,103	32	1,135
INVESTING ACTIVITIES			
ADDITIONS TO PROPERTIES	(626)	-	(626)
OTHER INVESTING ACTIVITIES	(50)	-	(50)
CASH USED IN INVESTING ACTIVITIES	(676)	-	(676)
FINANCING ACTIVITIES			
DIVIDENDS PAID	(144)	-	(144)
ISSUANCE OF COMMON SHARES	7	-	7
PURCHASE OF COMMON SHARES	(793)	-	(793)
ISSUANCE OF LONG-TERM DEBT (EXCLUDING COMMERCIAL PAPER)	848	-	848
REPAYMENT OF LONG-TERM DEBT (EXCLUDING COMMERCIAL PAPER)	(285)	-	(285)
NET ISSUANCE OF SHORT-TERM DEBT AND COMMERCIAL PAPER	-	-	-
OTHER FINANCING ACTIVITIES	(12)	-	(12)
CASH USED IN FINANCING ACTIVITIES	(379)	-	(379)
EFFECT OF FOREIGN CURRENCY FLUCTUATIONS ON FOREIGN-DENOMINATED CASH AND CASH EQUIVALENTS	-	-	-
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	$ 48	$ 32	$ 80

NOTES TO PRO FORMA SOURCES AND APPLICATION OF FUNDS (STATEMENT OF CASH FLOWS)
KCS
BASE YEAR

1. KCS HISTORICAL 2019 AS REPORTED: Represents KCS's 2019 sources and applications of funds as reported under US GAAP in its 2019 Annual Report on Form 10-K.

2. ADJUSTMENTS: Represents adjustments made to eliminate effects on KCS's sources and applications of funds of the following non-recurring transactions as reported in 2019:

(1) restructuring charges: $169 million ($125 million after $44 million tax expense), partially offset by $6M cash payments for restructuring charges;

(2) foreign exchange gain: $17 million ($12 million after $5 million tax expense);
(3) foreign exchange component of income taxes: $36 million expense;
(4) settlement of treasury lock agreements: $26 million.

3. KCS BASE YEAR: Represents KCS's 2019 sources and applications of funds as reported in the 2019 Annual Report on Form 10-K revised to include the adjustments indicated in 2.

Source: CP/KCS Application, vol. 1, Appendix G (Exhibit 18), pp. 3-4.

Exhibit B-VII
Canadian Pacific Railway (CP) and Kansas City Southern (KCS)
Recreated Pro-Forma Consolidated Income Statement

($US in Millions)	CP BASE YEAR (1)	KCS BASE YEAR (2)	PURCHASE ACCOUNTING ADJUSTMENT (3)	CP/KCS BASE YEAR (4)
TOTAL REVENUES	$ 5,999	$ 2,866	$ -	$ 8,865
OPERATING EXPENSES	*3,050*	*1,460*	-	*4,510*
DEPRECIATION & AMORTIZATION	*544*	351	-	*895*
TOTAL OPERATING EXPENSES	3,594	1,811	-	5,405
OPERATING INCOME	$ 2,405	$ 1,055	$ -	$ 3,460
LESS: OTHER (INCOME) EXPENSES	(290)	(1)	-	(291)
INCOME BEFORE INTEREST AND INCOME TAXES	$ 2,695	$ 1,056	$ -	$ 3,751
EARNINGS BEFORE INTEREST, TAXES, DEPRECIATION & AMORTIZATION	*$ 3,239*	*$ 1,407*	*$ -*	*$ 4,646*
NET INTEREST EXPENSE	345	116	-	461
INCOME BEFORE INCOME TAX EXPENSE	2,350	940	-	3,290
INCOME TAX EXPENSE	587	250	-	837
LESS: NET INCOME ATTRIBUTABLE TO NONCONTROLLING INTEREST	-	2	-	2
NET INCOME	$ 1,763	$ 688	$ -	$ 2,451

NOTES TO PRO FORMA INCOME STATEMENT
CP/KCS
BASE YEAR

1. CP BASE YEAR: Represents CP's 2019 income statement as reported under US GAAP in its 2019 Annual Report on Form 10-K, adjusted to eliminate the effects of non-recurring transactions, and converted from $CDN to $USD. See separate CP base year pro forma income statement included in this section of the Application.

2. KCS BASE YEAR: Represents KCS's 2019 income statement as reported under US GAAP in its 2019 Annual Report on Form 10-K, adjusted to eliminate the effects of non-recurring transactions. See separate KCS base year pro forma income statement included in this section of the Application.

3. PURCHASE ACCOUNTING ADJUSTMENTS: Represents the CP acquisition of KCS and related purchase accounting adjustments.

4. CP/KCS BASE YEAR: Represents the base year income statement for the combined CP/KCS entity.

Source: CP/KCS Application, vol. 1, Appendix F (Exhibit 17), pp. 5-6.

Exhibit B-VIII
Canadian Pacific Railway (CP) and Kansas City Southern (KCS)
Recreated Pro-Forma Consolidated Balance Sheet

($US in Millions)	CP BASE YEAR (1)	KCS BASE YEAR (2)	PURCHASE ACCOUNTING ADJUSTMENT (3)	CP/KCS BASE YEAR (4)
ASSETS				
CURRENT ASSETS				
CASH AND CASH EQUIVALENTS	$ 802	$ 149	$ (851)	$ 100
ACCOUNTS RECEIVABLE, NET	620	274	-	894
MATERIALS AND SUPPLIES	140	151	-	291
OTHER CURRENT ASSETS	69	155		224
TOTAL CURRENT ASSETS	1,631	729	(851)	1,509
GROSS PROPERTIES	20,985	11,496	-	32,481
ACCUMULATED DEPRECIATION	(6,236)	(2,690)	-	(8,926)
PROPERTIES, NET	14,749	8,806	-	23,555
OTHER ASSETS	1,541	252	23,580	25,373
TOTAL ASSETS	$ 17,921	$ 9,787	$ 22,729	$ 50,437
LIABILITIES AND SHAREHOLDERS' EQUITY				
CURRENT LIABILITIES				
ACCOUNTS PAYABLE AND ACCRUED LIABILITIES	$ 1,304	$ 473	$ 65	$ 1,842
LONG-TERM DEBT MATURING WITHIN ONE YEAR	461	18	549	1,028
TOTAL CURRENT LIABILITIES	1,765	491	614	2,870
LONG-TERM DEBT	6,281	3,228	9,142	18,651
DEFERRED INCOME TAXES	2,695	1,128	(66)	3,757
OTHER LONG-TERM LIABILITIES	1,037	194	-	1,231
TOTAL LIABILITIES	11,778	5,041	9,690	26,509
SHAREHOLDERS' EQUITY				
SHARE CAPITAL	1,535	7	17,881	19,423
ADDITIONAL PAID-IN CAPITAL	37	844	(844)	37
ACCUMULATED OTHER COMPREHENSIVE LOSS	(1,942)	(29)	29	(1,942)
RETAINED EARNINGS	6,513	3,601	(4,027)	6,087
TOTAL SHAREHOLDERS' EQUITY	6,143	4,423	13,039	23,605
NONCONTROLLING INTEREST	-	323	-	323
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	$ 17,921	$ 9,787	$ 22,729	$ 50,437

NOTES TO PRO FORMA BALANCE SHEET
CP/KCS
BASE YEAR

1. CP BASE YEAR: Represents CP's 2019 balance sheet as reported under US GAAP in its 2019 Annual Report on Form 10-K converted from $CDN to $USD. See separate CP base year pro forma balance sheet included in this section of the Application.

2. KCS BASE YEAR: Represents KCS's 2019 balance sheet as reported under US GAAP in its 2019 Annual Report on Form 10-K. See separate KCS base year pro forma balance sheet included in this section of the Application.

3. PURCHASE ACCOUNTING ADJUSTMENTS: Represents the CP acquisition of KCS and related purchase accounting adjustments:

CASH AND CASH EQUIVALENTS - Adjustments represents cash on hand used to fund the cash consideration portion of the purchase price.

OTHER LONG-TERM ASSETS - Adjustment represents remainder of the total purchase price consideration. Once detailed valuations and related calculations are completed, a material portion of this amount could be attributable to properties, goodwill and intangible assets, other assets, other long-term liabilities, and the related deferred income tax balances.

ACCOUNTS PAYABLE AND ACCRUED LIABILITIES - Adjustment represents post transaction compensation adjustments, primarily retention payments.

LONG-TERM DEBT - Represents the net issuance of long-term debt required to fund the cash consideration of the purchase price, CN agreement termination payments, CP and KCS merger transaction costs, cash settlement of outstanding KCS compensation equity awards, and fair value increase of KCS long-term debt.

DEFERRED INCOME TAXES - Adjustment relates to the fair value adjustment of long-term debt and lease obligations.

TOTAL SHAREHOLDERS' EQUITY - Represents CP common shares issued as part of the purchase price, less KCS base year total shareholders' equity, CP merger transaction costs, and accounts payable and accrued liabilities purchase accounting adjustments.

4. CP/KCS BASE YEAR: Represents the base year balance sheet for the combined CP/KCS entity.

Source: CP/KCS Application, vol. 1, Appendix E (Exhibit 16), pp. 5-6.

Exhibit B-IX
Canadian Pacific Railway (CP) and Kansas City Southern (KCS)
Recreated Pro-Forma Consolidated Statement of Cash Flows

($US in Millions)	CP BASE YEAR (1)	KCS BASE YEAR (2)	PURCHASE ACCOUNTING ADJUSTMENT (3)	CP/KCS BASE YEAR (4)
OPERATING ACTIVITIES				
NET INCOME	$ 1,763	$ 690	$ -	$ 2,453
RECONCILIATION OF NET INCOME TO CASH PROVIDED BY OPERATING ACTIVITIES:				
DEPRECIATION AND AMORTIZATION	544	351	-	895
DEFERRED INCOME TAX	182	56	-	238
OTHER OPERATING ACTIVITIES, NET	(167)	48	-	(119)
CHANGE IN NON-CASH WORKING CAPITAL BALANCES RELATED TO OPERATIONS	(20)	(10)	-	(30)
CASH PROVIDED BY OPERATING ACTIVITIES	2,302	1,135	-	3,437
INVESTING ACTIVITIES				
ADDITIONS TO PROPERTIES	(1,268)	(626)	-	(1,894)
OTHER INVESTING ACTIVITIES	14	(50)	-	(36)
CASH USED IN INVESTING ACTIVITIES	(1,254)	(676)	-	(1,930)
FINANCING ACTIVITIES				
DIVIDENDS PAID	(317)	(144)	-	(461)
ISSUANCE OF COMMON SHARES	20	7	-	27
PURCHASE OF COMMON SHARES	(873)	(793)	-	(1,666)
ISSUANCE OF LONG-TERM DEBT (EXCLUDING COMMERCIAL PAPER)	306	848	-	1,154
REPAYMENT OF LONG-TERM DEBT (EXCLUDING COMMERCIAL PAPER)	(385)	(285)	-	(670)
NET ISSUANCE OF SHORT-TERM DEBT AND COMMERCIAL PAPER	403	-	-	403
OTHER FINANCING ACTIVITIES	(9)	(12)	-	(21)
CASH USED IN FINANCING ACTIVITIES	(855)	(379)	-	(1,234)
EFFECT OF FOREIGN CURRENCY FLUCTUATIONS ON FOREIGN-DENOMINATED CASH AND CASH EQUIVALENTS	(4)	-	-	(4)
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	$ 189	$ 80	$ -	$ 269

NOTES TO PRO FORMA SOURCES AND APPLICATION OF FUNDS (STATEMENT OF CASH FLOWS)
CP/KCS
BASE YEAR

1. CP BASE YEAR: Represents CP's 2019 sources and applications of funds as reported under US GAAP in its 2019 Annual Report on Form 10-K, adjusted to eliminate the effects of non-recurring transactions, and converted from $CDN to $USD. See separate CP base year pro forma sources and applications of funds included in this section of the Application.

2. KCS BASE YEAR: Represents KCS's 2019 sources and applications of funds as reported under US GAAP in its 2019 Annual Report on Form 10-K, adjusted to eliminate the effects of non-recurring transactions. See separate KCS base year pro forma sources and applications of funds included in this section of the Application.

3. PURCHASE ACCOUNTING ADJUSTMENTS: Represents the CP acquisition of KCS and related purchase accounting adjustments.

4. CP/KCS BASE YEAR: Represents the base year sources and applications of funds for the combined CP/KCS entity.

Source: CP/KCS Application, vol. 1, Appendix G (Exhibit 18), pp. 5-6.

Exhibit B-X
Canadian Pacific Railway (CP) and Kansas City Southern (KCS)
Recreated Summary of CP/KCS Claimed Efficiencies

($US in Millions)

BENEFIT COMPONENT	YEAR ONE ANNUAL	YEAR ONE ONE-TIME	YEAR TWO ANNUAL	YEAR TWO ONE-TIME	YEAR THREE ANNUAL	YEAR THREE ONE-TIME	NORMAL YEAR	TO 2025 NORMAL YEAR*
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
OPERATING REVENUE GAINS								
Revenue Increase from Traffic Gains	$ 418.0		$ 726.7		$ 1,021.9		$ 1,021.9	$ 1,150.8
Cost of Handling Added Traffic	$ (129.2)		$ (217.8)		$ (306.3)		$ (306.3)	$ (345.0)
Net Revenue Gains	$ 288.9		$ 508.8		$ 715.6		$ 715.6	$ 805.8
OPERATING BENEFITS								
Engineering - Maintenance of Way	$ -	$ (53.6)	$ -	$ (60.9)	$ -	$ (12.0)	$ -	$ -
Mechanical	$ 19.9	$ -	$ 19.9	$ -	$ 19.9	$ -	$ 19.9	$ 22.4
Transportation	$ 59.3	$ -	$ 60.9	$ -	$ 62.5	$ -	$ 62.5	$ 70.4
Equipment Requirements & Utilization	$ 10.1	$ 45.0	$ 11.9	$ 45.0	$ 12.8	$ -	$ 12.8	$ 14.4
Intermodal Operations	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -
Purchasing	$ 4.2	$ -	$ 12.1	$ -	$ 20.5	$ -	$ 20.5	$ 23.1
Subtotal	$ 93.5	$ (8.6)	$ 104.8	$ (15.9)	$ 115.7	$ (12.0)	$ 115.7	$ 130.3
Support Functions (G&A)	$ 36.0	$ (7.7)	$ 51.0	$ (3.8)	$ 57.1	$ -	$ 57.1	$ 64.3
Total Operating Benefits	$ 129.5	$ (16.3)	$ 155.8	$ (19.7)	$ 172.8	$ (12.0)	$ 172.8	$ 194.6
Employee Separation/Relocation	$ -	$ (42.6)	$ -	$ (3.3)	$ -	$ (6.1)	$ -	$ -
Total Merger Benefits	$ 418.4	$ (58.9)	$ 664.6	$ (23.0)	$ 888.4	$ (18.1)	$ 888.4	$ 1,000.4

* Normal year converted from 2019 to 2025 $US using an index factor of 1.1262 based on Railroad Cost Adjustment Factor All-Inclusive Less Fuel with Error Adjustment (All-LF) forecast.

Source: CP/KCS Application, vol. 1, Appendix B.

Exhibit B-XI
Canadian Pacific Railway (CP) and Kansas City Southern (KCS)
Recreated Pro-Forma Consolidated Income Statement Including the Effects of the Claimed Efficiencies

	CP/KCS BASE YEAR (1)	YEAR 1 ADJ (2)	CP/KCS PRO FORMA YEAR 1 (3)	YEAR 2 ADJ (4)	CP/KCS PRO FORMA YEAR 2 (5)	YEAR 3 ADJ (6)	CP/KCS PRO FORMA YEAR 3 (7)	NORMAL YEAR ADJ (8)	CP/KCS PRO FORMA NORMAL YEAR (9)
TOTAL REVENUES	$ 8,865	$ 418	$ 9,283	$ 727	$ 9,592	$ 1,022	$ 9,887	$ 1,022	$ 9,887
OPERATING EXPENSES	4,510	-	4,510	62	4,572	134	4,644	134	4,644
DEPRECIATION & AMORTIZATION	895	41	936	95	990	148	1,043	201	1,096
TOTAL OPERATING EXPENSES	5,405	41	5,446	157	5,562	282	5,687	335	5,740
OPERATING INCOME	$ 3,460	$ 377	$ 3,837	$ 570	$ 4,030	$ 740	$ 4,200	$ 687	$ 4,147
LESS: OTHER (INCOME) EXPENSES	(291)	-	(291)	-	(291)	-	(291)	-	(291)
INCOME BEFORE INTEREST AND INCOME TAXES	$ 3,751	$ 377	$ 4,128	$ 570	$ 4,321	$ 740	$ 4,491	$ 687	$ 4,438
EARNINGS BEFORE INTEREST, TAXES, DEPRECIATION & AMORTIZATION	$ 4,646	$ 418	$ 5,064	$ 665	$ 5,311	$ 888	$ 5,534	$ 888	$ 5,534
NET INTEREST EXPENSE	461	191	652	176	637	146	607	114	575
INCOME BEFORE INCOME TAX EXPENSE	3,290	186	3,476	394	3,684	594	3,884	573	3,863
INCOME TAX EXPENSE	837	49	886	102	939	153	990	148	985
LESS: NET INCOME ATTRIBUTABLE TO NONCONTROLLING INTEREST	2	-	2	-	2	-	2	-	2
NET INCOME	$ 2,451	$ 137	$ 2,588	$ 292	$ 2,743	$ 441	$ 2,892	$ 425	$ 2,876

NOTES TO PRO FORMA INCOME STATEMENT

CP/KCS

YEAR 1 THROUGH NORMAL YEAR

1. CP BASE YEAR (2019): Represents pro forma combined CP/KCS base year income statement, included separately in this section of the Application.

2. YEAR 1 THROUGH NORMAL YEAR ADUSTMENTS: Represents the effects on the combined CP/KCS pro forma base year income statement of cumulative net benefits arising from implementation of the operating plan, inclusive of one-time expenses related to combining operations, as well as interest expense on acquisition debt:

TOTAL REVENUES - Represents gross revenue gains from additional traffic.

TOTAL OPERATING EXPENSES - Represents net benefits from operating efficiencies, reduced by: (1) additional expenses incurred to handle increased traffic; and (2) increased depreciation expense arising from annual additions to properties (resulting from the base-year sources and applications of funds), and one-time capital expenditures to combine operations.

NET INTEREST EXPENSE - Represents the net increase in interest expense arising from debt incurred to finance the acquisition, net of interest expense reductions arising from debt repayment, and amortization of the fair value increase to KCS long-term debt included in the purchase accounting adjustment.

INCOME TAX EXPENSE - Represents the change in current and deferred income taxes resulting from the net adjustments to pretax earnings as outlined above.

Source: CP/KCS Application, vol. 1, Appendix F (Exhibit 17), pp. 7-11.

Exhibit B-XII
Canadian Pacific Railway (CP) and Kansas City Southern (KCS)
Recreated Pro-Forma Consolidated Balance Sheet Including the Effects of the Claimed Efficiencies

($US in Millions)	CP/KCS BASE YEAR (1)	YEAR 1 ACTIVITY (2)	CP/KCS PRO FORMA YEAR 1 (3)	YEAR 2 ACTIVITY (4)	CP/KCS PRO FORMA YEAR 2 (5)	YEAR 3 ACTIVITY (6)	CP/KCS PRO FORMA YEAR 3 (7)	NORMAL YEAR ACTIVITY (8)	CP/KCS PRO FORMA NORMAL YEAR (9)
ASSETS									
CURRENT ASSETS									
CASH AND CASH EQUIVALENTS	$ 100	$ -	$ 100	$ -	$ 100	$ -	$ 100	$ -	$ 100
ACCOUNTS RECEIVABLE, NET	894	-	894	-	894	-	894	-	894
MATERIALS AND SUPPLIES	291	-	291	-	291	-	291	-	291
OTHER CURRENT ASSETS	224	-	224	-	224	-	224	-	224
TOTAL CURRENT ASSETS	1,509	-	1,509	-	1,509	-	1,509	-	1,509
GROSS PROPERTIES	32,481	1,910	34,391	1,914	36,305	1,906	38,211	1,894	40,105
ACCUMULATED DEPRECIATION	(8,926)	(936)	(9,862)	(990)	(10,852)	(1,043)	(11,895)	(1,096)	(12,991)
PROPERTIES, NET	23,555	974	24,529	924	25,453	863	26,316	798	27,114
OTHER ASSETS	25,373	155	25,528	155	25,683	155	25,838	155	25,993
TOTAL ASSETS	$ 50,437	$ 1,129	$ 51,566	$ 1,079	$ 52,645	$ 1,018	$ 53,663	$ 953	$ 54,616
LIABILITIES AND SHAREHOLDERS' EQUITY									
CURRENT LIABILITIES									
ACCOUNTS PAYABLE AND ACCRUED LIABILITIES	$ 1,842	$ (65)	$ 1,777	$ (30)	$ 1,747	$ (30)	$ 1,717	$ (30)	$ 1,687
LONG-TERM DEBT MATURING WITHIN ONE YEAR	1,028	(549)	479	-	479	-	479	-	479
TOTAL CURRENT LIABILITIES	2,870	(614)	2,256	(30)	2,226	(30)	2,196	(30)	2,166
LONG-TERM DEBT	18,651	(461)	18,190	(1,303)	16,887	(1,523)	15,364	(1,576)	13,788
DEFERRED INCOME TAXES	3,757	225	3,982	238	4,220	251	4,471	249	4,720
OTHER LONG-TERM LIABILITIES	1,231	(25)	1,206	(25)	1,181	(25)	1,156	(25)	1,131
TOTAL LIABILITIES	26,509	(875)	25,634	(1,120)	24,514	(1,327)	23,187	(1,382)	21,805
SHAREHOLDERS' EQUITY									
SHARE CAPITAL	19,423	-	19,423	-	19,423	-	19,423	-	19,423
ADDITIONAL PAID-IN CAPITAL	37	-	37	-	37	-	37	-	37
ACCUMULATED OTHER COMPREHENSIVE LOSS	(1,942)		(1,942)	-	(1,942)	-	(1,942)	-	(1,942)
RETAINED EARNINGS	6,087	2,004	8,091	2,199	10,290	2,345	12,635	2,335	14,970
TOTAL SHAREHOLDERS' EQUITY	23,605	2,004	25,609	2,199	27,808	2,345	30,153	2,335	32,488
NONCONTROLLING INTEREST	323	-	323	-	323	-	323	-	323
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	$ 50,437	$ 1,129	$ 51,566	$ 1,079	$ 52,645	$ 1,018	$ 53,663	$ 953	$ 54,616

NOTES TO PRO FORMA BALANCE SHEET

CP/KCS

YEAR 1 THROUGH NORMAL YEAR

1. CP/KCS BASE YEAR (2019) OR PRO FORMA FOR PRECEDING YEAR: For Year 1, represents the pro forma combined CP/KCS base year balance sheet. For Year 2 through Normal Year, represents the pro forma combined CP/KCS for the preceding year. See separate combined CP/KCS Year 1, Year 2, or Year 3 pro forma balance sheets included in this section of the Application.

2. YEAR 1 THROUGH NORMAL YEAR ACTIVITY: Represents the effects on the combined CP/KCS pro forma balance sheets of the operating results (earnings and cash flows) for the respective years, inclusive of adjustments to reflect implementation of the operating plan:

CASH AND CASH EQUIVALENTS - Represents the normal change in cash (resulting from the base year) as derived from the statement of sources and application of funds (statement of cash flows).

PROPERTIES, NET - Represents capital expenditures for each of the respective years, including capital expenditures necessary to combine operations of CP and KCS, less an allowance for depreciation for each year. All years reflect an increase in the normal allowance for depreciation resulting from the capital expenditures to combine operations of CP and KCS.

OTHER LONG-TERM ASSETS - Represents normal expenditures for other investing activities and normal annual other operating activities (base year).

ACCOUNTS PAYABLE AND ACCRUED LIABILITIES - Represents net cash flows from net changes in non-cash working capital balances related to operations, principally net changes in the balance of accounts payable and accrued liabilities.

LONG-TERM DEBT - Represents the net issuance or repayment of long-term debt for the respective years, as well as the amortization of the fair value increase to KCS long-term debt included in the purchase accounting adjustment. In any year where there is a net use of cash arising from the combination of CP and KCS and the implementation of the operating plan, long-term debt is assumed to be issued. In any year where there is a net source of cash arising from the combination and the operating plan, long-term debt is assumed to be repaid.

DEFERRED INCOME TAXES - Represents the net change in the deferred income tax liability resulting principally from different book and tax treatment for depreciation expense and for the depreciation or amortization of components of the excess purchase price resulting from the transaction.

OTHER LONG-TERM LIABILITIES - Represents normal proceeds from other financing activities (resulting from the base year), and effect of foreign currency fluctuations on foreign-denominated cash and cash equivalents, as derived from the statement of sources and application of funds (statement of cash flows).

RETAINED EARNINGS - Represents net earnings for the respective years, less dividends declared and paid to shareholders, and employee separation and relocation costs as a result of combining CP and KCS operations.

Source: CP/KCS Application, vol. 1, Appendix E (Exhibit 16), pp. 7-11.

Exhibit B-XIII
Canadian Pacific Railway (CP) and Kansas City Southern (KCS)
Recreated Pro-Forma Consolidated Statement of Cash Flows Including the Effects of the Claimed Efficiencies

($US in Millions)	CP/KCS BASE YEAR (1)	YEAR 1 ADJ (2)	CP/KCS PRO FORMA YEAR 1 (3)	YEAR 2 ADJ (4)	CP/KCS PRO FORMA YEAR 2 (5)	YEAR 3 ADJ (6)	CP/KCS PRO FORMA YEAR 3 (7)	NORMAL YEAR ADJ (8)	CP/KCS PRO FORMA NORMAL YEAR (9)
OPERATING ACTIVITIES									
NET INCOME	$ 2,453	$ 137	$ 2,590	$ 292	$ 2,745	$ 441	$ 2,894	$ 425	$ 2,878
RECONCILIATION OF NET INCOME TO CASH PROVIDED BY OPERATING ACTIVITIES:									
DEPRECIATION AND AMORTIZATION	895	41	936	95	990	148	1,043	201	1,096
DEFERRED INCOME TAX	238	(16)	222	(3)	235	10	248	8	246
OTHER OPERATING ACTIVITIES, NET	(119)	(58)	(177)	(17)	(136)	(20)	(139)	(12)	(131)
CHANGE IN NON-CASH WORKING CAPITAL BALANCES RELATED TO OPERATIONS	(30)	(35)	(65)	-	(30)	-	(30)	-	(30)
CASH PROVIDED BY OPERATING ACTIVITIES	3,437	69	3,506	367	3,804	579	4,016	622	4,059
INVESTING ACTIVITIES									
ADDITIONS TO PROPERTIES	(1,894)	(16)	(1,910)	(20)	(1,914)	(12)	(1,906)	-	(1,894)
OTHER INVESTING ACTIVITIES	(36)	-	(36)	-	(36)	-	(36)	-	(36)
CASH USED IN INVESTING ACTIVITIES	(1,930)	(16)	(1,946)	(20)	(1,950)	(12)	(1,942)	-	(1,930)
FINANCING ACTIVITIES									
DIVIDENDS PAID	(461)	(82)	(543)	(82)	(543)	(82)	(543)	(82)	(543)
ISSUANCE OF COMMON SHARES	27	(27)	-	(27)	-	(27)	-	(27)	-
PURCHASE OF COMMON SHARES	(1,666)	1,666	-	1,666	-	1,666	-	1,666	-
ISSUANCE OF LONG-TERM DEBT (EXCLUDING COMMERCIAL PAPER)	1,154	-	1,154	-	1,154	-	1,154	-	1,154
REPAYMENT OF LONG-TERM DEBT (EXCLUDING COMMERCIAL PAPER)	(670)	(1,476)	(2,146)	(1,770)	(2,440)	(1,990)	(2,660)	(2,045)	(2,715)
NET ISSUANCE OF SHORT-TERM DEBT AND COMMERCIAL PAPER	403	(403)	-	(403)	-	(403)	-	(403)	-
OTHER FINANCING ACTIVITIES	(21)	-	(21)	-	(21)	-	(21)	-	(21)
CASH USED IN FINANCING ACTIVITIES	(1,234)	(322)	(1,556)	(616)	(1,850)	(836)	(2,070)	(891)	(2,125)
EFFECT OF FOREIGN CURRENCY FLUCTUATIONS ON FOREIGN-DENOMINATED CASH AND CASH EQUIVALENTS	(4)	-	(4)	-	(4)	-	(4)	-	(4)
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	$ 269	$ (269)	$ -	$ (269)	$ -	$ (269)	$ -	$ (269)	$ -

NOTES TO PRO FORMA SOURCES AND APPLICATION OF FUNDS (STATEMENT OF CASH FLOWS)

CP-KCS

YEAR 1 THROUGH NORMAL YEAR

1. CP-KCS BASE YEAR (2019): Represents pro forma combined CP-KCS base year sources and application of funds (statement of cash flows), included separately in this section of the

2. YEAR 1 THROUGH NORMAL YEAR ACTIVITY: Represents the effects on the combined CP-KCS pro forma base year sources and application of funds of: (1) cumulative benefits arising from implementation o the operating plan; (2) one-time capital expenditures related to combining operations; and (3) the issuance or repayment of debt.

NET INCOME - Represents net adjustments to net income/(loss) in the respective years, as derived from the income statement.

DEPRECIATION AND AMORTIZATION - Represents the increased depreciation or amortization expense arising from: (1) annual additions to properties (resulting from the base year); and (2) one-time capital expenditures to combine operations.

DEFERRED INCOME TAX EXPENSE - Represents the adjustment to deferred income tax expense resulting from the net adjustment to pretax earnings.

OTHER OPERATING ACTIVITES, NET - Represents annual other operating activities (base year), one-time employee separation and relocation costs as a result of combining CP and KCS operations, and non-cash amortization of the fair value increase to KCS long-term debt included in the purchase accounting adjustment.

CHANGE IN NON-CASH WORKING CAPITAL BALANCES RELATED TO OPERATIONS - Represents annual changes to working capital accounts for each of the respective years, principally changes in accounts payable and accrued liabilities.

ADDITIONS TO PROPERTIES - Represents capital expenditures for each of the respective years, including one-time expenditures required to achieve the benefits of combining operations.

DIVIDENDS PAID - Represents dividend payments for CP's existing common shares outstanding and dividend payments for incremental CP common shares issued as part of the purchase price consideration.

LONG-TERM AND SHORT-TERM DEBT ISSUED / REPAID - Represents the issuance or repayment of long-term debt for the respective years. In any year where there is a net use of cash arising from the combination of CP and KCS and the implementation of the operating plan, long-term debt is assumed to be issued. In any year where there is a net source of cash arising from the combination and the operating plan, long-term debt is assumed to be repaid.

Source: CP/KCS Application, vol. 1, Appendix G (Exhibit 18), pp. 7-11.

Exhibit 5

Excerpts from Transcript of February 4, 2022 Deposition of John Brooks

WITHHELD FROM PUBLIC VERSION

Exhibit 6

Excerpts from Transcript of February 7, 2022 Deposition of W. Robert Majure, Ph.D.

WITHHELD FROM PUBLIC VERSION

Exhibit 7

Excerpts from Transcript of February 18, 2022 Deposition of Raymond A. Elphick and John F. Orr

WITHHELD FROM PUBLIC VERSION

Exhibit 8

Excerpts from Transcript of February 22, 2022 Deposition of Patrick J. Ottensmeyer

WITHHELD FROM PUBLIC VERSION

Exhibit 9

Excerpts from
2016 KCS
Annual Report

PUBLIC VERSION

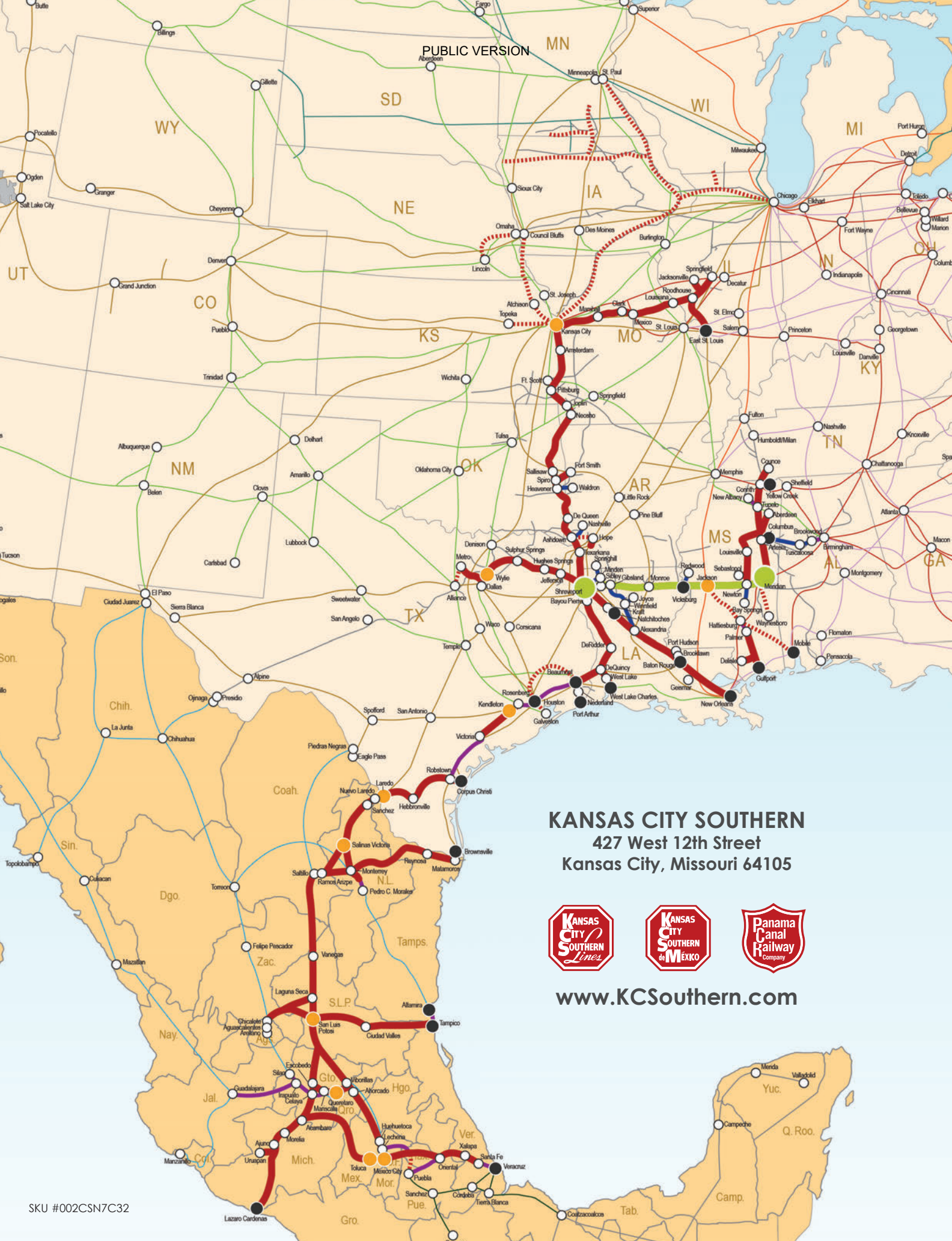
2016 Annual Report

KANSAS CITY SOUTHERN

Kansas City Southern Lines

Kansas City Southern de México

Panama Canal Railway Company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KANSAS CITY SOUTHERN
427 West 12th Street
Kansas City, Missouri 64105
www.KCSouthern.com
SKU #002CSN7C32

Exhibit 10

Excerpts from
2017 KCS
Annual Report

PUBLIC VERSION

2017 Annual Report

CONNECTING NORTH AMERICA

FOR PROSPERITY AND SECURITY

KANSAS CITY SOUTHERN

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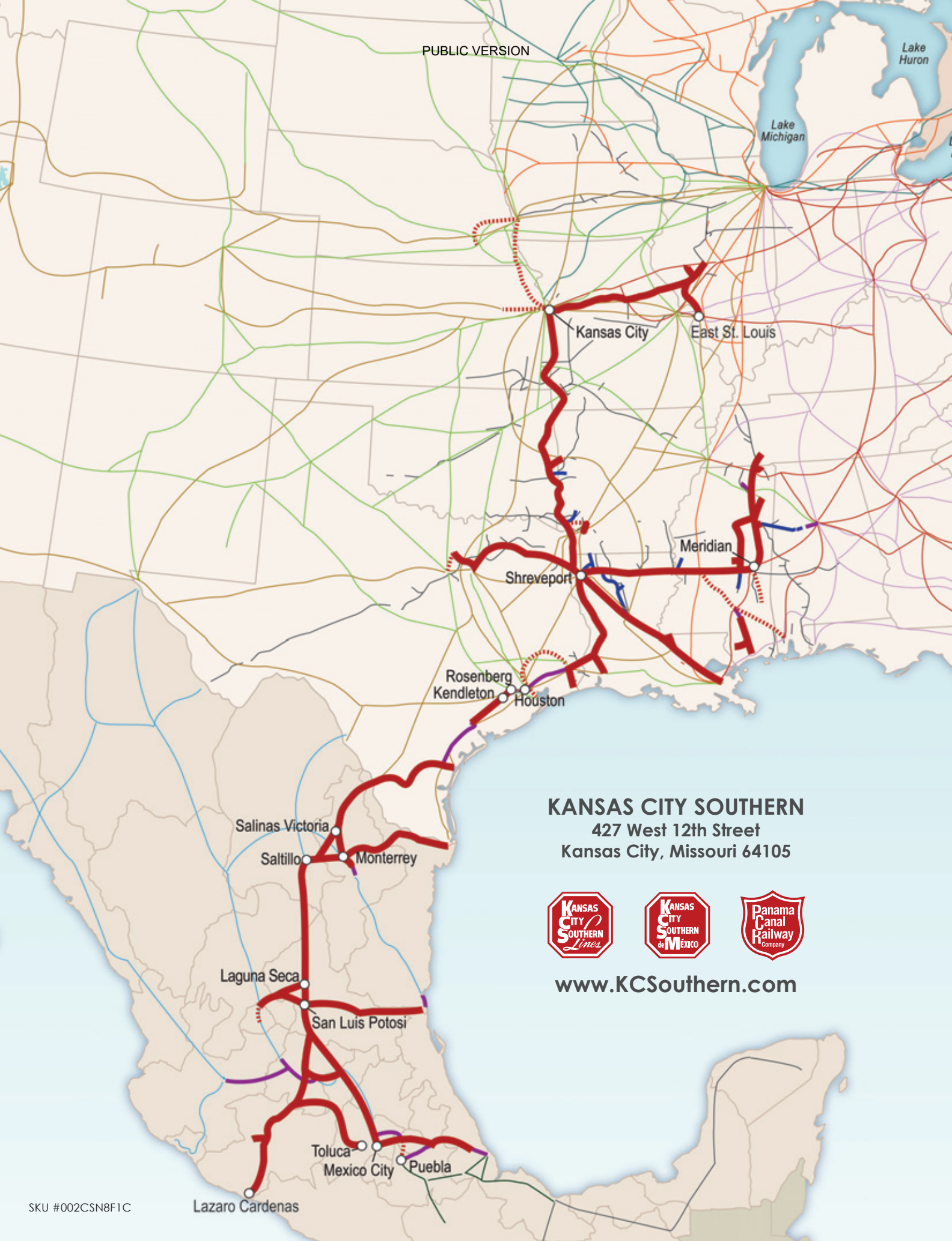

KANSAS CITY SOUTHERN
427 West 12th Street
Kansas City, Missouri 64105

www.KCSouthern.com

SKU #002CSN8F1C

Exhibit 11

December 3, 2019 Gibson Energy Press Release

Gibson Energy and USD Announce Joint Venture to Construct DRU at Hardisty Utilizing Innovative DRUbit™ Technology and Agreement with ConocoPhillips for 50,000 bbl/d of Capacity

Patented Diluent Recovery Unit Produces DRUbit™ Designed for Rail Transport and Reuse of Diluent Providing a Bitumen Market Access Solution with Significant Safety and Environmental Benefits and Increased Takeaway Capacity at a Cost Competitive with Pipelines

December 03, 2019 16:01 ET | Source: Gibson Energy Inc.

CALGARY, Alberta, Dec. 03, 2019 (GLOBE NEWSWIRE) -- US Development Group, LLC (through a wholly-owned affiliate, collectively **USD**) and Gibson Energy Inc. (**Gibson**) (TSX: GEI) jointly announced today an agreement to construct and operate a diluent recovery unit (**DRU**) near Hardisty, Alberta, Canada. ConocoPhillips Canada has contracted to process 50,000 barrels per day of inlet bitumen blend through the DRU to be shipped by Canadian Pacific (**CP**) (TSX: CP) (NYSE: CP) and Kansas City Southern Railway Company (**KCS**) (NYSE: KSU) to the U.S. Gulf Coast. USD and Gibson are currently in

USD's patented DRU technology separates the diluent that has been added to the raw bitumen in the production process which meets two important market needs – it returns the recovered diluent for reuse in the Alberta market, reducing delivered costs for diluent, and it creates **DRUbit™**, a proprietary heavy Canadian crude oil specifically designed for rail transportation. DRUbit™ is crude oil or bitumen that has been returned to a more concentrated, viscous state that creates safety and environmental benefits when transported by rail in Canada and the U.S. DRUbit™ is a market access solution that will satisfy demand for heavy Canadian crude oil on the U.S. Gulf Coast and in other markets at a cost that is economically competitive to the crude oil that is transported by pipeline today.

"Our DRU technology provides a sustainable, long-term solution for shipping Canadian crude oil to the U.S. Gulf Coast. DRUbit™ offers safety and environmental benefits in transportation, provides greater take-away capacity and improved economics for all parties," said USD CEO, Dan Borgen. "USD is a company that provides solutions for energy infrastructure and our patented DRU technology is another valuable solution. We are thrilled to work with ConocoPhillips Canada, our JV partner Gibson, and both CP and KCS to deliver this DRU and DRUbit™ solution as part of a networked system that provides direct market access for Canadian producers."

"The DRU process is an innovative solution that competes with pipeline economics and secures improved netbacks across the seasonality and widely varying differentials experienced in the Western Canadian spot market," said Kirk Johnson, President, ConocoPhillips Canada. "It helps address a critical challenge to Canada's oil producers — constrained market access — to the benefit of all Canadians."

"We expect DRUs to be a critical part of solving the egress challenges Western Canadian producers are facing, both today and over the long-term," said Steve Spaulding, Gibson's President and Chief Executive Officer. "Improved netbacks for producers will drive increased oilfield and related business activity, create new jobs and help revive communities as well as positively benefit all levels of government through increased royalties and other levies."

standard conditions. The new terminal in Port Arthur will be constructed, owned and operated solely by USD. It will have capability for rail unloading, barge dock loading and unloading, tank storage and blending, and will be pipeline connected to Phillips 66's Beaumont Terminal, providing customers access to a large network of refining and marine facilities. ConocoPhillips will re-blend the DRUbit™ with a variety of diluents to create higher-value customized blends that better meet the needs of its customers.

"From an innovation, sustainability and safety perspective, this is a game changer," said Keith Creel, CP President and CEO. "This process removes diluent from the crude-by-rail supply chain, and as a result, we end up moving a non-hazardous commodity. This will further increase the safety of crude-by-rail, to the benefit of the communities we operate in and through."

"KCS is pleased to be a strategic partner in this innovative solution to improve the economics and safety of moving crude oil," said KCS President and Chief Executive Officer Patrick J. Ottensmeyer. "It's also a great opportunity to grow our business in the Gulf Coast area and develop our Port Arthur asset."

Construction of the DRU is expected to take approximately 18 to 24 months and is subject to certain conditions, including obtaining agreements to underpin the economics of the project and receipt of required regulatory approvals, including from the Alberta Energy Regulator. The DRU could be placed into service as early as the second quarter of 2021.

Media & Investor Contacts

Gibson
Mark Chyc-Cies
Vice President, Strategy, Planning & IR
403-776-3146
mark.chyccies@gibsonenergy.com

USD Group
Mary Ellen Kilpatrick
713-412-1545
maryellen@goodengroup.com

About USD Group LLC

US Development Group, LLC ("USD") and its affiliates are engaged in designing, developing, owning, and managing large-scale multi-modal logistics centers and energy-related infrastructure across North America. USD solutions create flexible market access for customers in significant growth areas and key demand centers, including Western Canada, the U.S. Gulf Coast and Mexico. Among other projects, USD is currently pursuing the development of a premier energy logistics terminal on the Houston Ship

additional information, please visit www.usdg.com. Information on websites referenced in this release are not part of this release. DRUbit™ is a trademark of DRU Assets LLC, a subsidiary of USD, and is used by permission. All rights reserved.

About Gibson

Gibson is a Canadian-based oil infrastructure company with its principal businesses consisting of the storage, optimization, processing, and gathering of crude oil and refined products. Headquartered in Calgary, Alberta, the Company's operations are focused around its core terminal assets located at Hardisty and Edmonton, Alberta, and also include the Moose Jaw Facility and an infrastructure position in the U.S. Gibson shares trade under the symbol GEI and are listed on the Toronto Stock Exchange. For more information regarding Gibson as well as the DRU project visit www.gibsonenergy.com and Gibson's profile on SEDAR at www.sedar.com.

About ConocoPhillips

Headquartered in Houston, Texas, ConocoPhillips had operations and activities in 17 countries, $70 billion of total assets, and approximately 10,400 employees as of Sept. 30, 2019. Production excluding Libya averaged 1,310 MBOED for the nine months ended Sept. 30, 2019, and proved reserves were 5.3 BBOE as of Dec. 31, 2018. Our Canadian operations are focused on developing our world-class portfolio including the ConocoPhillips-operated Surmont Joint Venture with TOTAL E&P Canada in the Athabasca region of northeast Alberta and exciting opportunities in the liquids-rich Montney play in northeast British Columbia. For more information, go to www.conocophillips.ca.

About Canadian Paci c

Canadian Pacific (CP) is a transcontinental railway in Canada and the United States with direct links to major ports on the west and east coasts. CP provides North American customers a competitive rail service with access to key markets in every corner of the globe. CP is growing with its customers, offering a suite of freight transportation services, logistics solutions and supply chain expertise. Visit www.cpr.ca to see the rail advantages of CP.

About the Kansas City Southern Railway Company

Headquartered in Kansas City, Mo., Kansas City Southern (KCS) (NYSE: KSU) is a transportation holding company that has railroad investments in the

serving northeastern and central Mexico and the port cities of Lázaro Cárdenas, Tampico and Veracruz, and a 50 percent interest in Panama Canal Railway Company, providing ocean-to-ocean freight and passenger service along the Panama Canal. KCS' North American rail holdings and strategic alliances with other North American rail partners are primary components of a unique railway system, linking the commercial and industrial centers of the U.S., Mexico and Canada. More information about KCS can be found at www.kcsouthern.com.

Forward Looking Statements

Certain statements contained in this press release constitute forward-looking information and statements (collectively, ***forward-looking statements****) including, but not limited to, statements concerning the proposed construction and operations of the DRU, the anticipated benefits, opportunities and sustainability of the DRU and DRUbit™ for project participants, oil field and related business activities, market participants, local communities and governments, the methods of transportation of DRUbit™ and contribution of the DRU to the improvement of market access for oil producers, construction, ownership and operation of USD's Port Arthur terminal and the plans for such terminal, improved industry economics associated with the DRU and transportation of DRUbit™, the safety features of the transportation of DRUbit™ and expectations with respect to the business and financial prospects and opportunities related to the DRU and DRUbit™ transportation.*

These statements relate to future events or future performance. All statements other than statements of historical fact are forward-looking statements. The use of any of the words "anticipate", "plan", "aim", "target", "contemplate", "continue", "estimate", "expect", "intend", "propose", "might", "may", "will", "shall", "project", "should", "could", "would", "believe", "predict", "forecast", "pursue", "potential" and "capable" and similar expressions are intended to identify forward-looking statements. The forward looking statements reflect the project participant's beliefs and assumptions with respect to, among other things, the ability to obtain necessary commercial support and regulatory approvals in connection with the DRU and Port Arthur terminal, the timing of completion of the DRU and Port Arthur terminal, continued market demand, general economic trends, industry trends, commodity prices, capital markets, the governmental, regulatory and legal environment in the various jurisdictions in which they

current and future obligations, ability to obtain financing for capital programs and the DRU and Port Arthur terminal on acceptable terms, the successful and timely implementation of capital projects in a manner consistent with financial expectations and the other business activities of the participants, and other assumptions inherent in management's expectations of future operating and financial results and other forward-looking statements identified herein.

Forward-looking statements involve known and unknown risks, uncertainties and other factors that may cause actual results or events to differ materially from those anticipated in such forward-looking statements. Although the project participants believe these statements to be reasonable, no assurance can be given that these expectations will prove to be correct and such forward-looking statements included in this press release should not be unduly relied upon. Actual results could differ materially from those anticipated in these forward looking statements as a result of, among other things, risks inherent in the businesses conducted by each of the project participants, ability for Gibson and USD to secure additional long-term, take-or-pay agreements with other producer and refiner customers to fully underpin the economics of the project, the ability to satisfy the commercial conditions relating to ConocoPhillips' participation in the DRU project and other conditions associated with the DRU and its construction and operation, the ability of customers to discover and market reserves, construction costs in respect of the DRU and USD's Port Arthur terminal, regulatory decisions, competitive factors in the industries in which the project participants operate, prevailing economic conditions, world-wide demand for crude oil and petroleum products, volatility of commodity prices, currency and interest rates fluctuations, product supply and demand (including demand for DRUbit™), changes in credit ratings applicable to any of the participants, operating costs and the accuracy of cost estimates, exposure to counterparties and partners, including ability and willingness of such parties to satisfy contractual obligations in a timely manner, future capital expenditures, ability to obtain necessary regulatory approvals for the DRU and USD's Port Arthur terminal, the availability, costs, terms and timing of or execution of, and competition for, required regulatory approvals, rail capacity and terminal access, the successful and timely implementation of construction on the DRU and Port Arthur terminal and/or stages thereof, changes to any of the

regulations, including environmental and tax laws and regulations, competition for employees and other personnel, equipment, material and services related thereto, the availability and cost of employees and other personnel, equipment, materials and services, weather, including its impact on product demand, exploration, production and transportation, inherent risks associated with the exploration, development, production and transportation of bitumen, the timing and extent of changes in foreign currency exchange rates, interest rates, inflation rates, global and domestic financial market conditions and global and domestic general economic conditions, political developments around the world, including the areas in which the project participants individually, or collectively, operate, many of which are beyond the control of any of the project participants. Readers are cautioned that the foregoing lists are not exhaustive. For a full discussion of the material risk factors please refer to those included in Gibson's Annual Information Form dated March 4, 2019 as filed on SEDAR and available on the Gibson website at www.gibsonenergy.com, the more detailed information about factors that could affect future events may be found in filings by ConocoPhillips with the Securities and Exchange Commission including ConocoPhillips' Annual Report on Form 10-K for the year ended December 31, 2018 and subsequent reports, those detailed from time to time in reports filed by CP with securities regulators in Canada and the United States under "Risk Factors" and "Management's Discussion and Analysis of Financial Condition and Results of Operations - Forward-Looking Information" in CP's annual and interim reports on Form 10-K and 10-Q, and the more detailed information about factors that could affect future events may be found in filings by KCS with the Securities and Exchange Commission including KCS' Annual Report on Form 10-K for the year ended December 31, 2018 and subsequent reports.

Tags

Gibson Energy | DRUbit | dru | usd

Related Links

- Gibson Energy Website
- US Development Group Website

Recommended

Source: Gibson Energy Inc.

Gibson Energy Con rms 2020 Fourth Quarter and Year-End Earnings Release Date and Provides Conference Call & Webcast Details

CALGARY, Alberta, Jan. 25, 2021 (GLOBE NEWSWIRE) -- Gibson Energy Inc. announced today that it expects to release its 2020 fourth quarter and year-end nancial and operating results on Monday,...

Source: Gibson Energy Inc.

Gibson Energy Announces Redemption of Convertible Debentures

CALGARY, Alberta, Dec. 23, 2020 (GLOBE NEWSWIRE) -- Gibson Energy Inc. announced today that it has completed the previously announced redemption of its outstanding 5.25% convertible unsecured...

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Exhibit 12

Excerpts from October 20, 2020 KCS Board of Directors Meeting Slides

WITHHELD FROM PUBLIC VERSION

Exhibit 13

Excerpts from February 4, 2021 KCS Board of Directors Meeting Materials

WITHHELD FROM PUBLIC VERSION

Exhibit 14

June 3, 2021 CN-KCS Presentation Slides, Bernstein's 37th Annual Strategic Decisions Conference

PUBLIC VERSION

Bernstein's 37th Annual Strategic Decisions Conference

JJ Ruest
President & CEO, CN

Patrick J. Ottensmeyer
President & CEO, KCS

June 3, 2021

Forward-Looking Statements

Certain statements included in this presentation constitute "forward-looking statements" within the meaning of the United States Private Securities Litigation Reform Act of 1995 and under Canadian securities laws, including statements based on management's assessment and assumptions and publicly available information with respect to KCS, regarding the proposed transaction between CN and KCS, the expected benefits of the proposed transaction and future opportunities for the combined company. By their nature, forward-looking statements involve risks, uncertainties and assumptions. CN cautions that its assumptions may not materialize and that current economic conditions render such assumptions, although reasonable at the time they were made, subject to greater uncertainty. Forward-looking statements may be identified by the use of terminology such as "believes," "expects," "anticipates," "assumes," "outlook," "plans," "targets," or other similar words.

Forward-looking statements are not guarantees of future performance and involve risks, uncertainties and other factors which may cause actual results, performance or achievements of CN, or the combined company, to be materially different from the outlook or any future results, performance or achievements implied by such statements. Accordingly, readers are advised not to place undue reliance on forward-looking statements. Important risk factors that could affect the forward-looking statements in this presentation include, but are not limited to: the outcome of the proposed transaction between CN and KCS; the parties' ability to consummate the proposed transaction; the conditions to the completion of the proposed transaction; that the regulatory approvals required for the proposed transaction may not be obtained on the terms expected or on the anticipated schedule or at all; CN's indebtedness, including the substantial indebtedness CN expects to incur and assume in connection with the proposed transaction and the need to generate sufficient cash flows to service and repay such debt; CN's ability to meet expectations regarding the timing, completion and accounting and tax treatments of the proposed transaction; the possibility that CN may be unable to achieve expected synergies and operating efficiencies within the expected time-frames or at all and to successfully integrate KCS' operations with those of CN; that such integration may be more difficult, time-consuming or costly than expected; that operating costs, customer loss and business disruption (including, without limitation, difficulties in maintaining relationships with employees, customers or suppliers) may be greater than expected following the proposed transaction or the public announcement of the proposed transaction; the retention of certain key employees of KCS may be difficult; the duration and effects of the COVID-19 pandemic, general economic and business conditions, particularly in the context of the COVID-19 pandemic; industry competition; inflation, currency and interest rate fluctuations; changes in fuel prices; legislative and/or regulatory developments; compliance with environmental laws and regulations; actions by regulators; the adverse impact of any termination or revocation by the Mexican government of KCS de México, S.A. de C.V.'s Concession; increases in maintenance and operating costs; security threats; reliance on technology and related cybersecurity risk; trade restrictions or other changes to international trade arrangements; transportation of hazardous materials; various events which could disrupt operations, including illegal blockades of rail networks, and natural events such as severe weather, droughts, fires, floods and earthquakes; climate change; labor negotiations and disruptions; environmental claims; uncertainties of investigations, proceedings or other types of claims and litigation; risks and liabilities arising from derailments; timing and completion of capital programs; and other risks detailed from time to time in reports filed by CN with securities regulators in Canada and the United States. Reference should also be made to Management's Discussion and Analysis in CN's annual and interim reports, Annual Information Form and Form 40-F, filed with Canadian and U.S. securities regulators and available on CN's website, for a description of major risk factors relating to CN. Additional risks that may affect KCS' results of operations appear in Part I, Item 1A "Risks Related to KCS's Operations and Business" of KCS' Annual Report on Form 10-K for the year ended December 31, 2020, and in KCS' other filings with the U.S. Securities and Exchange Commission ("SEC").

Forward-looking statements reflect information as of the date on which they are made. CN assumes no obligation to update or revise forward-looking statements to reflect future events, changes in circumstances, or changes in beliefs, unless required by applicable securities laws. In the event CN does update any forward-looking statement, no inference should be made that CN will make additional updates with respect to that statement, related matters, or any other forward-looking statement.

Additional Information

No Offer or Solicitation
This presentation does not constitute an offer to sell or the solicitation of an offer to buy any securities or a solicitation of any vote or approval, nor shall there be any sale of securities in any jurisdiction in which such offer, solicitation or sale would be unlawful prior to registration or qualification under the securities laws of any such jurisdiction. No offer of securities shall be made except by means of a prospectus meeting the requirements of Section 10 of the Securities Act of 1933, as amended.

Additional Information and Where to Find It
In connection with the proposed transaction, CN will file with the SEC a registration statement on Form F-4 to register the shares to be issued in connection with the proposed transaction. The registration statement will include a preliminary proxy statement of KCS which, when finalized, will be sent to the stockholders of KCS seeking their approval of the merger-related proposals. This presentation is not a substitute for the proxy statement or registration statement or other document CN and/or KCS may file with the SEC or applicable securities regulators in Canada in connection with the proposed transaction.

INVESTORS AND SECURITY HOLDERS ARE URGED TO READ THE PROXY STATEMENT(S), REGISTRATION STATEMENT(S), TENDER OFFER STATEMENT, PROSPECTUS AND ANY OTHER RELEVANT DOCUMENTS FILED WITH THE SEC OR APPLICABLE SECURITIES REGULATORS IN CANADA CAREFULLY IN THEIR ENTIRETY IF AND WHEN THEY BECOME AVAILABLE BECAUSE THEY WILL CONTAIN IMPORTANT INFORMATION ABOUT CN, KCS AND THE PROPOSED TRANSACTIONS. Any definitive proxy statement(s), registration statement or prospectus(es) and other documents filed by CN and KCS (if and when available) will be mailed to stockholders of CN and/or KCS, as applicable. Investors and security holders will be able to obtain copies of these documents (if and when available) and other documents filed with the SEC and applicable securities regulators in Canada by CN free of charge through at www.sec.gov and www.sedar.com. Copies of the documents filed by CN (if and when available) will also be made available free of charge by accessing CN's website at www.CN.ca. Copies of the documents filed by KCS (if and when available) will also be made available free of charge at www.investors.kcsouthern.com, upon written request delivered to KCS at 427 West 12th Street, Kansas City, Missouri 64105, Attention: Corporate Secretary, or by calling KCS's Corporate Secretary's Office by telephone at 1-888-800-3690 or by email at corpsec@kcsouthern.com.

Participants
This presentation is neither a solicitation of a proxy nor a substitute for any proxy statement or other filings that may be made with the SEC and applicable securities regulators in Canada. Nonetheless, CN, KCS, and certain of their directors and executive officers and other members of management and employees may be deemed to be participants in the solicitation of proxies in respect of the proposed transactions. Information about CN's executive officers and directors is available in its 2021 Management Information Circular, dated March 9, 2021, as well as its 2020 Annual Report on Form 40-F filed with the SEC on February 1, 2021, in each case available on its website at www.CN.ca/investors/ and at www.sec.gov and www.sedar.com. Information about KCS' directors and executive officers may be found on its website at www.kcsouthern.com and in its 2020 Annual Report on Form 10-K filed with the SEC on January 29, 2021, available at www.investors.kcsouthern.com and www.sec.gov. Additional information regarding the interests of such potential participants will be included in one or more registration statements, proxy statements, tender offer statements or other documents filed with the SEC and applicable securities regulators in Canada if and when they become available. These documents (if and when available) may be obtained free of charge from the SEC's website at www.sec.gov and from www.sedar.com, as applicable.

Non-GAAP Measures
CN reports its financial results in accordance with United States generally accepted accounting principles (GAAP). This presentation includes certain forward looking non-GAAP measures, including EBITDA, free cash flow and adjusted debt-to-adjusted EBITDA multiples. These non-GAAP measures may not be comparable to similar measures presented by other companies. It is not practicable to reconcile, without unreasonable efforts, these forward-looking measures to the most comparable GAAP measures, due to unknown variables and uncertainty related to future results. Please see note on Forward-Looking Statements above for further discussion.

All amounts in this presentation are expressed in US dollars, unless otherwise noted. All references to the "Company" are to CN.

CN-KCS: An "End-to-End" Merger That Will Enhance Choice and Competition

CUSTOMER CHOICE

- Wide variety of transportation options in the center of the U.S. including rails, highways and barges on the Mississippi River system
- The CN-KCS combination will create and add new direct rail routes that will **enhance multimodal competition** and **maximize customer choice**
- Committed to preserve connectivity by **keeping current gateways open**

NEW OPPORTUNITIES

- Create service where no direct choices exist today, **enhancing competition** between motor carriers and railroads and among railroads
- Provide grain shippers in Illinois with **new access** to East St. Louis and new direct single-line service to Mexico and ports in Mobile / New Orleans

NO OVERLAP

- CN has committed to a divestiture of a 70-mile section of track that would result in **zero overlap**
- **End-to-end** merger ensures that shippers enjoy the **same number of options** that they do today

CONTINUED INVESTMENT

- **$250 million in infrastructure investments** across CN and KCS lines
- Results in **more efficiency, more capacity and more opportunities for employees and communities**

CN-KCS is a fully end-to-end merger that will produce significant public interest benefits

High Confidence in Our Original Estimate of $1B in EBITDA Synergies

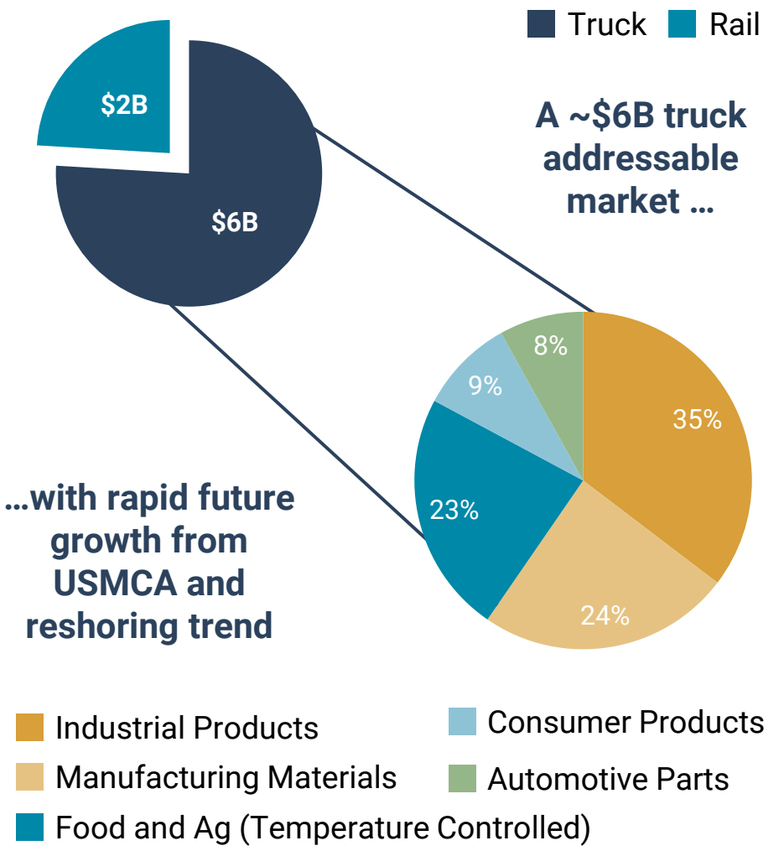
New Revenue Opportunities

- ✓ The revenue opportunities are based on two major routes:
  - – Kansas City Speedway – connecting CN's Midwest foothold and the KC region
  - – CN Greenway – connecting Mexico, East Texas and the Gulf with CN's US Midwest and Eastern Canada foothold
- ✓ Combined business could target an incremental $6B of truck intermodal and $2B of rail TAM
- ✓ Diligence on KCS identified additional opportunities beyond original assessment (mostly carloads)

Cost Efficiencies

- ✓ Improved fuel efficiency and lower costs
- ✓ Technology deployment on a larger network
- ✓ More effective purchasing of operating and capital expenditures
- ✓ Core of cost savings will not be people-driven

Intermodal Opportunity Breakdown (1)



Synergies are predominantly growth and revenue-driven; and will yield environmental benefits by taking trucks off the road

(1) Conservative estimate based on CN's original assessment of new revenue opportunities.

CN's Advanced Technology Applied to a Larger Rail Network

Autonomous Track Inspection Program *(for Safety and Capacity)*

- Latest sensors and AI technology for accurate preventative maintenance, enabling up to 20x more inspections
- Proven rail safety improvements (reduce incidents, reduce incident costs, better customer sentiment)

Digitalized and Automated Train Inspection *(for Safety and Reliability)*

- More frequent and better machine vision-based inspections
- High-resolution imaging coupled with powerful machine learning algorithms

Connecting the Supply Chain *(for Service and Business Growth)*

- Real-time "track and trace" for customer shipments
- Reducing end-to-end variability and cycle times

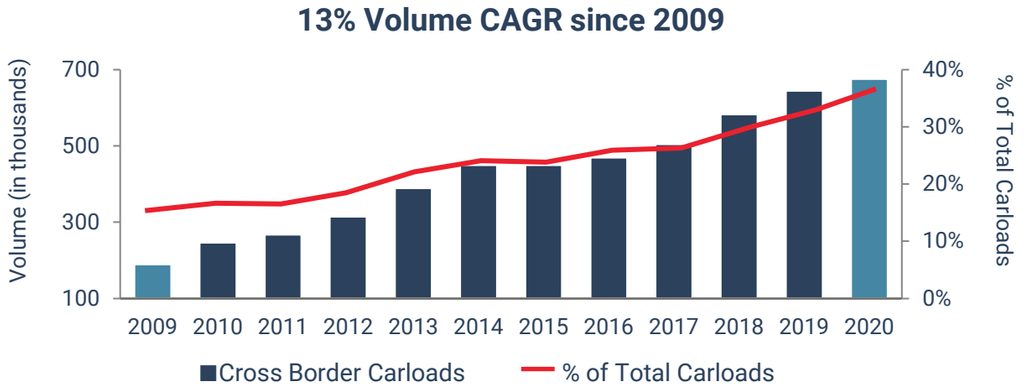
The combined CN-KCS customers will benefit from CN's leadership and investments in advanced technology

Mexico Provides Unparalleled Growth Opportunities

Mexico Near-Sourcing Benefits and Positive Drivers

- ✓ Multiple factors (including the ratification of USMCA, the COVID-19 pandemic, and other macro geo-political trends) have led to an increased corporate focus on near-sourcing / near-shoring
- ✓ Mexico's manufacturing economy will reap material benefits
- ✓ Companies who near-source in Mexico have multiple advantages:
  - Trade advantages
  - Manufacturing clusters
  - Competitive labor costs with a highly trained workforce

KCS US-Mexico Volume



KCS Customer / Partner Investments and Projects

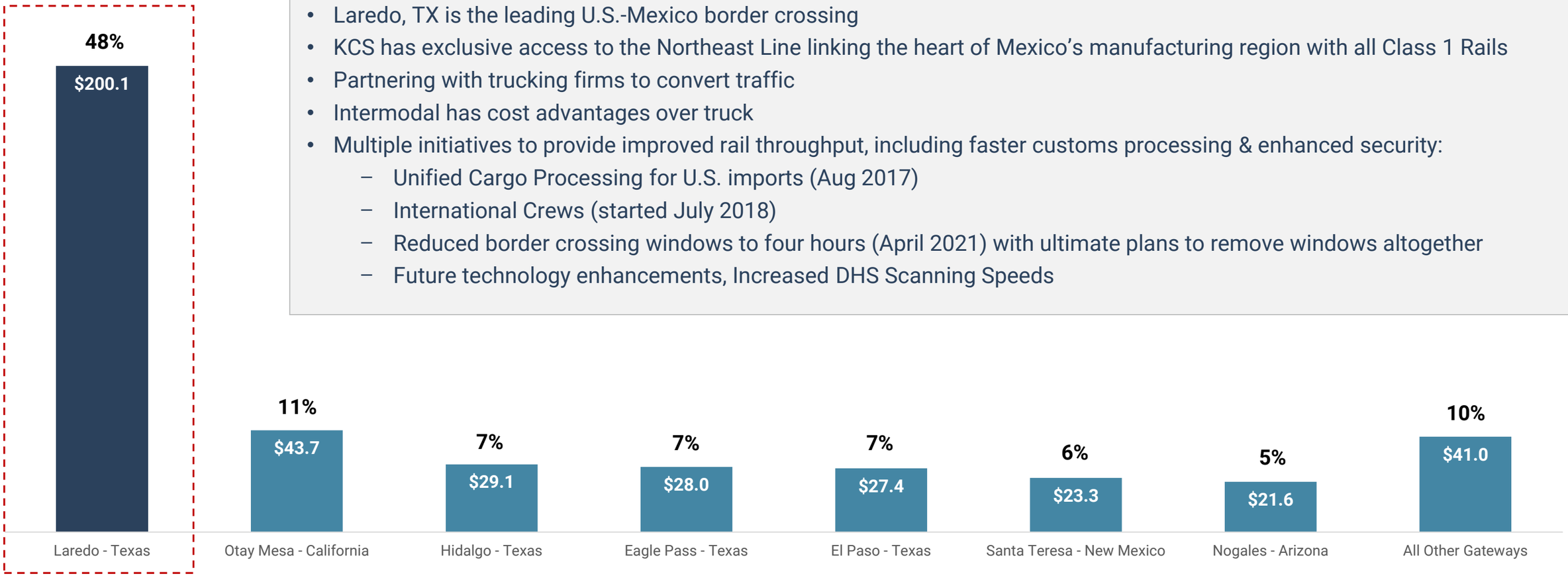
CN-KCS will be very well positioned to participate in Mexico's growing economy and near-sourcing phenomenon

Source: KCS public filings

Creating A Seamless, Same-System U.S.–Mexico Connection via Laredo, TX

2020 U.S. & Mexico Surface Trade by Border Crossing Import and Export

Value (US$ billions) & % Share



Commentary

- Laredo, TX is the leading U.S.-Mexico border crossing
- KCS has exclusive access to the Northeast Line linking the heart of Mexico's manufacturing region with all Class 1 Rails
- Partnering with trucking firms to convert traffic
- Intermodal has cost advantages over truck
- Multiple initiatives to provide improved rail throughput, including faster customs processing & enhanced security:
  - Unified Cargo Processing for U.S. imports (Aug 2017)
  - International Crews (started July 2018)
  - Reduced border crossing windows to four hours (April 2021) with ultimate plans to remove windows altogether
  - Future technology enhancements, Increased DHS Scanning Speeds

The CN-KCS Premier USMCA rail network will connect the U.S. and Mexico through the #1 gateway in Laredo, TX

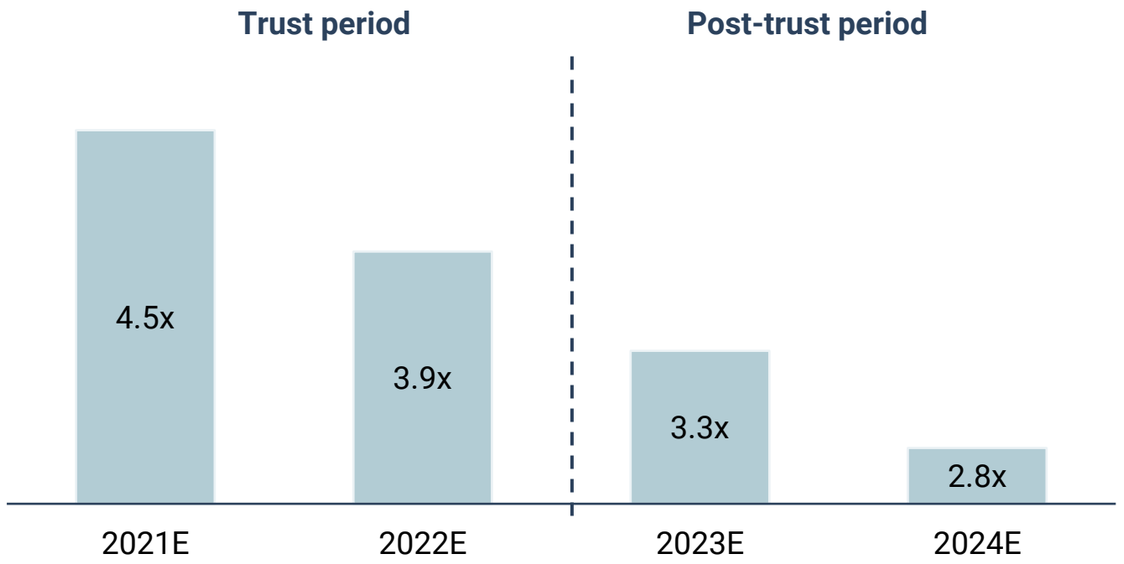
Source: KCS public filings

Committed to Maintaining a Strong Balance Sheet and Investment Grade Rating – During and After the Voting Trust

CN's Strong Financial Profile

- Strongest balance sheet among Class I rail carriers
- S&P and Moody's expect CN to remain investment grade
- Suspended share buy-backs
- Strong FCF profile
- Continued capital expenditure investments
- Rapid deleveraging profile

Projected Rapid Deleveraging Profile (1)



CN is committed to maintaining a strong financial position and investment grade profile

(1) Represents adjusted debt-to-adjusted EBITDA multiple, assuming closing into trust at end of 2021. Please see the heading Non-GAAP Measures in this presentation.

KCS Management and Governance While in Voting Trust

1. Continuity of KCS' existing governance and executive management

- KCS management will remain in control of KCS (CN will have no governance rights nor exercise any control over KCS)
- Pat Ottensmeyer will continue to lead KCS as CEO, reporting to the Board and the Trustee
- KCS' Board has approved retention bonuses to ensure the team stays in place and manages the company

2. No change in KCS' existing strategic plan and operations

- KCS management will lead and operate KCS in the same manner as it currently does
- KCS will act in the ordinary course of business and will continue to pursue its existing strategic plan

3. No change in capital allocation policy; KCS will continue to be well-capitalized and make investments in its business

- Investment grade rating of BBB+ / Baa2
- KCS will continue to deploy 40-50% of available cash to capital expenditures
- KCS will make marketing and capital investments with the interests of KCS and its customers in mind, not those of CN

CN application satisfies every aspect of Voting Trust approval framework

Exhibit 15

Excerpts from Canadian Pacific Railway Limited Form F-4 Registration Statement, filed with the Securities and Exchange Commission on October 1, 2021

SECURITIES AND EXCHANGE COMMISSION

FORM F-4

Registration statement for securities issued by foreign private issuers in certain business combination transactions

Filing Date: **2021-10-01**
SEC Accession No. 0001193125-21-289901

(HTML Version on secdatabase.com)

FILER

CANADIAN PACIFIC RAILWAY LTD/CN
CIK:**16875**| IRS No.: **980355078** | Fiscal Year End: **1231**
Type: **F-4** | Act: **33** | File No.: **333-259991** | Film No.: **211300045**
SIC: **4011** Railroads, line-haul operating

Mailing Address
7550 OGDEN DALE ROAD S.E.
CALGARY ALBERTA A0 T2C 4X9

Business Address
7550 OGDEN DALE ROAD S.E.
CALGARY ALBERTA A0 T2C 4X9
403-319-3591

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Table of Contents

As filed with the Securities and Exchange Commission on October 1, 2021

Registration No. 333-[–]

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM F-4
REGISTRATION STATEMENT
UNDER
THE SECURITIES ACT OF 1933

Canadian Pacific Railway Limited
(Exact name of registrant as specified in its charter)

Canada	4011	98-0355078
(State or other jurisdiction of incorporation or organization)	**(Primary Standard Industrial Classification Code Number)**	**(IRS Employer Identification Number)**

7550 Ogden Dale Road S.E., Calgary, Alberta,
Canada, T2C 4X9
(403) 319-7000
(Address, including zip code, and telephone number, including area code, of registrant' s principal executive offices)

With copies to:

Jeffrey J. Ellis	Francis J. Aquila	Adam Godderz	Steven A. Rosenblum
Canadian Pacific Railway Limited	C. Andrew Gerlach	Kansas City Southern	Elina Tetelbaum
7550 Ogden Dale Road S.E.	Sullivan & Cromwell LLP	427 West 12th Street	Wachtell, Lipton, Rosen & Katz
Calgary, Alberta, Canada T2C 4X9	125 Broad Street	Kansas City, Missouri 64105	51 West 52nd Street
(403) 319-7000	New York, New York 10004	(816) 983-1303	New York, New York 10019
	(212) 558-4000		(212) 403-1000

Approximate date of commencement of proposed sale of the securities to the public:
As soon as practicable after the effectiveness of this registration statement and upon completion of the transaction described in the enclosed proxy statement/prospectus.

If this Form is filed to register additional securities for an offering pursuant to Rule 462(b) under the Securities Act of 1933, as amended, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. ☐

If this Form is a post-effective amendment filed pursuant to Rule 462(d) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. ☐

If applicable, place an X in the box to designate the appropriate rule provision relied upon in conducting this transaction:

U.S. Exchange Act Rule 13e-4(i) (*Cross-Border Issuer Tender Offer*) ☐
U.S. Exchange Act Rule 14d-1(d) (*Cross-Border Third Party Tender Offer*) ☐

Indicate by check mark whether the registrant is an emerging growth company as defined in Rule 405 of the Securities Act of 1933.

Emerging growth company ☐

If an emerging growth company that prepares its financial statements in accordance with U.S. GAAP, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards† provided pursuant to Section 7(a)(2)(B) of the Securities Act ☐

† The term "new or revised financial accounting standard" refers to any update issued by the Financial Accounting Standards Board to its Accounting Standards Codification after April 5, 2012.

The registrant hereby amends this registration statement on such date or dates as may be necessary to delay its effective date until the registrant shall file a further amendment which specifically states that this registration statement shall thereafter become effective in accordance with Section 8(a) of the Securities Act, or until this registration statement shall become effective on such date as the U.S. Securities and Exchange Commission, acting pursuant to said Section 8(a), may determine.

CALCULATION OF REGISTRATION FEE

Title of Each Class of Securities to Be Registered	Amount to Be Registered	Proposed Maximum Offering Price Per Share	Proposed Maximum Aggregate Offering Price	Amount of Registration Fee
Canadian Pacific Railway Limited common shares	264,723,380(1)	N/A	$16,669,128,225.64(2)	$1,545,228.19(3)

(1) Represents the maximum number of Canadian Pacific Railway Limited ("CPRL") common shares estimated to be issuable or subject to stock-based awards that may be assumed by the registrant upon the completion of the transaction described herein. The calculation of the number of CPRL common shares being registered is based on (a) the sum of (i) 90,789,609, an estimate of the maximum number of shares of common stock, par value $0.01 per share, of Kansas City Southern ("KCS") issued and outstanding as of September 27, 2021, and (ii) 1,000,744.6654, the maximum number of shares of KCS common stock issuable upon the exercise or settlement of KCS options and time-based and performance-based awards (collectively, the "KCS equity awards") with respect to KCS common stock (together, the "estimated number"), multiplied by (b) the exchange ratio of 2.884 CPRL common shares for each share of KCS common stock.

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(2) Calculated pursuant to Rules 457(c), 457(f)(1) and 457(f)(3) promulgated under the Securities Act of 1933, as amended (the "U.S. Securities Act"), and solely for the purpose of calculating the registration fee. The proposed maximum aggregate offering price of the securities being registered was calculated based on (a) the product of (i) $271.60, the average of the high and low prices for shares of KCS common stock as reported on the New York Stock Exchange on September 24, 2021, multiplied by (ii) the estimated number (which represents the estimated maximum number of shares of KCS common stock that may be exchanged in the transactions contemplated by the merger agreement described herein, as described in footnote (1) above), minus (b) $8,261,131,829.89 (which represents the estimated aggregate amount of cash that will be paid by CPRL to the holders of shares of KCS common stock in the transactions contemplated by the merger agreement described herein). In accordance with Rule 416, this registration statement also covers an indeterminate number of CPRL common shares as may be issuable as a result of stock splits, stock dividends or similar transactions.

(3) The registration fee for the securities registered hereby has been calculated pursuant to Section 6(b) of the U.S. Securities Act, by multiplying the proposed maximum aggregate offering price for the securities by 0.0000927.

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Table of Contents

"*The KCS Merger Proposal–Opinion of Morgan Stanley*" and "*The KCS Merger Proposal–Opinion of BofA Securities*" on pages 71 and 84, respectively. After further discussion and deliberation, the KCS board unanimously determined that the final CPRL proposal continued to constitute a company superior proposal and approved the proposed waiver letter agreement with CN, termination of the CN merger agreement, KCS' s payment of the $700.0 million CN agreement termination payment and the $700.0 million CN refund owed to CN (or its affiliates) under the terms of the CN agreement, and KCS' s entry into the merger agreement with CPRL. The KCS board also approved the updated retention and severance arrangements set forth in the final CPRL proposal.

Following the completion of the KCS board meeting, KCS management notified CN of the KCS board' s determination, after which KCS and CN entered into the waiver letter agreement and KCS terminated the CN agreement and paid the $700.0 million CN agreement termination payment. Shortly thereafter, KCS delivered an executed signature page to the merger agreement with CPRL, which had already been executed by CPRL, and KCS and CPRL issued a joint press release announcing the transaction. Following execution of the merger agreement, CPRL remitted to KCS $700.0 million in connection with the payment of the CN agreement termination payment made by KCS to CN, KCS paid the $700.0 million CN refund to an affiliate of CN, and CPRL remitted to KCS $700.0 million in connection with the payment of the CN refund made by KCS to an affiliate of CN.

Recommendation of the KCS Board; KCS' s Reasons for the Transaction

At a special meeting held on September 15, 2021, the KCS board unanimously: (1) determined that it was in the best interests of KCS and its stockholders, and declared it advisable, to enter into the merger agreement with CPRL; (2) approved the execution, delivery and performance of the merger agreement and the transactions contemplated by the merger agreement (including the merger); (3) recommended that the stockholders of KCS adopt the merger agreement; and (4) directed that the merger agreement be submitted to a vote at a meeting of KCS' s stockholders. **The KCS board unanimously recommends that KCS stockholders vote "FOR" the merger proposal.**

In evaluating the transaction and in reaching its determinations and making its recommendations with respect to the merger agreement, the KCS board consulted with KCS senior management and outside legal and financial advisors over the course of several meetings, and considered a number of factors, including the following material factors that weighed in favor of the transaction.

Strategic Considerations and Synergies:

The KCS board believes the transaction will create the first rail network connecting the U.S., Mexico and Canada, with the ability to deliver dramatically expanded market reach for KCS and CPRL customers, provide new competitive transportation options, provide infrastructure, public safety and environmental benefits through truck to rail conversion opportunities, and support North American economic growth;

The KCS board believes CPRL and KCS are the fastest growing Class I railroads, with significant success in the transformation to Precision Scheduled Railroading;

The KCS board considered a synergy analysis (based on CPRL' s synergies analysis) showing annualized EBITDA synergies for the combined company of approximately $990 million (plus $20 million of capital expenditure and depreciation and amortization synergies) expected to be realized within the first three years after the transaction, primarily by executing the combined growth strategies of KCS and CPRL with new efficiencies for customers and improved on-time performance under their respective PSR programs; the KCS board also considered a more conservative synergy analysis
prepared by KCS management showing EBITDA synergies of approximately $377 million (plus

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$23 million of capital expenditure and depreciation and amortization synergies) over three years, and assessed both synergy analyses in making its decision, as further described in the section entitled "*KCS Unaudited Prospective Financial Information*";

The KCS board believes that the combined company will have the scale, balance sheet strength, financial flexibility, and free cash flow to fund future growth, and improved ability to access the capital markets on more favorable terms than available to KCS as an independent company, which would allow the combined company to be more competitive in capturing strategic opportunities;

The KCS board received information from and had discussions with KCS' s management, in consultation with outside financial advisors, regarding CPRL' s business, results of operations, financial and market position, KCS management' s expectations concerning the combined company' s business and financial prospects, and historical and current trading prices of CPRL common shares;

Attractive Value and Mix of Consideration

The KCS board considered the aggregate value and nature of the consideration to be received in the transaction by KCS stockholders, including:

that the merger consideration had an implied value per share of KCS common stock of $300, based on the closing price of CPRL common shares on the NYSE as of August 9, 2021 (the last full trading day prior to the date on which CPRL submitted the revised CPRL proposal), which represented a premium of approximately 34% to KCS stockholders based on the unaffected closing price of KCS common stock on March 19, 2021 (the last trading day before the KCS board' s approval of and the announcement of the prior CP merger agreement);

that based on CPRL' s market price on September 13, 2021, approximately 69% of the merger consideration consists of CPRL common shares, with the CPRL common shares to be issued to KCS common stockholders constituting approximately 28% of the outstanding shares of CPRL common shares following the transaction, offering KCS common stockholders the opportunity for meaningful ownership participation in the future earnings, dividends, synergies and growth of the combined company, a company which the KCS board considers to be an attractive investment for the reasons discussed above in the section entitled "*Strategic Considerations and Synergies*";

that based on CPRL' s market price on September 13, 2021, approximately 31% of the merger consideration consists of cash, which provides KCS stockholders with immediate liquidity for a portion of their shares; and

that the first merger and the second merger, taken together, are intended to qualify as a "reorganization" within the meaning of Section 368(a) of the Code and that Section 367(a)(1) of the Code will not apply to cause the mergers to result in gain recognition by holders of KCS common stock that exchange their shares of KCS common stock for the merger consideration (other than any Excepted Shareholder), as more fully described in the section entitled "*Material U.S. Federal Income Tax Consequences*";

Attractive Strategic Alternative:

The KCS board believes that the transaction with CPRL is attractive in comparison to the alternative of remaining independent and continuing to execute on KCS' s long-range business strategy and is also attractive in comparison to other alternatives, including the CN agreement. In this regard, the KCS board considered:

the course and history of KCS' s discussions and competitive negotiations with Party A and CN, including: (i) the fact that, after six rounds of bidding, Party A' s last proposal to acquire KCS for

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Table of Contents

have received or in the future may receive compensation for the rendering of these services, including (i) having acted as a bookrunning manager and/or co-manager on certain debt capital markets transactions for CPRL, (ii) having acted or acting as a lender under CPRL' s $1.3 billion revolving credit facility, which consists of a $1.0 billion tranche and a $300 million tranche, which was amended on September 24, 2021 to extend the maturity dates of such tranches to September 27, 2026 and September 27, 2023, respectively, and (iii) having provided or providing certain treasury services and products to CPRL. From September 1, 2019, through August 31, 2021, BofA Securities and its affiliates derived aggregate revenues from CPRL of approximately $6.6 million for corporate and/or investment banking services. In addition, BofA Securities received a customary fee of less than $100,000 in connection with its commitment to act as a lender under CPRL' s amended revolving credit facility, which was received subsequent to such period.

KCS Unaudited Prospective Financial Information

The prospective financial information included in this section has been prepared by, and is the responsibility of, KCS' s management. This prospective financial information was not prepared with a view toward compliance with published guidelines of the SEC or the guidelines established by the American Institute of Certified Public Accountants for preparation or presentation of prospective financial information.

Neither Deloitte LLP nor PricewaterhouseCoopers LLP has audited, reviewed, examined, compiled nor applied agreed-upon procedures with respect to the accompanying prospective financial information and, accordingly, neither Deloitte LLP nor PricewaterhouseCoopers LLP expresses an opinion or any other form of assurance with respect thereto. The PricewaterhouseCoopers LLP report incorporated by reference in this document relates to KCS' s previously issued financial statements. It does not extend to the prospective financial information and should not be read to do so.

Summary of KCS Prospective Financial Information

KCS Unaudited Prospective Financial Information

As described under the section of this proxy statement/prospectus entitled "*The KCS Merger Proposal–Background of the Transaction*," on page 49, KCS management maintains the KCS long-range plan, which is periodically updated and reviewed with the KCS board, that reflects KCS management' s financial and business outlook for KCS over a ten-year period. This KCS long-range plan was reviewed by the KCS board in connection with its consideration of a transaction with CPRL, CN and other potential strategic alternatives throughout the latter half of 2020 continuing through its meeting on September 15, 2021. The KCS long-range plan included certain unaudited prospective financial information concerning KCS on a standalone basis for the fiscal years ending December 31, 2021 through December 31, 2029. We refer to these unaudited projections as the "KCS management unaudited KCS projections". The KCS management unaudited KCS projections were provided to Morgan Stanley and BofA Securities, which were directed by KCS management to use and rely upon the KCS management unaudited KCS projections for purposes of their respective financial analyses and fairness opinions. In addition, certain of the KCS management unaudited KCS projections were provided to CPRL, the CPRL board and their respective financial advisors, BMO, Goldman Sachs and Evercore.

In connection with the transaction, KCS management also prepared certain unaudited prospective financial information concerning CPRL on a standalone basis using (i) the CPRL five-year plan (as prepared by CPRL management and provided to KCS management) and (ii) extrapolations prepared by KCS management on the basis of the CPRL five-year plan for the fiscal years ending December 31, 2026 through December 31, 2029. Such unaudited prospective financial information was translated into U.S. dollar amounts from the original Canadian dollar amounts presented in the CPRL five-year plan based on an assumed foreign exchange ratio of 1.25x. We refer to these unaudited projections as the "KCS management unaudited CPRL projections," and the KCS management unaudited KCS projections and the KCS management unaudited CPRL projections, collectively, as the "KCS management unaudited projections". The KCS management unaudited CPRL

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Table of Contents

projections were provided to the KCS board in connection with its consideration of the transaction as well as to Morgan Stanley and BofA Securities, which were directed by KCS management to use and rely upon the KCS management unaudited CPRL projections for purposes of their respective financial analyses and fairness opinions.

The KCS management unaudited projections were prepared treating KCS and CPRL, respectively, on a standalone basis, without giving effect to the transaction, including any impact of the negotiation or execution of the transaction, the expenses that may be incurred in connection with the transaction or the consummation thereof, the potential synergies that may be achieved by the combined company as a result of the transaction, the effect of any business or strategic decision or action that has been or will be taken as a result of the merger agreement having been executed or in anticipation of the transaction, or the effect of any business or strategic decisions or actions which would likely have been taken if the merger agreement had not been executed but which were instead altered, accelerated, postponed or not taken in anticipation of the transaction.

In connection with the transaction, KCS management prepared pro forma analyses, which were presented to the KCS board, that included CPRL' s estimated potential earnings before interest, taxes, depreciation and amortization (which we refer to as "EBITDA") synergies of $990 million (consisting of $810 million from revenue synergies and $180 million from operating and expense synergies), together with an alternative case showing a lower estimate of potential EBITDA synergies of $377 million (consisting of $222 million from revenue synergies and $155 million from operating and expense synergies). The primary difference between the two cases was a more conservative assumption on revenue synergies (specifically the combined company' s share of bulk commodities) in the $377 million EBITDA synergies case. The assumptions used in the $990 million EBITDA synergies case were based on CPRL' s assessment of market opportunities that the combined company could reasonably be expected to capture, leading to a substantially greater estimate of revenue synergies. KCS management believed, however, that for purposes of the KCS board' s consideration of the transaction, the KCS board should also consider a synergies estimate reflecting the more conservative assumptions. The $377 million EBITDA synergies case also used slightly more conservative assumptions with respect to operating and expense synergies. The pro forma analyses, in each case, assumed a phase-in of synergies over the three years following CPRL' s receipt of STB final approval, beginning in fiscal year 2023. KCS management, among other things, assumed that the aggregate cost of achieving the projected synergies would be, with respect to the $990 million synergies case, $180 million, and with respect to the $377 million synergies case, $155 million, with half of the costs to be incurred in the first year of the phase-in and the remaining half to be incurred in the second year of the phase-in. KCS management also assumed, with respect to the $990 million synergies case, no dissynergies, $20 million of capital expenditure and depreciation and amortization synergies and a one-time capital investment of $50 million, and, with respect to the $377 million synergies case, $50 million of dissynergies and $23 million of capital expenditure and depreciation and amortization synergies. These assumed dissynergies or additional synergies were subtracted from or added to the EBITDA synergies estimates. The assumed EBITDA synergies, including the cost to achieve such synergies, included in the two cases (which we refer to collectively as the "KCS management assumed synergies") are not reflected in the KCS management unaudited projections. The KCS management assumed synergies were provided to Morgan Stanley and BofA Securities, which were directed by KCS management to use and rely upon the KCS management assumed synergies for purposes of their respective financial analyses and fairness opinions.

Other than annual financial guidance provided to investors, which is generally updated each quarter, KCS does not as a matter of course make public long-term forecasts or projections as to future performance, revenues, earnings or other results, due to, among other reasons, the inherent difficulty of accurately predicting financial performance for future periods and the uncertainty of the underlying assumptions and estimates. However, the financial projections by KCS management are being included in this proxy statement/prospectus to give shareholders access to certain non-public information provided to the KCS board and KCS' s financial advisors and to CPRL and the CPRL board and their respective financial advisors. The inclusion of the financial projections by KCS should not be regarded as an indication that the KCS board, KCS, the CPRL board, CPRL, Morgan Stanley, BofA Securities, BMO, Goldman Sachs or Evercore or any other recipient of this information

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considered, or now considers, it to be an assurance of the achievement of future results or an accurate prediction of future results, and they should not be relied on as such.

This prospective financial information was not prepared with a view toward compliance with published guidelines of the SEC or the guidelines established by the American Institute of Certified Public Accountants for preparation or presentation of prospective financial information, or GAAP, but, in the view of KCS' s management were prepared on a reasonable basis, reflected the best available estimates and judgments at the time of preparation, and presented as of the time of preparation, to the best of KCS' s management' s knowledge and belief, the expected course of action and the expected future financial performance of KCS or CPRL, as applicable. However, this information is not fact and should not be relied upon as being necessarily indicative of future results, and readers of this proxy statement/prospectus are cautioned not to place undue reliance on the KCS management unaudited projections or the KCS management assumed synergies. Although KCS' s management believes there is a reasonable basis for the KCS management unaudited projections and the KCS management assumed synergies, KCS cautions stockholders that future results could be materially different from the KCS management unaudited projections and the KCS management assumed synergies. This summary of the KCS management unaudited projections and the KCS management assumed synergies is included in this proxy statement/prospectus because the KCS management unaudited projections and the KCS management assumed synergies were provided to KCS' s financial advisors and to the KCS board for purposes of considering and evaluating the transaction and the merger agreement.

Other than annual financial guidance provided to investors, CPRL does not as a matter of course share with third parties long-term forecasts or projections as to future performance, revenues, earnings or other results due to, among other reasons, the inherent difficult of accurately predicting financial performance for future periods and the uncertainty of underlying assumptions and estimates. CPRL' s management prepared and provided to KCS' s management the CPRL five-year plan solely in connection with KCS' s consideration of a transaction with CPRL. The fact that the CPRL five-year plan was provided to KCS management should not be regarded as an indication that the CPRL board, CPRL, KCS or any other recipient of the CPRL five-year plan considered, or now considers, it to be an assurance of the achievement of future results or an accurate prediction of future results of CPRL, and it should not be relied on as such.

The KCS management unaudited projections and the KCS management assumed synergies are subject to estimates and assumptions in many respects and, as a result, subject to interpretation. While presented with numerical specificity, the KCS management unaudited projections and the KCS management assumed synergies are based upon a variety of estimates and assumptions that are inherently uncertain, though considered reasonable by KCS' s management as of the date of their preparation. These estimates and assumptions may prove to be inaccurate for any number of reasons, including general economic conditions, industry trends, the regulatory environment, competition, and the risks discussed in this proxy statement/prospectus under the sections entitled "*Cautionary Statement Regarding Forward-Looking Statements*" and "*Risk Factors*" beginning on pages 36 and 21, respectively. See also "*Where You Can Find Additional Information*" beginning on page 229. The KCS management unaudited projections and the KCS management assumed synergies also reflect assumptions as to certain business decisions that are subject to change. Because the KCS management unaudited projections were developed for KCS on a standalone basis without giving effect to the transaction, they do not reflect any divestitures or other restrictions that may be imposed in connection with the receipt of any necessary governmental or regulatory approvals, any synergies that may be realized as a result of the transaction or any changes to KCS' s or CPRL' s operations or strategy that may be implemented after completion of the transaction. There can be no assurance that the KCS management unaudited projections or the KCS management assumed synergies will be realized, and actual results may differ materially from those shown. Generally, the further out the period to which the KCS management unaudited projections and the KCS management assumed synergies relate, the less predictable and more unreliable the information becomes.

The KCS management unaudited projections contain certain non-GAAP financial measures that KCS believes are helpful in understanding its past financial performance and future results. KCS management regularly uses a

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Table of Contents

variety of financial measures that are not in accordance with GAAP for forecasting, budgeting and measuring financial performance. The non-GAAP financial measures are not meant to be considered in isolation or as a substitute for comparable GAAP measures. While KCS believes that these non-GAAP financial measures provide meaningful information to help investors understand the operating results and to analyze KCS' s financial and business trends on a period-to-period basis, there are limitations associated with the use of these non-GAAP financial measures. These non-GAAP financial measures are not prepared in accordance with GAAP, are not reported by all of KCS' s competitors and may not be directly comparable to similarly titled measures of KCS' s competitors due to potential differences in the exact method of calculation.

Financial measures included in projections provided to a financial advisor and a board of directors in connection with a business combination transaction are excluded from the definition of "non-GAAP financial measures" under the rules of the SEC, and therefore such financial measures are not subject to SEC rules regarding disclosures of non-GAAP financial measures, which may otherwise require a reconciliation of a non-GAAP financial measure to a GAAP financial measure. Reconciliations of non-GAAP financial measures were not provided to and were not relied on by Morgan Stanley or BofA Securities for purposes of their respective financial analyses and opinions or by the KCS board in connection with its consideration of the transaction, nor were they provided to CPRL or its financial advisors. Accordingly, a reconciliation of these non-GAAP financial measures has not been provided.

None of KCS, CPRL, the combined company or their respective affiliates, advisors, officers, directors or other representatives can provide any assurance that actual results will not differ from the KCS management unaudited projections or the KCS management assumed synergies, and none of them undertakes any obligation to update, or otherwise revise or reconcile, the KCS management unaudited projections or the KCS management assumed synergies to reflect circumstances existing after the date the KCS management unaudited projections or the KCS management assumed synergies were prepared or to reflect the occurrence of future events, even in the event that any or all of the assumptions underlying the KCS management unaudited projections or the KCS management assumed synergies, as applicable, are shown to be in error. Except as required by applicable securities laws, KCS does not intend to make publicly available any update or other revision to the KCS management unaudited projections or the KCS management assumed synergies, even in the event that any or all assumptions are shown to be in error. None of KCS or its affiliates, advisors, officers, directors or other representatives has made or makes any representation to any KCS stockholder or other person regarding KCS' s ultimate performance compared to the information contained in the KCS management unaudited projections or the KCS management assumed synergies or that forecasted results will be achieved. KCS has made no representation to CPRL, in the merger agreement or otherwise, concerning the KCS management unaudited projections or the KCS management assumed synergies.

The prospective financial information included in this document has been prepared by, and is the responsibility of, KCS management. Neither PricewaterhouseCoopers LLP nor Deloitte LLP have audited, reviewed, examined, compiled nor applied agreed-upon procedures with respect to the accompanying prospective financial information and, accordingly, neither PricewaterhouseCoopers LLP nor Deloitte LLP express an opinion or any other form of assurance with respect thereto. The PricewaterhouseCoopers LLP report incorporated in this document relates to KCS' s previously issued financial statements, and the Deloitte LLP reports incorporated in this document relate to CPRL' s previously issued financial statements. These reports do not extend to the prospective financial information and should not be read to do so.

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Table of Contents

The following table presents a summary of the KCS management unaudited KCS projections that were reviewed by the KCS board in connection with its consideration of the transaction and provided to Morgan Stanley and BofA Securities for purposes of their respective financial analyses and fairness opinions. In addition, certain of the KCS management unaudited KCS projections were provided to CPRL.

(Dollars in millions)	FY' 21	FY' 22	FY' 23	FY' 24	FY' 25	FY' 26	FY' 27	FY' 28	FY' 29
Revenue	$2,992	$3,292	$3,554	$3,748	$3,946	$4,143	$4,344	$4,556	$4,770
EBITDA(1)	1,551	1,827	2,033	2,174	2,318	2,462	2,610	2,768	2,928
Capital Expenditures	500	541	586	618	651	684	717	752	787
EPS(2)	8.29	10.75	12.60	14.21	16.06	18.04	20.20	22.60	25.20
Unlevered Free Cash Flow(3)	364 (4)	779	940	1,013	1,089	1,164	1,242	1,324	1,408

(1) EBITDA is defined as earnings before interest, taxes, depreciation and amortization.
(2) EPS is defined as diluted earnings per share adjusted for the depreciation component of income tax driven by the difference in the Mexican peso to U.S. dollar exchange rate that existed at the time assets in Mexico were put into service and the current Mexican peso to U.S. dollar exchange rate.
(3) Unlevered Free Cash Flow is defined as EBITDA less depreciation and amortization, plus other income, less other expenses, tax affected, plus depreciation and amortization, adjusted for changes in net working capital, less capital expenditures and less other investing activities. The calculation of Unlevered Free Cash Flow was not expressly included in the KCS management unaudited KCS projections but was derived from the KCS management unaudited KCS projections and is included for reference.
(4) Figure represents July – December 2021.

The following table presents a summary of the KCS management unaudited CPRL projections that were provided to the KCS board in connection with its consideration of the transaction as well as to Morgan Stanley and BofA Securities for purposes of their respective financial analyses and fairness opinions.

(Dollars in millions)	FY' 21	FY' 22	FY' 23	FY' 24	FY' 25	FY' 26	FY' 27	FY' 28	FY' 29
Revenue	$6,580	$7,086	$7,498	$7,875	$8,287	$8,694	$9,111	$9,551	$9,995
EBITDA(1)	3,526	3,862	4,127	4,376	4,652	4,943	5,242	5,558	5,878
Capital Expenditures	1,260	1,240	1,200	1,224	1,249	1,310	1,373	1,439	1,506
Unlevered Free Cash Flow(2)	852 (3)	1,989	2,267	2,457	2,666	2,603	2,775	2,958	3,143

(1) EBITDA is defined as earnings before interest, taxes, depreciation and amortization.
(2) Unlevered Free Cash Flow is defined as EBITDA less depreciation and amortization, plus other income, less other expenses, tax affected, plus depreciation and amortization, less capital expenditures, less other cash/non-cash expenses, plus land sales and others and plus increase in deferred tax liability.
(3) Figure represents July – December 2021.

Listing of CPRL Common Shares

It is a condition to the completion of the transaction that the CPRL common shares issuable under the merger agreement are approved for listing on the NYSE, subject to official notice of issuance, and the TSX, subject to customary listing requirements.

CPRL must use its reasonable best efforts to cause the CPRL common shares to be issued in the first merger to be approved for listing on the NYSE, subject to official notice of issuance, and the TSX, subject to customary listing conditions, prior to the effective time. Listing will be subject to CPRL fulfilling all the listing requirements of the NYSE and TSX. There can be no assurance that the CPRL common shares will be accepted for listing on the NYSE or the TSX.

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Exhibit H

UP-10

BEFORE THE
SURFACE TRANSPORTATION BOARD

Finance Docket No. 36500

CANADIAN PACIFIC RAILWAY LIMITED; CANADIAN PACIFIC RAILWAY COMPANY; SOO LINE RAILROAD COMPANY; CENTRAL MAINE & QUEBEC RAILWAY US INC.; DAKOTA, MINNESOTA & EASTERN RAILROAD CORPORATION; AND DELAWARE & HUDSON RAILWAY COMPANY, INC.
—CONTROL—
KANSAS CITY SOUTHERN; THE KANSAS CITY SOUTHERN RAILWAY COMPANY; GATEWAY EASTERN RAILWAY COMPANY; AND THE TEXAS MEXICAN RAILWAY COMPANY

UNION PACIFIC RAILROAD COMPANY'S COMMENTS AND REQUEST FOR CONDITIONS

CRAIG V. RICHARDSON
JAMES B. BOLES
TONYA W. CONLEY
WHITNEY LARKIN
Union Pacific Railroad Company
1400 Douglas Street
Omaha, Nebraska 68179
(402) 544-7004

MICHAEL L. ROSENTHAL
DEREK LUDWIN
JAMES J. O'CONNELL
PRATIK AGARWAL
SAHEL SRA
Covington & Burling LLP
One CityCenter
850 Tenth Street, NW
Washington, D.C. 20001
(202) 662-6000

Attorneys for Union Pacific Railroad Company

February 28, 2022

TABLE OF CONTENTS

I. Introduction And Summary Of Position 2

A. An Unconditioned Combination of CP and KCS Would Likely Cause a Significant Loss of Competition to the Detriment of Shippers 2

B. The Public Interest Requires CPKC to Bear the Costs of New Capacity Necessary to Implement the Proposed Transaction. 10

II. A Combination Of CP And KCS Would Likely Cause A Substantial Lessening Of Competition For Traffic Moving Via The Laredo Gateway And Other Gateways. 12

A. The Laredo Gateway Is Vitally Important to U.S.-Mexico Rail Transportation and the Proposed Combination of CP and KCS. 14

1. The Laredo Gateway Is Critical to Applicants' Plans. 14

2. The Board Has Recognized the Need to Protect Rail Competition Via the Laredo Gateway. 15

3. The Laredo Gateway Remains Critical to U.S.-Mexico Rail Transportation. 16

B. CP Control of KCS Would Undermine Competition Via the Laredo Gateway. 19

1. Shippers Benefit from Competition at the Laredo Gateway. 19

2. CPKC Would Have the Incentive and Ability to Use Its Control of KCSM to Deprive Shippers of the Price and Service Benefits of UP-KCSM Routings. 21

III. The Board Should Not Simply Presume That The Proposed Transaction Would Not Have Anticompetitive Effects. 32

A. Professor Salop's Analysis Explains Why Reliance on the One-Lump Presumption Would be Inappropriate in This Case. 35

B. The Statement of Applicants' Expert Does Not Support a Presumption That the Proposed Transaction Will Not Have Anticompetitive Effects. 39

C. A Presumption That Certain Categories of Mergers Are Procompetitive Is Inconsistent With Current Antitrust Enforcement Policy. 44

IV. Other Transportation Alternatives Will Not Prevent Anticompetitive Effects. 46

V. Mexico's Regulatory Regime Will Not Prevent CPKC From Engaging In Anticompetitive Acts Affecting U.S. Shippers. 48

VI. Applicants' Failure To Address The Proposed Transaction's Impacts On Facilities Applicants Share With Other Railroads Precludes The Board From Finding That An Unconditioned Transaction Would Be Consistent With The Public Interest. 50

A. Applicants Failed to Address Their Operations on Lines Owned by UP 53

B. Applicants Failed to Fully Address Operations on Facilities They Own and Share With Others. 59

VII. If The Board Approves The Proposed Transaction, It Should Impose Conditions To Protect Competition At The Laredo Gateway And Other Gateways And To Address Fully The Infrastructure Needed To Support Applicants' Planned Traffic Growth. 67

A. The Board Should Impose Conditions to Protect Competition at Gateways. 68

1. The Board Should Require CPKC to Offer Shippers "Commercially Reasonable" Rates to Gateways Based on a Mileage Prorate of CPKC Single-Line Rates. 69

2. The Board Should Require CPKC to Comply with KCS's Promises Regarding Laredo Gateway Operations and the Laredo Bridge. 74

B. The Board Should Impose Conditions to Remedy Applicants' Failure to Address Investment in Joint Facilities. 76

VIII. Conclusion 77

VERIFIED STATEMENTS

Verified Statement of Kenny Rocker and John Turner

Verified Statement of Steven C. Salop

Verified Statement of Thomas C. Haley

Verified Statement of Luis F. de la Calle

EXHIBITS

Ex. 1 W. Robert Majure Deposition Transcript (excerpts)

Ex. 2 CP Letter to National Industrial Transportation League (CP-C-00000851–854)

Ex. 3 KCS and CP's Joint Responses and Objections to UP's First Set of Discovery Requests (excepts)

Ex. 4 CP Additional Comments in *KCS/Tex Mex* (CPR-5), FD 34342 (Sept. 30, 2004)

Ex. 5. Patrick J. Ottensmeyer Deposition Transcript (excerpts)

Ex. 6 KCS Schedule 14A (Nov. 3, 2021) (excerpt)

Ex. 7 John Brooks Deposition Transcript (excerpts)

Ex. 8 Lazaro Cardenas Presentation (KCSR-C-00016306–16312)

Ex. 9 Lazaro Cross-Border Pricing Business Review (KCSR-HC-00017701–17707)

Ex. 10. UP's Motion to Compel (UP-8) (Jan. 27, 2022) (excerpt)

Ex. 11 KCS and CP's Joint Responses and Objections to UP's Second Set of Discovery Requests (excerpt)

Ex. 12 KCS and CP's Supplemental Joint Responses and Objections to CSXT's Second Set of Discovery Requests (excerpts)

Ex. 13 KCS Policy on Rate Offers for KCSM Routes (KCSR-HC-00020720–20726)

Ex. 14 CP Board of Directors Meeting Materials (CP-HC-00010640–10678) (excerpt)

Ex. 15 Raymond J. Elphick and John F. Orr Deposition Transcript (excerpts)

Ex. 16 Elphick/Orr Deposition Exhibit 2 (OP Plan workpaper "HC - Capacity - Methodology_docx.docx")

Ex. 17 Elphick/Orr Deposition Exhibit 3 (OP Plan workpaper "HC - 2021 - 10-20 CP RJct-KCity and KCS KCity-Laredo.pdf")

Ex. 18 Elphick/Orr Deposition Exhibit 7 (CP-HC-00007947.xlsx)

Ex. 19 Applicants' Reply to UP's Motion to Compel (Feb. 7, 2022)

Ex. 20 Brooks Deposition Exhibit 8 (CP-HC-00006432–6439)

UNION PACIFIC RAILROAD COMPANY'S COMMENTS AND REQUEST FOR CONDITIONS

UP submits these comments on CP's proposed combination with KCS.[1] In support of these comments, UP is submitting the joint verified statement of Kenny Rocker, UP's Executive Vice President, Marketing and Sales, and John Turner, UP's Vice President, Network Planning & Operations, as well as verified statements from Steven C. Salop, Professor of Economics and Law at the Georgetown University Law Center, Thomas C. Haley, an independent railroad consultant, and Dr. Luis de la Calle, managing director and founding partner of De la Calle, Madrazo, Mancera, S.C.

An unconditioned combination of CP and KCS would likely cause a significant loss of competition, especially for traffic moving via the Laredo Gateway. CP would gain control of KCSM, and thus the ability to increase the costs or reduce the quality of rail service in Mexico for railroads providing shippers competitive options to CPKC north of Laredo. CPKC would have a strong incentive to engage in this type of anticompetitive conduct: to meet Applicants' aggressive promises to investors, CPKC must divert substantial volumes of business from shippers currently using UP or BNSF to provide service north of Laredo without sacrificing profits. The limited (if not illusory) efficiencies arising from the proposed transaction will not achieve those aggressive promises. UP's comments propose narrowly tailored conditions the Board should impose to prevent the reduction of competitive options at gateways, particularly the Laredo Gateway.

UP's comments also address a fundamental issue Applicants failed to discuss in their Application: the need for investment in jointly-used rail infrastructure critical to implementing

[1] UP is using the abbreviations the Board used in Decision No. 11 in this proceeding, served November 23, 2021.

their proposed transaction, including investment necessary to maintain fluid operations in the Houston terminal. Applicants should not expect others to subsidize their transaction. The Board should not allow Applicants to increase their operations over lines they share with other railroads until they reach agreements with those railroads regarding investments in new capacity necessary to accommodate the traffic levels projected in their Application.

I. Introduction And Summary Of Position

A. An Unconditioned Combination of CP and KCS Would Likely Cause a Significant Loss of Competition to the Detriment of Shippers.

An unconditioned combination of CP and KCS would likely cause a significant loss of competition among railroads in the United States, especially for traffic moving via the Laredo Gateway, to the ultimate detriment of shippers. CPKC would control KCSM, the only railroad serving the Mexican side of the critically important Laredo Gateway. The Board recognized long ago that rail competition via the Laredo Gateway must be protected because other gateways and other modes do not provide effective alternatives. KCS's right to operate from Kansas City to Laredo exists only because the Board concluded in 1996 that the Laredo Gateway "occupied a position of separate and surpassing economic significance" to U.S.-Mexico rail transportation.[2]

Since 1996, the Laredo Gateway has become even more important to cross-border trade. In 2019, the Port of Laredo was the leading U.S.-international freight gateway, moving $226.8 billion in cargo, which included 264,406 loaded rail containers crossing from Mexico to the

[2] *Union Pac. Corp.—Control & Merger—S. Pac. Rail Corp.* ("*UP/SP*"), 1 S.T.B. 233, 422 (1996). In that proceeding, one of the Applicants here, Tex Mex, argued that U.S. policy regarding the North American Free Trade Agreement required the Board to "give heightened scrutiny to transactions within its jurisdiction that present a danger of diminishing competition for transportation of U.S.-Mexican traffic." *UP/SP*, FD 32760, Brief of the Texas Mexican Ry. (TM-39) at 17 (June 3, 1996).

United States, an increase of 282% from 69,204 loaded rail containers in 1996.[3] The Board should prioritize protecting the Laredo Gateway in evaluating the proposed combination.

The Biden Administration has emphasized the need for vigilance against vertical (*e.g.*, end-to-end) mergers that harm competition, as well as the need to protect shippers, and has called on the Board to work with the antitrust enforcement and other agencies to meet these goals.[4] Consistent with that approach, the DOJ and FTC have rejected the notion that vertical mergers are presumptively procompetitive, and instead are challenging proposed vertical transactions where the agencies identify potential harm to consumers.[5]

Applicants' own evidence shows why a CP/KCS combination would harm shippers. Applicants' expert economist, Dr. Majure, concedes that end-to-end mergers can cause competitive harm where the merged carrier would have the ability and incentive to force inferior terms on shippers.[6] The evidence shows CPKC would have both such ability and such incentive.

CPKC Would Have the Ability to Force Inferior Terms on Shippers. Applicants do not address the *ability* of a combined CPKC to force inferior rate and service terms on a

---

[3] U.S. Department of Transportation, Bureau of Transportation Statistics, *Freight Facts and Figures* (2019), https://data.bts.gov/stories/s/International-Freight-Gateways/4s7k-yxvu/

[4] *Executive Order on Promoting Competition in the American Economy* (July 9, 2021) ("*Biden Competition Order*"), Sec. 2(d) (Board charged with "resisting consolidation and promoting competition within industries through the independent oversight of mergers"), https://www.whitehouse.gov/briefing-room/presidential-actions/2021/07/09/executive-order-on-promoting-competition-in-the-american-economy/

[5] *Prepared Remarks on Modernizing Merger Guidelines* (Jan. 18, 2022), https://www.justice.gov/opa/speech/assistant-attorney-general-jonathan-kanter-delivers-remarks-modernizing-merger-guidelines

[6] *See* APP Vol. 2 at 18, Majure VS ¶ 22.

References to "APP Vol." are to the consecutively numbered pages in the Application. References to verified statements accompanying the application are identified by the last name of the witness submitting the statement and "VS."

significant number of shippers who depend on rail service via the Laredo Gateway. Dr. Majure asserts that CPKC could not force inferior terms on hypothetical customers with "ready alternatives,"[7] but neither Dr. Majure nor any other witness for Applicants asserts (nor could they) that CPKC could not force inferior terms on customers that lack such ready alternatives.[8] Applicants' witnesses do not dispute that such customers exist; in fact, as Mr. Rocker explains, *many* shippers lack viable alternatives to rail service via Laredo.[9] And although Dr. Majure hypothesizes that FXE might be a viable competitive alternative to KCSM for some shippers,[10] he does not analyze the issue or show that FXE actually offers a viable option for shippers using KCSM.[11]

Mr. Rocker and Professor Salop also describe CPKC's ability to make UP-KCSM transportation less attractive to shippers in practical terms: CPKC could raise KCSM rate factors for shippers who prefer to use UP service north of Laredo, or reduce KCSM cooperation with UP on operational and service matters in Mexico and at the Laredo Gateway.[12] In sum, CPKC would have the ability to engage in anticompetitive conduct.

CPKC Would Have the Incentive to Force Inferior Terms on Shippers. Dr. Majure tries to dismiss concerns about CPKC's *incentives* to foreclose competition by pointing to the

[7] *See* APP Vol. 2 at 19–20, Majure VS ¶ 25.

[8] Professor Salop also shows that end-to-end transactions can produce anticompetitive effects even for shippers who have the option of using Ferromex ("FXE") service via an alternative Mexican gateway. *See* Salop VS ¶ 15, ¶¶ 62–72.

[9] *See* Rocker/Turner VS at 16–17.

[10] *See* APP Vol. 2 at 19–20, Majure VS ¶ 25.

[11] *See* Ex. 1 (Majure Tr. 84:18–24 ("Q: Have you done any analysis as to whether FXE is a ready alternative for shippers using KCSM today? A: No, I have not tried to isolate the -- or test whether this hypothetical applied to any particular shipper or the degree to which it was.")).

[12] *See* Rocker/Turner VS at 11–16; Salop VS ¶¶ 75, 81.

"one-lump theory." Under that theory, he asserts, CPKC would have no incentive to force inferior terms on customers who depend on KCSM service in Mexico and ship traffic from Laredo to points served by both CP and UP (or CP and BNSF), because KCS already collects the full measure of returns associated with KCSM's existing market power.[13] While that theory may apply in some circumstances, it does not apply in this particular case.

As Professor Salop explains, when an upstream monopolist (KCSM) and downstream rivals (UP and CP) lack full information about each other's costs and prices, or when the rivals provide differentiated services—*i.e.*, services that shippers view as qualitatively different—the monopolist generally cannot extract the full "one lump," so the shipper retains a surplus.[14] In those circumstances, which exist here, the merged carrier *does* have an incentive to engage in anticompetitive conduct: to eliminate the shipper's surplus and extract the full "one lump."[15]

In addition, and as Professor Salop also explains, CPKC will have *increased* incentives to foreclose rivals using the Laredo Gateway. That is because CPKC would capture a greater portion of the proceeds from a foreclosure strategy than KCS standing alone. That increased incentive undermines Applicants' unsupported assertions that the proposed merger will not change the status quo at Laredo Gateway.

To be clear, UP is not claiming that all end-to-end transactions harm shippers or that the Board needs to abandon long-standing precedent. As Professor Salop explains, economic modeling shows that outcomes depend on a variety of factors affecting the incentives of market participants. The Board should merely adopt modern antitrust enforcement's more tailored

[13] *See* APP Vol. 2 at 19, Majure VS ¶ 24.

[14] *See* Salop VS ¶¶ 36–39 (imperfect information); *id.*, ¶¶ 40–59 (differentiated products).

[15] *See id.*, ¶¶ 39, 43.

approach to evaluating vertical mergers—and the suitability of a presumption—on the particular facts of the transaction.

Data Regarding KCS's Acquisition of KCSM Do Not Support Applicants' Arguments. Dr. Majure also tries to dismiss concerns about competition at gateways by reviewing KCS, UP, and BNSF shares of traffic that KCSM moved north to the Laredo Gateway from Mexico in 2019.[16] According to Dr. Majure, the share data show that no gateway-related harm resulted from KCS's acquisition of Tex Mex and KCSM's predecessor, TFM, S.A. de C.V.[17] But, as Professor Salop explains, Dr. Majure's analysis is uninformative because it fails to address the central question in any such antitrust analysis: what the traffic shares would have been but for the KCS-TM-TFM transaction.[18] In fact, KCS's share of Laredo Gateway traffic increased significantly after the transaction—a result that is at least as consistent with anticompetitive foreclosure as with any procompetitive explanation.[19] Moreover, had Dr. Majure reviewed KCS, UP, and BNSF shares of traffic that KCS moved *south* to the Laredo Gateway from the United States, he would have observed that the vast majority of traffic he classifies as "competitive" moved on KCS.[20]

Notably, in the KCS-TM-TFM transaction, KCS projected minimal diversions of cross-border traffic from UP.[21] By contrast, Applicants here project substantial diversions of cross-

[16] *See* APP Vol. 2 at 22–24, Majure VS ¶¶ 30–31.

[17] *See Kansas City S.—Control—The Kansas City S. Ry., et al.* ("*KCS/Tex Mex*"), FD 34342 (STB served Nov. 29, 2004).

[18] *See, e.g.*, Salop VS ¶ 89.

[19] *See id.*, ¶ 90.

[20] *See id.*, ¶¶ 94–96.

[21] *See KCS/Tex Mex*, FD 34342, Railroad Control Application (KCS-3/TM-3) at 122 (May 14, 2003); *see also KCS/Tex Mex*, FD 34342, slip op. at 11.

border traffic for which UP and CP compete within the United States. That is further indication that CPKC would have much stronger incentives to foreclose competition at the Laredo Gateway than the applicants in KCS-TM-TFM.

The CP/KCS Application Raises a Series of Red Flags. Applicants project that their transaction will produce $1 billion annually in quantifiable benefits through a combination of revenue gains and cost savings by 2025.[22] The projected costs savings are modest, amounting to approximately 3.1% of CP's and KCS's combined pre-merger operating costs.[23] Most of the savings are not even merger-related: they reflect plans to apply CP's version of "precision scheduled railroading" to KCS and KCSM.[24]

Applicants' benefits projection relies primarily on aggressive assumptions that CPKC will (i) divert existing U.S.-Mexico traffic interchanged by KCSM and UP, or KCS and BNSF, to CPKC single-line routes, and (ii) grow U.S.-Mexico traffic that would move on the former-KCS north of Laredo using hundreds of miles of trackage rights over UP-owned lines that are already at capacity. Their plans to grow traffic are highly speculative. This leaves diversion of existing U.S.-Mexico traffic as a critical source of their projected revenue growth. However, Applicants provide no plan to compete for this traffic on the merits. They do not claim their transaction will create faster, more efficient routes than UP and BNSF provide today. In fact, CPKC's route between Laredo and Chicago will be far less efficient than UP's and BNSF's

[22] *See* APP Vol. 1 at 351, Vargas VS ¶ 41 & Table 2.

[23] *See* Haley VS ¶ 14.

[24] *See id.*, ¶¶ 18–31.

route.[25] Applicants do not promise to reduce rates to attract this traffic. To the contrary, their own revenue projections require them to capture interline traffic at existing revenue levels.[26]

In short, Applicants would be under tremendous pressure to divert this traffic without competing harder to attract the business. How would they do it? Their only path would be to restrain competition and divert traffic without competing on the merits.

Applicants acknowledge the validity of concerns about the CP/KCS transaction's effects on shippers' competitive options at gateways. {

}[27]

To address these significant concerns, Applicants offer only a vague commitment to keep the Laredo Gateway "and other affected gateways open both physically and commercially."[28] They promise to provide shippers rates to gateways that are "commercially reasonable."[29] However, they do not present any concrete, enforceable proposal for defining "commercially reasonable." Instead, they say rates would be commercially reasonable "in the sense that they would be established by CPKC in good faith."[30]

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[25] *See id.*, ¶¶ 53–59.

[26] *See id.*, ¶ 54; *see also* APP Vol. 2 at 133, Brown/Zebrowski VS ¶ 32 (assuming rate reductions averaging five percent only when diverting traffic from existing single-line service).

[27] Ex. 2 (CP Letter to National Industrial Transportation League (CP-C-00000851–854 at 852)). Material within single braces ("{ }") has been designated "Confidential" under the Protective Order in this proceeding. Material within double braces ("{{ }}") has been designated "Highly Confidential." Confidential and Highly Confidential materials have been redacted from the public version of this filing.

[28] APP Vol. 1 at 20–21, Application at 11–12.

[29] APP Vol. 1 at 233, Brooks VS ¶ 46.

[30] Ex. 3 (KCS and CP's Joint Responses and Objections to UP's First Set of Discovery Requests, Response to Request No. 40).

If the Board does authorize the transaction, shippers should not have to rely on CPKC's "good faith." The Board should impose conditions to prevent the reduction of competitive options at gateways, particularly the Laredo Gateway.

First, the Board should impose a concrete, enforceable standard requiring CPKC to establish gateway rates that are "commercially reasonable." UP has identified an appropriately concrete and enforceable approach: When a customer asks CPKC to provide rates for (i) CPKC service for only former-CP, former-KCS, and/or former-KCSM portions of an origin-to-destination route, and (ii) CPKC single-line service on a competitive route, CPKC must provide the customer with a Rule 11 rate for the former-CP, former-KCS, or former-KCSM portions that reflects a mileage-based prorate of the CPKC single-line rate.[31]

As discussed in Part VII, UP's proposed condition is a narrowly tailored remedy designed to ameliorate harmful effects of the transaction by protecting competition, not competitors. It places control in the hands of the shippers that the condition is intended to protect.

Second, the Board should require Applicants to abide by the commitments KCS made when it acquired Tex Mex to protect operations involving the Laredo Gateway and Laredo Bridge. These commitments (as applied to CPKC) include:

- CPKC will not change the basic structure and operations of KCSM except through negotiations. CPKC's carriers (including KCSM) will continue to cooperate closely and fairly with UP, BNSF and other rail carriers on interline services such as pre-blocking rail cars, improving automated customs pre-clearance procedures, supplying cars for shipments, accommodating run-through train service, providing excellent service, and promptly quoting rates.

[31] "Rule 11" rates apply to interline shipments where railroads do not establish "through pricing" or "through rates." The rule means each carrier in the route bills the customer separately for its portion of the movement. Rule 11 rates are often used to protect confidential prices.

- CPKC will honor the terms of all existing Tex Mex and KCSM agreements and will allow such agreements to continue to their full term and not seek to cancel them early, even if it has the legal right to do so.

- CPKC will treat all carriers fairly at the Laredo Bridge. CPKC will abide by the existing dispatching and operating practices over the Bridge, will not make any unilateral changes in the way the Bridge is dispatched and operated, and KCS, Tex Mex, and KCSM will continue to be bound by the contracts and agreements that now govern operations over the Bridge.

- CPKC will ensure safety remains a top priority with regard to CPKC operations at the Laredo Gateway.[32]

The Board also should make one aspect of these commitments more concrete: UP's right to access any new railroad bridge constructed by CPKC in Laredo on the same terms as its right to access the existing International Bridge. These narrowly tailored operational conditions are discussed in more detail in Part VII.

B. The Public Interest Requires CPKC to Bear the Costs of New Capacity Necessary to Implement the Proposed Transaction.

The conditions described above would help mitigate competitive harms that would arise from the proposed transaction, but they would not be enough to ensure the transaction is in the public interest. As part of their overall effort to show their transaction would be in the public interest, Applicants identified "the additional infrastructure needs required to support anticipated traffic growth" on CPKC lines "to ensure that the trains on these lines would operate fluidly."[33] They outlined specific plans for investing in new capacity and described the investments as "among the highest priorities on the combined CPKC system."[34] However, Applicants failed entirely to address the impact of their transaction on infrastructure that they use but that is owned by other railroads. The Application contains no analysis, no plans, and no promises to add

[32] *See KCS/Tex Mex*, FD 34342, slip op. at 13–14; *id.* at 18–19.

[33] APP Vol. 2 at 340, OP Plan ¶ 238.

[34] *Id.* at 344, OP Plan ¶ 244.

capacity to ensure operations on the lines owned by other carriers would remain fluid while supporting Applicants' planned traffic growth.

Most significantly, Applicants failed to address the need for additional infrastructure and investment to accommodate the additional eight to twelve trains per day they plan to operate on UP-owned tracks between Robstown and Beaumont, Texas, including lines through the crowded Houston terminal. BNSF also operates its own trains on many of these lines. Amtrak also operates on UP's lines between Beaumont and Houston. Applicants also failed to address other railroads' operations in analyzing the investment needs on lines they own but share with other railroads. They did not account for UP, BNSF, and Amtrak operations over the Neches River Bridge, a chokepoint for traffic moving between Houston and New Orleans. They also failed to address whether the 42-mile joint facility that UP and CP use to access Kansas City could accommodate their planned traffic growth of 14 trains per day. They also failed to address the impacts of their plan to route additional traffic through St. Paul, Minnesota, where their operations overlap with the operations of UP, BNSF, and Amtrak.

Applicants might dispute how much new capacity would be necessary to accommodate their planned operations on shared facilities, but no one should dispute the basic principle that Applicants should not make others subsidize investments needed to implement their transaction. If the Board allows the proposed transaction to proceed despite Applicants' failure to identify all the investments necessary to accommodate their plans, it should not allow Applicants to increase their operations above pre-merger levels until they enter into agreements with other affected railroads that identify and provide for funding of investments in new capacity necessary to accommodate their planned traffic growth.

II. A Combination Of CP And KCS Would Likely Cause A Substantial Lessening Of Competition For Traffic Moving Via The Laredo Gateway And Other Gateways.

CP proposes to acquire the KCS rail network, which extends in a north-south corridor from Kansas City south to the Pacific Ocean at the Port of Lázaro Cárdenas. In Mexico, KCS conducts operations through KCSM. KCS and KCSM connect at the Laredo Gateway, where KCSM also connects to UP.

The Board's charge in this proceeding is to determine whether the proposed combination of CP and KCS is "'consistent with the public interest.'"[35] "In determining the public interest," the Board "balance[s] the benefits of the merger against any harm to competition, essential service(s), labor, and the environment that cannot be mitigated by conditions."[36]

Since the early 2000s, the Board has recognized that one crucial harm to competition that must be addressed is the commercial or physical closure of major existing gateways. The Board's current rules for major rail consolidations require applicants to "explain how they would preserve the use of major existing gateways."[37] When the Board adopted the rules in 2001, it said that applicants must "present an effective plan to keep open major existing gateways," and that it would "impose conditions on any transaction that [it] approve[s] to ensure that result."[38] While CP and KCS obtained a waiver from the current rules, Applicants acknowledged that the Board's policy of keeping gateways open predates the current rules, and that the Board has "ample

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[35] *Canadian Nat'l Ry.—Control—Ill. Cent. Corp.*, 4 S.T.B. 122, 139 (1999) (quoting *Missouri-Kansas-Texas R. Co. v. United States*, 632 F.2d 392, 395 (5th Cir. 1980)).

[36] *Id.*

[37] 49 C.F.R. § 1180.6(b)(10)(i); *see also Major Rail Consolidation Procedures*, 5 S.T.B. 539, 546–47 (2001) ("Applicants also will be expected to include . . . effective plans to keep open major existing gateways.").

[38] *Major Rail Consolidation Procedures*, 5 S.T.B. at 563.

conditioning power under the pre-2001 rules" to impose conditions requiring them to keep gateways open physically and commercially.[39]

CP has previously recognized the need in railroad merger cases to protect competition at gateways, particularly the Laredo Gateway. When KCS proposed to acquire Tex Mex and TFM to create a "NAFTA Rail" system, CP actively urged the Board to protect against the commercial closure of the Laredo Gateway. It told the Board that "the Laredo gateway plays an indispensable role in the movement of rail freight to and from Mexico."[40] It echoed the Board's statements that Laredo "'occupie[s] *a position of separate and surpassing economic significance*' among the rail gateways serving the U.S.-Mexico border."[41] And CP criticized KCS's and Tex Mex's "vague[] assert[ions] that they would 'keep the Laredo gateway open on commercially reasonable terms'" as insufficient because the applicants had "*not* committed on the record to any *specific measures* to assure that result."[42]

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[39] *Canadian Pac. Ry.—Control—Kan. City S.*, FD 36500, Applicants' Reply to Objections to KCS Waiver from 2001 Major Merger Rules (CP-8/KCS-8) at 22 (Apr. 12, 2021).

[40] Ex. 4 (CP Additional Comments in *KCS/Tex Mex* (CPR-5) at 2 (Sept. 30, 2004)).

[41] *Id.* (quoting *UP/SP*, 1 S.T.B. at 422) (emphasis in CP's original filing).

[42] *Id.* (first emphasis in original). CP also recognized that KCS's settlement agreement with the National Industrial Transportation League (NITL)—which Applicants rely upon here, *see* APP Vol. 1 at 238–42, Brooks VS, Ex. 1—"does not mitigate the potential for competitive harm," because it does "'not require NAFTA Rail to establish and maintain commercially reasonable contract or common carrier rates and charges with respect to traffic interchanged between UP and TFM at the Laredo Gateway.'" Ex. 4 (CP Additional Comments at 6 (quoting NITL-4/KCS-17, Letter to David Meyer dated Aug. 18, 2003) (emphasis omitted)).

As CP explained: "The KCS-NITL settlement applies *only* to U.S.-Mexico cross-border movements in which KCS and/or TexMex are the participating carriers, and preserves interline competition only at interchange points *other than Laredo*. The KCS-NITL Agreement does *not* address the ability of non-Applicant railroads to access the Laredo gateway on commercially reasonable terms following the creation of a 'NAFTA Rail' system . . . ." *Id.*

Here, Applicants fail their own test: they have "*not* committed on the record to any specific measures to assure" rivals' access to the Laredo Gateway.[43] Indeed, they acknowledge the insufficiency of their own vague assertions about keeping gateways open "on commercially reasonable terms."[44] Relying on Applicants' vague promises is far riskier than in the KCS/Tex Mex transaction. As explained below, the potential for anticompetitive harm is great, particularly at the Laredo Gateway. Applicants will have the ability and incentive to divert traffic from interline routes to CPKC routes not on the merits, but by raising rates and degrading service for shippers seeking competitive alternatives to CPKC.

A. The Laredo Gateway Is Vitally Important to U.S.-Mexico Rail Transportation and the Proposed Combination of CP and KCS.

The Board should be concerned about the proposed transaction's impact on competition via all gateways potentially affected by a combination of CP and KCS, but no gateway is more important to competition in the United States, or more likely to be affected by the proposed transaction, than the Laredo Gateway.

1. The Laredo Gateway Is Critical to Applicants' Plans.

Applicants talk grandly about "the potential for a CP/KCS combination to transform North American railroading."[45] But their plans depend entirely on their ability to capture existing and new traffic that KCSM and UP could otherwise interchange at the Laredo Gateway (or that KCS and BNSF could interchange at Robstown, just north of the Laredo Gateway). Applicants'

[43] Ex. 4 (CP Additional Comments at 2).

[44] *See* APP Vol. 1 at 233, Brooks VS ¶ 47 (committing to "work with shippers to find ways to make these commitments more concrete and readily enforceable").

[45] APP Vol. 1 at 159, Creel VS ¶ 11.

projection of a $1.15 billion annual revenue increase from traffic gains by 2025[46] assumes that CPKC will capture {{ }} carloads and containers of existing and new rail business, of which approximately {{ }} or {{ }} would move between the United States and Mexico via the Laredo Gateway.[47] Handling all this new traffic would require CPKC to increase the average number of trains currently moving over KCS's Laredo Subdivision from 10 per day to 20 per day.[48] CPKC would have a strong incentive to meet its aggressive projections by using commercial and operational control of KCSM to foreclose competition from UP.

2. The Board Has Recognized the Need to Protect Rail Competition Via the Laredo Gateway.

In the 1996 *UP/SP* merger proceeding, the Board concluded that the Laredo Gateway was "the most important U.S.-Mexican rail gateway,"[49] occupying a position of "separate and surpassing economic significance" in U.S.-Mexico commerce.[50] To ensure there would be no reduction in competition for traffic moving via the Laredo Gateway, the Board granted Tex Mex trackage rights over UP's lines between Robstown and Corpus Christi, Texas, on the one hand, and a connection with KCS in Beaumont, Texas, on the other hand.[51] Applicants would rely on

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[46] *See* APP Vol. 1 at 351, Vargas VS ¶ 41, Table 2.

[47] *See* Haley VS ¶ 42 (citing Operating Plan workpaper "HC - 1.Proposed Final FTI Rail to Rail Diversions for Merger Application_matching Finance with Truck to Rail.xlsx").

[48] *Compare* APP Vol. 2 at 452, OP Plan, App. N at 1, *with id.* at 454, OP Plan, App. O at 1.

[49] *UP/SP*, 1 S.T.B. at 422.

[50] *Id*. The Board said Laredo's status as "the principal rail gateway between the United States and Mexico" is "due to its superior infrastructure, especially customs inspection facilities, and its location on the shortest route between many U.S. and Mexican origins and destinations." *Id.* at 410.

[51] *See id.* at 424 (justifying grant of trackage rights "to ensure the continuation of an effective competitive alternative to UP's routing into the border crossing at Laredo"); *see also UP/SP*, *Houston Gulf/Coast Oversight*, Decision No. 10, slip op. at 9 (STB served Dec. 21, 1998) (noting that Tex Mex's trackage rights over UP "were designed to address the potential loss of competition at Laredo").

those rights to implement their proposed transaction: without the rights, CPKC could not move traffic between the Laredo Gateway and KCS's connection with CP in Kansas City.[52]

In 2004, the Board considered whether conditions were needed to protect competition via the Laredo Gateway in the context of KCS's merger with Tex Mex. The Board did not believe a merged KCS and Tex Mex could raise rates or foreclose competition by UP or BNSF via Laredo. Nonetheless, the Board found the "Laredo Bridge and gateway are so significant to rail traffic between the U.S. and Mexico" that it imposed a condition requiring KCS to adhere to a series of pledges to "guarantee that traffic will continue to flow fairly and efficiently at the Laredo Bridge and through the Laredo gateway."[53] The pledges included KCS's commitment to "establish and maintain commercially reasonable rates over any existing interchange with any railroad."[54]

CP's combination with KCS presents different and greater risks to competition via the Laredo Gateway than KCS's merger with Tex Mex. And the Laredo Gateway continues to play an irreplaceable role for traffic moving between the United States and Mexico.

3. The Laredo Gateway Remains Critical to U.S.-Mexico Rail Transportation.

The Laredo Gateway remains by far the most important rail gateway between the United States and Mexico. Approximately 54% of all U.S.-Mexico rail traffic (by dollar value) crosses the border at Laredo.[55] The Laredo Gateway's share of total U.S.-Mexico rail traffic understates

[52] KCS relies on trackage rights over UP between Corpus Christi/Robstown and Victoria, Texas, and between Rosenberg, Texas, and Beaumont. Between Victoria and Rosenberg, KCS operates on a line that UP sold Tex Mex in 2000. *See Texas Mexican Ry.—Purchase Exemption—Union Pac. R.R.*, FD 33914 (STB served Dec. 11, 2000).

[53] *KCS/Tex Mex*, FD 34342, slip op. at 19 (emphasis added).

[54] *Id.*

[55] *See* Rocker/Turner VS at 4–5.

its importance. Basic geography makes the three rail gateways in western Mexico—Calexico, El Paso, and Nogales—non-viable alternatives to Laredo for most rail traffic flowing between the central and eastern United States (and Canada) and the most populous and industrialized regions of Mexico. Those gateways generally handle traffic moving between the western United States and points in western Mexico.[56]

Of the three rail gateways in Eastern Mexico—Laredo, Eagle Pass/Piedras Negras, and Brownsville/Matamoros—the Laredo Gateway's share is the largest. In 2019, Laredo handled over 66% of total rail traffic (by dollar value).[57] The principal alternative to Laredo is Eagle Pass/Piedras Negras, where UP and BNSF connect with Ferromex ("FXE").[58]

The Laredo Gateway remains critical to UP and its customers. UP was never willing to rely on KCS's vague commitment to keep the Laredo Gateway open "on commercially reasonable terms." Over time, UP has worked with FXE to make the Eagle Pass Gateway a more attractive alternative for customers, in an effort to reduce reliance on KCS and the Laredo Gateway. UP has an additional incentive to encourage customers to route traffic via Eagle Pass whenever feasible: UP owns a 26% equity interest in FXE. Despite UP's strong incentives, the Laredo Gateway's share of UP traffic moving via the Laredo or Eagle Pass gateways in 2019 was 57%.[59]

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[56] *See id.* at 5.

[57] *See id.*

[58] *See id.* Brownsville/Matamoros is used principally for traffic moving between the United States and Mexican points just across the border from Brownsville, and for routing of empties to relieve congestion at Laredo. *See id.*

[59] *See id.* at 6.

In addition, focusing on aggregate cross-border traffic flows understates the importance of the Laredo Gateway. For example, for the business CPKC is most focused on diverting—*i.e.*, finished vehicles, auto parts, and intermodal—the Laredo Gateway's share of UP traffic moving via the Laredo and Eagle Pass gateways is approximately 62%.[60] For traffic moving between the Upper Midwest and Mexican states in the industrialized heartland of northeastern and central Mexico, Laredo's share of UP cross-border traffic in many cases exceeds 95%.[61]

The Laredo Gateway's critical role in cross-border rail transportation stems in large part from the fact that it provides the only efficient connection with KCSM. Many shippers of cross-border traffic have no choice but to continue routing substantial volumes of traffic via Laredo because there are significant flows for which FXE service via Eagle Pass cannot provide an efficient alternative to KCSM service via Laredo. KCSM has two main advantages over FXE:

First, KCSM serves many important points in Mexico exclusively, including Toluca, San Luis Potosí, and many locations in Nuevo Leon. Of the more than 300,000 cars and containers UP interchanged with KCSM in 2019, UP estimates that more than half moved between Laredo and locations served exclusively by KCSM.[62] The overwhelming majority of the exclusively-served traffic is the finished vehicle, auto parts, and intermodal business that CPKC is most focused on targeting for diversion.[63]

Second, KCSM often has significant routing advantages for cross-border traffic, even when shippers have access to both KCSM and FXE. For example, KCSM and FXE both can

[60] *See id*.

[61] *See id*.

[62] *See id.* at 7.

[63] *See id*.

access shippers in the Valle de Mexico region surrounding Mexico City through a jointly owned railroad, Ferrocarril y Terminal del Valle de México. But FXE's route from the Mexico City area to Eagle Pass is 55% (392 miles) longer than KCSM's route to Laredo.[64] Nearly 80% of UP's traffic between the U.S. and the Mexico City area moves via the Laredo Gateway.[65]

B. CP Control of KCS Would Undermine Competition Via the Laredo Gateway.

In *UP/SP* and *KCS/Tex Mex*, the Board acted to preserve effective competition for cross-border traffic moving via the Laredo Gateway. CP's proposal to acquire control of KCS requires the Board to act once again to protect the interests of shippers who depend on rail service via the Laredo Gateway. Applicants have acknowledged the validity of concerns that their transaction will harm shippers' competitive options at gateways. Those concerns are particularly justified with regard to harms to competitive options at the Laredo Gateway.

1. Shippers Benefit from Competition at the Laredo Gateway.

Today, most shippers that depend on rail service via the Laredo Gateway have at least two competitive options for moving cross-border traffic within the United States. UP and BNSF compete to provide service between the border area and common points throughout the western two-thirds of the United States, and they have efficient connections to carriers serving shippers in the Eastern United States and Canada.[66] In some cases, shippers have the option to use KCS's

[64] *See id*. FXE's concession from the Mexican government includes trackage rights over KCSM's line between Ramos Arizpe and Querétaro, which would provide FXE a more efficient route to Eagle Pass. However, FXE cannot use the rights for cross-border traffic. *See* OECD, International Transport Forum, Freight Railway Development in Mexico at 25 (April 2014), https://www.itf-oecd.org/sites/default/files/docs/14mexicorail.pdf

[65] *See* Rocker/Turner VS at 7.

[66] *See id.* at 9.

network in the United States. Often, KCS's only participation in a cross-border movement in the United States will be to move traffic between Laredo and an interchange with BNSF.

When UP and BNSF compete, each relies on KCSM to handle the traffic between the border and points in Mexico. With regard to operational matters, KCSM and UP have a good working relationship. Between KCSM's Sanchez Yard, located just south of the border, and points in Mexico, traffic KCSM interchanges with UP typically moves in the same trains as traffic KCSM interchanges to KCS for BNSF. The use of the same trains for both railroads' traffic helps ensure UP traffic is handled in an equitable, even-handed manner by KCSM.[67] More generally, KCSM has strong incentives to cooperate with UP on operational matters because a substantial portion of its cross-border business depends on its ability to provide efficient service in Mexico for traffic UP originates or terminates in the United States.[68]

With regard to commercial matters, shippers benefit from competition created by the confidential nature of most pricing for cross-border traffic. Most of UP's cross-border traffic moves under "Rule 11" rates.[69] When a shipper requests a Rule 11 rate, each carrier participating in an interline route separately and confidentially provides the shipper a rate for its portion of the route. In other words, a shipper asks KCSM for a rate to move traffic between a point in Mexico and the border, and it asks UP and BNSF to provide competing rates to move the traffic between the border and a point in the United States. UP and BNSF compete to provide transportation in the United States with regard to the rates they offer the shipper and on non-price dimensions as

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[67] *See id.*

[68] *See id.*; *see also* Ex. 5 (Ottensmeyer Tr. 140:8–141:4 {

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[69] *See* Rocker/Turner VS at 9.

well (*e.g.*, transit time, equipment supply, reliability).[70] KCSM's rates are constrained by its concerns that the combined price might exceed what the customer is willing to pay.[71]

UP believes that not all shippers experience the same benefit from competition at the Laredo Gateway that they experienced before KCS acquired Tex Mex and KCSM. In particular, UP is concerned that KCSM sets Rule 11 rates to discourage shippers from using UP, and to extract extra revenue from shippers who use UP, when KCS has a single-line alternative. That is one reason UP has worked to improve the Eagle Pass Gateway. But UP's ability to offer alternative routes is limited by FXE's route structure and KCSM's exclusive access in Mexico.[72]

However, for most cross-border traffic that Applicants plan to divert from UP and BNSF, KCS cannot currently offer a viable alternative north of the border. KCS's network extends only as far north as Kansas City—it does not reach Chicago and other origins and destinations in the Upper Midwest. CP's Chief Marketing Officer explains that CP and KCS had tried but failed to develop lasting interline relationships that would allow KCS to extend its cross-border hauls further into the United States.[73] As a result, KCS's incentive has been to create a competitive environment for most traffic moving via the Laredo Gateway to grow revenue on KCSM.

2. CPKC Would Have the Incentive and Ability to Use Its Control of KCSM to Deprive Shippers of the Price and Service Benefits of UP-KCSM Routings.

CPKC's incentives to skew the competitive playing field at the Laredo Gateway would be vastly different from KCS's incentives today. By combining KCS's routes between Mexico

[70] *See id.* at 10.

[71] *See id.*

[72] *See id.* at 6–7, 16.

[73] *See* APP Vol. 1 at 226–28, Brooks VS ¶¶ 28–34. KCS's Chief Executive Officer also describes KCS's unsuccessful efforts to extend its reach through alliances with other railroads. *See* APP Vol. 1 at 198, Ottensmeyer VS at 12.

and Kansas City with CP's routes between Kansas City and the Upper Midwest, CPKC would have the opportunity to generate hundreds of millions of dollars of additional revenue by carrying north of the border the several hundred thousand carloads and containers of traffic that KCSM currently interchanges with UP and BNSF via the Laredo Gateway. Applicants are specifically targeting more than {{ }} containers of intermodal freight, more than {{ }} carloads of automotive business, and thousands of carloads of metals, minerals, consumer products, chemicals, energy, and grain products that moved between the U.S. and Mexico via the Laredo Gateway in 2019.[74]

CPKC would have a significant incentive to manipulate competitive outcomes for cross-border traffic to favor routes in which it participates in the United States. When KCS acquired Tex Mex and TFM, KCS faced no pressure to divert UP-KCSM traffic moving over the Laredo Gateway: it projected essentially no diversions of cross-border traffic from UP to KCS.[75] By contrast, Applicants here have promised investors a $1.15 billion annual revenue increase from traffic gains by 2025.[76] To meet these aggressive projections, Applicants' plans require CPKC to capture more than {{ }} carloads and containers of existing and new business, of which more than {{ }} or approximately{{ }} would be traffic moving between the United States and Mexico via the Laredo Gateway.[77] KCS's public disclosures emphasize the truly aggressive nature of the projections. KCS's proxy statement urging shareholders to approve the

[74] *See* Salop VS ¶ 76, Fig. 3.

[75] *See KCS/Tex Mex*, FD 34342, Railroad Control Application (KCS-3/TM-3) at 122; *see also KCS/Tex Mex*, FD 34342, slip op. at 11.

[76] *See* APP Vol. 1 at 351, Vargas VS ¶ 41, Table 2.

[77] *See* Haley VS ¶ 42 (citing Operating Plan workpaper "HC - 1.Proposed Final FTI Rail to Rail Diversions for Merger Application_matching Finance with Truck to Rail.xlsx").

proposed transaction, which was filed November 3, 2021—that is, *after* the Application had been submitted to the Board—shows CP projected annualized synergies for the combined companies of approximately $990 million would be realized within the first three years after the transaction, while KCS management projected just $377 million in annualized synergies.[78]

If the proposed transaction enabled the merged CPKC to attract Laredo Gateway traffic to its lines north of Laredo solely by reducing rates or improving service, the effect would be procompetitive, not anticompetitive. UP might lose traffic, but shippers would not be harmed.

However, CP control of KCS poses a serious threat to the competitive process because it would likely undermine the transportation options available to shippers for traffic moving via the Laredo Gateway. Applicants have placed themselves in a difficult position. They promised the proposed transaction would generate significant merger-related benefits, but they are unlikely to achieve their objectives by competing for business on the merits.

CPKC would not generate significant merger benefits through cost savings. Applicants say the proposed transaction creates "tremendous opportunities for efficiency gains."[79] However, Applicants' actual projected operating cost savings are minimal, amounting to just 3.1% of CP's and KCS's current combined operating costs—a level of productivity improvement that railroads regularly achieve as part of their normal course of business.[80] Applicants have few opportunities to generate cost savings because the CP and KCS systems connect at just one location—Kansas City—where they already share a yard.[81] CPKC would not be able to offer shorter, more efficient

[78] *See* Ex. 6 (KCS Schedule 14A at 65 (Nov. 3, 2021)). KCS's Chief Executive Officer, Mr. Ottensmeyer, described the difference as { } Ex. 5 (Ottensmeyer Tr. 96:6–97:3).

[79] APP Vol. 2 at 283, OP Plan ¶ 76.

[80] *See* Haley VS ¶ 14.

[81] *See id.*, ¶¶ 15–16.

routes or reduce costs by combining terminals and facilities, other than headquarters facilities.[82] Applicants say CPKC would generate cost savings by optimizing train operations. But aside from eliminating interchange of a few cars in Kansas City, the "optimization" merely reflects CP's application of precision scheduled railroading ("PSR") principles to KCS and KCSM—a change that does not require a merger.[83]

Making Applicants' task even more daunting, CP apparently knows very little about railroad business in Mexico. CP's Chief Marketing Officer has never worked in Mexico, has never done sales in Mexico, and does not even know how much KCSM traffic is handled to or from locations exclusively served by KCSM. Before agreeing to merge, CP apparently never analyzed pricing opportunities in Mexico or performed any competitive analysis regarding traffic that could move between CP or KCS-served points and KCSM-served points in Mexico.[84]

Applicants describe aspirations to draw substantial quantities of new traffic to their combined system, anchored by vague plans to attract international intermodal traffic to the Port of Lázaro Cárdenas and expand shipments of DRUbit—a more concentrated form of crude oil. Of the {{ }} containers and carloads of traffic that Applicants identify in their "growth initiative," {{ }} is Lazaro intermodal traffic and {{ }} is DRUbit.[85] But the Lázaro Cárdenas project is entirely speculative. Applicants' documents produced in discovery show {{

[82] *See id.*, ¶¶ 15–16.

[83] *See id.*, ¶ 31.

[84] *See* Ex. 7 (Brooks Tr. 188:19–190:8).

[85] *See* Wahba/Naatz workpaper "Growth Initiative Calculations.xlsx."

}}[86] As for DRUbit, Applicants acknowledge CP and KCS were already cooperating to connect CP-served origins and KCS-served destinations to promote DRUbit.[87] They also appear to suggest DRUbit will merely displace crude oil already being moved by CP and interchanged with KCS or BNSF.[88] Either way, prospects for additional, merger-related growth are speculative.

Ultimately, Applicants' most credible prospect for merger-related traffic growth comes from traffic they plan to divert at the Laredo Gateway. However, Applicants offer no reason customers would willingly choose longer CPKC routes over existing interline routes. Applicants make clear they would not offer lower rates to attract traffic from interline routes—their revenue projections require them to divert interline traffic at existing rates.[89] If they reduced rates to attract traffic, they would break their $1 billion promise to investors. Applicants also do not have a realistic prospect of attracting traffic by offering better service than existing alternatives. On

[86] *See* Ex. 8 (Lazaro Cardenas Presentation (KCSR-C-00016306–16312, at 16312)); Ex. 9 (Lazaro Cross-Border Pricing Business Review (KCSR-HC-00017701–17707, at 11704)).

[87] *See* APP Vol. 1 at 284–86, Wahba/Naatz VS ¶¶ 90–92; *see also* Marybeth Luczak, USD, Gibson Launch "DRUBit by Rail," Railway Age (Dec. 15, 2021), https://www.railwayage.com/freight/class-i/usd-gibson-launch-drubit-by-rail/

[88] *See* APP Vol. 1 at 283, Wahba/Naatz VS ¶¶ 85–87. Applicants appear to take a contradictory position, first saying "[t]he volume of crude oil shipments from source to refinery is determined by macroeconomic forces that will not be affected by the Transaction," *id.* at 280, Wahba/Naatz VS ¶ 80, and suggesting DRUbit will merely substitute for existing moves already handled by CP and interchanged with KCS or BNSF, *id.* at 283, Wahba/Naatz VS ¶ 85, but then claiming significant additional volumes and revenues as part of their planned "growth initiative," *see* Wahba/Naatz workpaper "Growth Initiative Calculations.xlsx"; *see also* OP Plan workpaper "HC – 1.Proposed Final FTI Rail to Rail Diversion Results for Merger Application_matching Finance with Truck to Rail.xlsx."

[89] *See* Haley VS ¶ 54.

average, their routes would be 217 miles longer than existing options.[90] A very substantial portion of Applicants' planned diversions involve traffic moving between Laredo and Chicago, but their route in that important corridor is approximately {{ }} more circuitous, and thus less efficient, than the average existing route, according to their own calculation.[91]

In short, Applicants would face enormous post-merger pressure to divert traffic from existing KCSM interline service to CPKC single-line service using strategies that reduce shippers' existing competitive options. As explained below, CPKC would have the ability to implement such anticompetitive strategies by raising rates shippers must pay for interline service or degrading the quality of service shippers receive when using interline service.

a) CPKC Would Have the Ability to Raise Interline Rates on Cross-Border Traffic to Foreclose Competition.

CPKC could readily disable competition for cross-border rail traffic by raising the rates KCSM charges shippers for UP-KCSM movements. UP could have the most efficient routes and best service north of the border, but CPKC could make UP-KCSM interline service too expensive to overcome those advantages.[92]

As Mr. Rocker and Professor Salop explain, CPKC could foreclose competition from UP without refusing to offer shippers rates for UP-KCSM interline movements, and even without discriminating between UP and CPKC in the KCSM rates it offers. CPKC could accomplish its objective by raising KCSM's rate factor in relation to CPKC's rates north of the border, which Mexican law would allow.[93]

[90] *See* APP Vol. 2 at 132, Brown/Zebrowski VS ¶ 30, Table 6.

[91] *See* Haley VS ¶ 57.

[92] *See* Rocker/Turner VS at 12–14.

[93] *See id*. at 13; Salop VS ¶¶ 81–82; de la Calle VS at 4–5.

CPKC's anticompetitive strategy can be illustrated using a simple example: Assume that before CP gains control of KCS, KCSM quotes a shipper a rate of $100 from a Mexican origin to the Laredo Gateway. UP and CP serve the destination. UP has an efficient route and quotes a rate of $100. KCS and CP could move the traffic using a less efficient route through Kansas City, but the customer prefers the UP route, even if KCS and CP would jointly charge the same $100. In today's competitive market, the shipper would choose the KCSM-UP route and pay $200.

After the transaction, CPKC could raise KCSM's rate factor to $110—or even higher—while still offering the customer a single-line rate of $200. In other words, CPKC could easily disadvantage UP's efforts to compete for the traffic without lowering rates or improving service. The customer would have to choose between accepting CPKC service to avoid a rate increase or paying KCSM an additional $10 (or more) to continue using UP. Either way, CPKC would generate more revenue and more profit (assuming the CP/KCS joint rate of $100 included some return), and the shipper would lose the benefits of real competition—by paying more, by losing its preferred route north of the border, or by having to accept poorer service.[94]

CPKC could easily implement this strategy. Even today KCS and KCSM do not have separate rate-setting functions. "KCS has a core pricing team for all rates, US and Mexico. KCS and KCSM do not have separate pricing groups . . . ."[95] As Applicants explained in discovery, when KCS offers single-line service between Mexico and the United States, KCSM's revenue division is established *after* the overall rate has been determined. KCS and KCSM first set an overall price based "on a variety of factors and considerations." Then, "[o]nce the overall rate is

[94] *See* Rocker/Turner VS at 12–14.

[95] Ex. 10 (UP's Motion to Compel, Ex. C at 9).

determined, revenue divisions are assigned between KCSR and KCSM."[96] In other words, the strategy would not require any additional coordination. CPKC could maintain the veneer of charging non-discriminatory KCSM rates in Mexico, while structuring KCSM-UP and CPKC single-line rates it offers to foreclose competition from UP.

In addition, CPKC would have a great deal of latitude to manipulate KCSM's rates to foreclose competition from UP. There are no effective regulatory limits on the level of KCSM's rates for transportation within Mexico, as Dr. de la Calle explains.[97] CPKC could cause KCSM to increase its rates as much as necessary to assure that UP is effectively disabled from competing, while offsetting any increase in the single-line rates it offers shippers.

As Mr. Rocker and Professor Salop explain, CPKC's implementation of such a strategy would hurt shippers and competition, not just UP. In the example above, CPKC would not be shifting $10 from UP's pockets to CPKC's pockets. The shipper would be forced to choose between (i) receiving inferior service, and (ii) paying more to KCSM while paying the same amount to UP. Applicants claim KCSM already extracts every last dollar of revenue that might be available for cross-border moves.[98] However, they offer no proof.[99] They cannot offer any

[96] Ex. 11 (KCS and CP's Joint Responses and Objections to UP's Second Set of Discovery Requests, Response to Request No. 148).

[97] *See* de la Calle VS at 6.

[98] *See* APP Vol. 1 at 208, Ottensmeyer VS at 22 ("With respect to existing rail dependent movements, prices are already pushed to market levels.").

[99] Applicants acknowledged in discovery that their expert economist's claim that "KCS would already be collecting the full measure of returns associated with its existing market power" from shippers with "no ready alternative to KCS," APP Vol. 2 at 19, Majure VS ¶ 24, "was not based on any specific documentary evidence in the possession of Applicants." Ex. 12 (KCS and CP's Supplemental Joint Responses and Objections to CSXT's Second Set of Discovery Requests, Response to Interrog. No. 12). When asked for documents discussing whether KCS or KCSM was collecting the full measure of returns associated with its existing market power, Applicants responded: "KCS does not have any responsive documents." Ex. 3 (KCS and CP's Joint

proof because their claim is incorrect. As Professor Salop explains, KCS/KCSM's lack of full information about CP's and UP's costs and pricing and its incomplete knowledge about the particular circumstances and demand factors facing CP's and UP's customers in the United States reduces KCS/KCSM's ability to effectively discriminate among customers on their cross-border movements. The CP/KCS transaction would give CPKC full control of costs and pricing of its single-line route and additional insight into customer circumstances that would allow the combined entity to increase its profits at the expense of shippers—if CPKC is given the opportunity to foreclose competition.[100]

A CPKC pricing strategy that expressly treats KCSM-UP movements differently from CPKC single-line movements would be even easier to implement. As Dr. de la Calle observes, it is unclear whether Mexican anti-discrimination law would even regard a difference between the portion of a CPKC single-line rate allocated to KCSM and the KCSM factor in a KCSM-UP interline rate as a prohibited "discrimination."[101] Even today, KCS's interpretation of Mexican antidiscrimination rules {{

}}[102] CPKC would have incentives to take an even more aggressive legal position to meet its revenue projections.

Responses and Objections to UP's First Set of Discovery Requests, Response to Request No. 99).

[100] *See e.g.*, Salop VS ¶¶ 60–61.

[101] *See* de la Calle VS at 5–9.

[102] *See* Ex. 13 (KCS Policy on Rate Offers for KCSM Routes (KCSR-HC-00020720–20726)).

b) CPKC Would Have the Ability to Reduce KCSM Cooperation with UP on Operational and Service Matters in Mexico and at the Laredo Gateway.

CP control of KCS would also provide opportunities to divert cross-border traffic by making UP-KCSM transportation offerings more costly or less attractive in other ways. Today's competitive UP-KCSM service is built on and continues to depend on cooperation between the carriers on a wide variety of operational matters.[103] However, CPKC's incentive to cooperate with UP would be different from KCSM's incentives. Although Applicants claim "cooperating with UP at Laredo . . . will be in the self-interest of the CP/KCS system,"[104] their Application makes clear their interests would lie in diverting traffic from UP-KCSM service to CPKC service.

Applicants' incentives to reduce operational cooperation with UP would grow along with any growth of their business in Mexico. KCSM currently has strong incentives to provide excellent service to UP to expand its overall business, and the incentives are reinforced by the fact that UP traffic often moves on the same trains as other KCSM traffic.[105] If Applicants' plans come to fruition, CPKC would have more trains carrying only CPKC traffic, more customers receiving service from only CPKC, and thus reduced incentives to provide equal treatment for customers choosing UP service north of the Laredo Gateway. The result would be a downward spiral in which the reduction in the quality of service provided to UP-served shippers in Mexico would force shippers to move their business to CPKC, which in turn would lead to further reductions in the quality of service provided to UP-served shippers.

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[103] *See* Rocker/Turner VS at 9, 14.

[104] APP Vol. 1 at 232, Brooks VS ¶ 43.

[105] *See* Rocker/Turner VS at 9–10, 15.

CPKC could also reduce competition by giving preferential treatment to its own traffic moving over the International Bridge at Laredo. KCS controls the bridge through its ownership of Tex Mex and KCSM. Operations over the bridge are governed by a 1951 agreement between Tex Mex and a UP predecessor, but the agreement speaks only in general terms about Tex Mex's obligations to perform service "impartially" with "no preference . . . to movements of cars by one of the parties."[106] UP and KCS have given meaning to the agreement by setting aside alternating "windows" for northbound and southbound traffic.[107] However, Applicants have indicated they may want to change the current process.[108] Any change to operations that would permit a more subjective interpretation of Tex Mex's contractual obligation would give CPKC opportunities to restrict UP's use of the bridge in ways that would harm customers of UP.

In addition, UP and KCSM have worked together over the years to increase the effective capacity of the existing bridge. Recently, KCS obtained a Presidential Permit to construct a new rail bridge at Laredo.[109] KCS currently has strong incentives to cooperate to ensure the existing bridge has sufficient capacity to accommodate both parties' future needs. If CPKC could shift operations to a new bridge, while excluding UP and maintaining control of the existing bridge, CPKC could act on its incentive to confine UP's future ability to compete for cross-border transportation at Laredo.

[106] Rocker/Turner workpaper "C - International Bridge Agreement.pdf."

[107] *See* Rocker/Turner VS at 15.

[108] *See* APP Vol. 2 at 317, OP Plan ¶ 162 (discussing goal to "[e]volve the operational model at the border").

[109] *See* Rocker/Turner workpaper "P - Presidential Permit.pdf."

III. The Board Should Not Simply Presume That The Proposed Transaction Would Not Have Anticompetitive Effects.

Applicants dismiss concerns regarding CPKC's enhanced ability and incentive to foreclose competition. In lieu of any probative analysis to support their claim that their transaction will not harm competition, they rely heavily on the "one-lump" theory to presume that CPKC will have no incentive to force inferior terms on customers who depend on KCSM service in Mexico and ship traffic from Laredo to points served by both CP and UP (or CP and BNSF). That theory, which the Board has utilized at times in reviews of other mergers, in turn rests on the assumption that KCS must already be collecting the full measure of returns associated with KCSM's existing market power[110] and that merging with CP therefore cannot increase the post-merger firm's ability or incentive to foreclose.

While the one-lump theory may apply in some circumstances, it does not apply in this particular case. As Professor Salop explains, modern economic analysis has shown that when an upstream monopolist (KCSM) and downstream rivals (UP and CP) lack full information about each other's costs and prices, or when the rivals provide differentiated services—*i.e.*, services that shippers view as qualitatively different—the monopolist generally cannot extract the full "one lump," so the shipper retains a surplus.[111] In those circumstances, which exist here, the merged carrier *does* have an incentive to engage in anticompetitive conduct: to eliminate the shipper's surplus and extract the full "one lump."[112]

Applicants' expert Dr. Majure leans so heavily on the "one lump" presumption that, in Applicants' own words, his conclusion that "[a] combined CP/KCS would not be expected to

[110] *See* APP Vol. 2 at 19, Majure VS ¶ 24.

[111] *See* Salop VS ¶¶ 36–39 (imperfect information); *id.*, ¶¶ 40–59 (differentiated products).

[112] *See id.*

have any incentive to affect the competitive terms available to [a solely-served] shipper, because KCS would already be collecting the full measure of returns associated with its existing market power"[113] "was not based on any specific documentary evidence in the possession of Applicants."[114] In other words, Dr. Majure reviewed no documents or information from KCSM regarding how that railroad operates. He conducted no assessment of whether KCSM is obtaining its single monopoly profit today, which means that Applicants are asking the Board to rely on a presumption—that the post-merger firm will not have an increased incentive to use its control of Laredo to foreclose competition—that is based purely on an untested assumption.

To support the assertion that KCSM is not presently acting on its incentive to foreclose competition by exploiting its control of the Laredo bottleneck, Dr. Majure presents an analysis of a single-year, incomplete snapshot of data—the results of which are as consistent with the existence of some foreclosure as with none and are thus of no probative value whatsoever. And while Dr. Majure questions whether the post-merger firm will have the ability to foreclose by suggesting that shippers can turn to FXE as an alternative to KCSM in Mexico, he conducted no analysis to determine whether that hypothesis is correct.

Applicants' proposed merger also comes at a time of increasing concern regarding the potential competitive effects of vertical transactions. At the suggestion of the White House,[115]

[113] APP Vol. 2 at 19, Majure VS ¶ 24.

[114] Ex. 12 (KCS and CP's Supplemental Joint Responses and Objections to CSXT's Second Set of Discovery Requests, Response to Interrog. No. 12); *see also* APP Vol. 2 at 19, Majure VS ¶ 24.

[115] *See Biden Competition Order*, Sec. 5(c) ("To address the consolidation of industry in many markets across the economy, as described in section 1 of this order, the Attorney General and the Chair of the FTC are encouraged to review the horizontal and vertical merger guidelines and consider whether to revisit those guidelines.").

the antitrust enforcement agencies are currently revisiting their enforcement guidelines.[116] They have also recently challenged several vertical transactions on the theory that one party had market power and could use control of the other party to foreclose competition—enforcement actions that make no presumption the party with market power was already extracting its full "lump."[117] And the current version of their Vertical Merger Guidelines contains no presumption that certain vertical mergers are procompetitive or competitively neutral.

Applicants themselves acknowledge that concerns about foreclosure are valid.[118] Applicants have promised to address those concerns by providing shippers "commercially reasonable" rates to and from gateways.[119] However, while they also apparently recognize that their current commitments are neither sufficiently concrete nor readily enforceable,[120] their promises do not include any more concrete or enforceable provisions.

Applicants would thus have the Board rely on a flawed and unsupported presumption that their vertical merger cannot harm competition, at a time of increasing concern regarding the possible competitive effects of vertical mergers, with only Applicants' vague assurances as a backstop. UP proposes that if the Board is inclined to approve the transaction, it impose remedies—including an administrable, readily enforceable formula for developing competitively

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[116] *See* Press Release, U.S. Dep't of Just., *Justice Department Issues Statement on the Vertical Merger Guidelines* (Sept. 15, 2021); Press Release, F.T.C., *Federal Trade Commission Withdraws Vertical Merger Guidelines and Commentary* (Sept. 15, 2021).

[117] *See, e.g.*, Complaint, *Illumina, Inc.*, Docket No. 9401 (F.T.C. Mar. 30, 2021); Complaint, *Lockheed Martin Corp.*, Docket No. 9405 (Jan. 25, 2022); Complaint, *Nvidia Corp.*, Docket No. 9404 (F.T.C. Dec. 6, 2021).

[118] *See* Ex. 2 (CP Letter to National Industrial Transportation League) ({ }).

[119] APP Vol. 1 at 16, Application at 7; *see also* APP Vol. 1 at 214, 233, Brooks VS ¶¶ 4, 46.

[120] *See* APP Vol. 1 at 233, Brooks VS ¶ 47 ("Finally, we will work with shippers to find ways to make these commitments more concrete and readily enforceable, including via appropriate alternative dispute resolution mechanisms.").

reasonable interline rates—to prevent the anticompetitive foreclosure that might otherwise result from the proposed merger.

A. Professor Salop's Analysis Explains Why Reliance on the One-Lump Presumption Would be Inappropriate in This Case.

The Board has utilized the "one-lump" theory in previous cases to presume that end-to-end mergers with a monopolist in one segment and competition in the other segment will not cause competitive harm.[121] Put simply, the theory assumes the monopolist is already earning its "one lump" and that merging with a downstream company therefore cannot increase its incentive or ability to foreclose. The theory has its roots in the "single monopoly profit" theory developed in the early industrial organization economics literature analyzing tying arrangements and then was applied to vertical mergers. As Professor Salop explains:

> [I]n this economic model applied to vertical mergers, one firm has a monopoly in producing an "input," while there is perfect competition among the competing firms, (*i.e.*, two or more firms with perfect information producing an undifferentiated (homogeneous) "output" that use the input and sell that output to consumers. According to this theory, the monopolist would not need to acquire one or both of the competitors in the output market in order to be able to extract all of its input monopoly profits from consumers. That is, the acquisition does not change anything, absent efficiencies, because there is only "one lump" of profits that can be extracted by the monopolist, and it can do so either with or without the acquisition.[122]

Modern economic analysis has shown the one-lump presumption is appropriate only when certain conditions are present, including that the parties have perfect information about each other's prices and costs, and that the downstream competitors offer homogenous (i.e., identical) products. But, as Professor Salop explains, the monopolist is *not* presumed to be

[121] *See* Salop VS ¶ 21.

[122] *Id.*, ¶ 22 (internal citations omitted).

earning its lump if the competing downstream firms earn a positive margin over costs. That can be the result if, for example, the companies are selling differentiated products or operating with imperfect information regarding each other's prices and costs, as is the case in the rail markets likely to be affected by the proposed transaction.[123]

Dr. Majure acknowledges the one lump theory may not apply where the merging parties have imperfect information about each other's costs, prices, and rates.[124] As Professor Salop explains, in such a rail market, the monopoly carrier may not be able to extract its "one lump" prior to the merger. Instead, uncertainty regarding the rates and costs of the other carriers may result in the monopoly carrier setting its pre-merger divisions below the monopoly level, out of concern that if the through rate exceeds the price the shipper is willing to pay the carrier will not win the movement.[125]

Thus, competition in the pre-merger market with imperfect information leads to the shipper obtaining through rates that are below its reservation price at least some of the time.[126] A merger with one of the downstream competing railroads, however, reduces that uncertainty, which increases the likelihood that the merged firm will be able to profitably raise rates. After (and because of) the merger, for example, CP and KCS will know each other's costs and prices, be better able to set a single-line rate equal to the shipper's reservation price—in other words, a higher price than the shipper is offered today—and thus will be better able to extract the full

[123] *See id.*, ¶ 23.

[124] *See* Ex. 1 (Majure Tr. 60:18–25 ("[T]he degree of imperfection of the information would affect the degree to which the theory is applicable.")).

[125] *See* Salop VS ¶ 37.

[126] *See id.*, ¶ 38.

monopoly revenue from the shipper than KCS can today. Contrary to the one-lump presumption, a merger in such a market increases the post-merger firm's ability and incentive to foreclose.[127]

As Professor Salop explains, even in markets where the participants have access to better information, the one-lump theory does not apply to an end-to-end merger involving a monopoly carrier and one of the competing carriers if the services offered by the competing carriers are not perfect substitutes for each other.[128] That is precisely the situation here. The transport services offered by UP and KCS differ across a spectrum of factors, such as relative distance from a shipper's business to the origin and destination stations, the speed of the shipment, etc. As a result, today UP and KCS are able to charge through rates that exceed their marginal costs, and KCSM may therefore be unable to extract its single monopoly profit. KCS already has the ability and incentive to foreclose today, and merging with CP will only exacerbate those concerns, because it will enable the combined CPKC to earn additional revenue and profits on the CP segments of movements, increasing the financial benefits of foreclosure.

Professor Salop illustrates the inapplicability of the one-lump presumption to the proposed transaction with simulation models designed to reflect some of the variations in characteristics of shippers, commodities, and origin-destination routes that could be affected by the merger.[129] Professor Salop's work recognizes that the effects of a merger may differ across origin/destination markets and commodities. And, as the results of his models demonstrate, he notes that the ultimate effects of a vertical merger on shippers depends on the interplay of numerous factors, including the extent to which the incentive to raise prices through a

[127] *See id.*, ¶ 39.
[128] *See id.*, ¶¶ 40–43.
[129] *See id.*, ¶¶ 50–54.

foreclosure strategy may be offset by the incentive to lower prices, for example as a result of merger-specific efficiencies.

Professor Salop's models confirm that vertical mergers like the proposed transaction can produce either or both sorts of incentives, and they may benefit some shippers and harm others. The models do not attempt to predict the likelihood of any particular outcome, but rather demonstrate that vertical mergers in markets with characteristics such as those at issue in this transaction can lead to a wide variety of impacts. The results of his simulation models show that significant price changes are highly possible, and that some or all shippers can be harmed as a result of an end-to-end merger.[130] That there is no certain or even "most likely" general result is precisely the point; the models demonstrate that there is no economic basis for presuming that a merger such as the CP/KCS merger will be procompetitive, anticompetitive, or competitively neutral.

In fact, as other aspects of Professor Salop's analysis demonstrate, the proposed merger raises serious risks of anticompetitive foreclosure. Applicants' experts Brown and Zebrowski estimate the volume of traffic that moves through the Laredo gateway that the post-merger company could be able to divert. Their calculations incorporate the assumption that CPKC will not reduce rates to attract business away from competitors that currently interline with KCS and KCSM and that CPKC will rely instead on post-merger quality improvements—improvements that UP witness Thomas Haley explains are largely not merger-specific[131]—to win the significant volumes of additional traffic necessary to justify the cost of the acquisition.[132] Brown and Zebrowski also assume that CPKC will not engage in foreclosure but that, again, is just another

[130] *See id.*, ¶ 54.

[131] *See generally* Haley VS ¶¶ 18–36.

[132] *See* Salop VS ¶¶ 83–84.

assumption—Brown and Zebrowski neither provide nor cite to any evidence that CPKC will not have an incentive to foreclose rivals.

As Professor Salop notes, if CPKC will be able to divert traffic by reducing its own costs, as Brown and Zebrowski's formulation assumes, it could also divert traffic by increasing its rivals' costs through a foreclosure strategy.[133] And in fact, CPKC will have an *increased* incentive and ability to raise KCSM interline rates, compared to the situation pre-merger (where such incentives already exist), because shipments diverted from competitors like UP will enable CPKC to capture the revenue and profits associated with the KCS segments as well as the CP segments.[134] Professor Salop illustrates this conclusion by extending the Brown and Zebrowski analysis to an example of movements of finished automobiles from Mexico to Chicago via Laredo, demonstrating that even partial foreclosure would be profitable for CPKC, even if it resulted in CPKC losing some revenue and margin as a result of decreased interlining between KCSM and the foreclosed competitors.[135]

B. The Statement of Applicants' Expert Does Not Support a Presumption That the Proposed Transaction Will Not Have Anticompetitive Effects.

In his Verified Statement, Dr. Majure dismisses concerns regarding CPKC's incentives and ability to foreclose competition without actually analyzing or addressing those concerns. As discussed above, Dr. Majure relies entirely on the "one lump" presumption that vertical end-to-end mergers with a monopolist at one end and a railroad facing competition at the other end cannot have anticompetitive effects. Relying on that presumption, Dr. Majure asserts that CPKC will not have "the incentive and ability as a combined firm to foreclose rivals or otherwise lessen

[133] *See id.*, ¶ 75.

[134] *See id.*, ¶ 76.

[135] *See id.*, ¶¶ 77–80.

competition as a result of vertical integration,"[136] because "KCS would already be collecting the full measure of returns associated with its existing market power."[137]

Dr. Majure's use of the conditional progressive—"would already be collecting," not "is already collecting . . . ."—is telling. It reflects that Dr. Majure does not *know* whether KCSM is currently collecting the full measure of returns associated with its existing market power. He cannot know, because he has not examined any documents or data from KCSM and, as Applicants' responses to interrogatories admit, his analysis was "not based on any specific documentary evidence in the possession of Applicants."[138] Nor has he tested his hypothesis that the post-merger firm will not have the ability to foreclose if shippers and interlining carriers have alternatives to KCSM. He suggests that FXE may be such an alternative,[139] but does not analyze the issue or show that FXE actually offers a viable option for shippers using KCSM.[140]

Dr. Majure's only effort to address these serious gaps in his analysis is his examination of traffic shares for the northbound traffic that KCSM brought to Laredo from Mexico in 2019. He claims that this empirical analysis—specifically, his conclusion that in 2019 KCSM interchanged 68% of shipments with UP at the Laredo gateway for which KCS could have served the final destination—is "consistent" with the absence of foreclosure incentives.[141] But that percentage is

[136] APP Vol. 2 at 12, Majure VS ¶ 12.

[137] *Id*. at 19, Majure VS ¶ 24.

[138] Ex. 12 (KCS and CP's Supplemental Joint Responses and Objections to CSXT's Second Set of Discovery Requests, Response to Interrog. No. 12); *see also* Ex. 1 (Majure Tr. 63:22–64:11).

[139] *See* APP Vol. 2 at 20, Majure VS ¶ 25.

[140] *See* Ex. 1 (Majure Tr. 84:18–24 ("Q: Have you done any analysis as to whether FXE is a ready alternative for shippers using KCSM today? A: No, I have not tried to isolate the -- or test whether this hypothetical applied to any particular shipper or the degree to which it was.")).

[141] APP Vol. 2 at 22–23, Majure VS ¶¶ 30–31 & Ex. 2; *see also* Ex. 1 (Majure Tr. 64:2–65:6).

equally consistent with the opposite of what Dr. Majure claims. It also tells us nothing about how merging with CP may increase KCS's incentives to foreclose.

Even leaving aside that Dr. Majure's use of very broad BEA areas to define the relevant geographic areas of competition almost certainly overstated the extent to which KCS could have handled the movements that were interchanged with UP at Laredo, Dr. Majure's analysis is flawed for at least two fundamental reasons.

First, Dr. Majure analyzes only a snapshot of some 2019 traffic. He does not compare his results with what the market looked like fifteen years earlier, when KCS acquired KCSM's predecessor and control of the Laredo Gateway,[142] nor does he compare his 2019 results with the counterfactual: the market "but for" the KCS/TFM/Tex-Mex transaction.[143]

Because no counterfactual is presented against which to measure his claims, one cannot reasonably conclude that the share of traffic Dr. Majure claims KCS interchanged with UP moving north of Laredo demonstrates anything at all, other than perhaps that KCS was not engaging in a strategy of *complete* foreclosure in 2019. In fact, as Professor Salop notes, UP's share of northbound shipments from Laredo was significantly *higher* prior to the merger that gave KCS control of that gateway than it was in the single year Dr. Majure chose to examine.[144] There are many possible explanations for that decline, as both Professor Salop[145] and Dr.

[142] *See, e.g.*, Ex. 1 (Majure Tr. 101:16–19 ("I did not try to do a before-and-after comparison of the number of cars that came to Laredo before and after the merger.")).

[143] *See, e.g.*, APP Vol. 2 at 21–25, Majure VS ¶¶ 28–33; *see also* Ex. 1 (Majure Tr. 101:20–102:2 ("Q: So you did not attempt to define a but-for world in which the KCS/TFM transaction didn't occur. Correct? A: Didn't try to -- I did not try to forecast how the traffic might have evolved over the course of 15 years in a hypothetical where there was no transaction.")).

[144] *See* Salop VS ¶ 90.

[145] *See id.*, ¶ 91.

Majure[146] acknowledge. Dr. Majure's analysis sheds no light on the reasons for the change, because he did not measure his 2019 numbers against figures for earlier years, nor did he attempt to identify what would have happened to those shares had the earlier merger not occurred.

Second, Dr. Majure did not analyze traffic moving south from Laredo into Mexico.[147] That is not surprising, because the results of that analysis are at odds with his conclusions. Using the same format that Dr. Majure used for his assessment of northbound traffic, Professor Salop found that UP's share of southbound traffic interchanged from areas that KCS serves is far *smaller* than its share of such traffic moving north. If, as Dr. Majure claims, UP moving a large share of traffic in areas that KCS can serve north of Laredo is consistent with KCS having no incentive to foreclose, then applying Dr. Majure's logic, UP's much smaller share of such southbound traffic must be consistent with a significant foreclosure concern.[148]

Of course, the key question is not only whether KCS has the pre-merger incentive and ability to foreclose competition, but whether the merger with CP will increase that incentive and ability. The one-lump theory presumes that certain vertical mergers cannot have that effect, but Professor Salop explains in his Verified Statement why that presumption is not applicable to the proposed transaction. He also explains why the post-merger CPKC will have *greater* incentive to foreclose than KCS does today, because it will earn additional revenue and profits on the CP segments of movements, increasing the financial benefits of foreclosure.

Dr. Majure and Applicants ignore that reality, instead arguing that foreclosure concerns cannot be cognizable unless the Board or opponents of the transaction identify pre-merger

[146] *See* Ex. 1 (Majure Tr. 228:10–229:24).

[147] APP Vol. 2 at 22, Majure VS ¶ 30 n.17; *see also* Ex. 1 (Majure Tr. 122:5–7 ("I have not tried to do a similar exercise to Exhibit 2 focused on southbound movements.")).

[148] *See* Salop VS ¶¶ 94–96 & Fig. 8.

constraints on the parties' ability to foreclose and explain how the merger would relax or eliminate those constraints.[149] Dr. Majure has testified that because he could identify no such constraints, CP and KCS must not "have any unexploited power . . . that might be unlocked by a merger."[150] But pre-merger constraints on the parties' ability to foreclose are not difficult to find, if one looks for them. For example, the merger would improve the cost and price information to which the merging parties will have access, making it easier for CPKC to exploit fully KCSM's monopoly power.[151] The merger would also eliminate the information asymmetries and strategic bargaining incentives that would make it difficult for the parties today to reach agreement to structure their pricing and operations in a way that forecloses competitors, as well as the legal constraints on the parties' ability to enter into such anticompetitive agreements.[152]

There is therefore no basis for Dr. Majure to move from his limited conclusion that, in 2019, KCS interchanged a large amount of northbound traffic to UP to his sweeping claim that "a combined CPKC would not have the ability and incentive to preclude its rivals' access to gateways."[153] His analysis, such as it is, says nothing about whether KCS has the incentive and ability to foreclose some competition today, nothing about whether the merger with CP will increase those incentives, and nothing about whether foreclosure may be a profitable strategy for

[149] *See* Ex. 1 (Majure Tr. 89:24–90:25); Ex. 12 (KCS and CP's Supplemental Joint Responses and Objections to CSXT's Second Set of Discovery Requests, Response to Interrog. No. 27 (arguing that "the conditions that would raise concern about possible foreclosure" include "a pre-existing constraint that can be shown to limit the feasibility of arrangements CP and/or KCS could have, as separate entities, to align their respective incentives and abilities in a fashion that would lessen competition" and "a credible mechanism by which [the merger] makes the constraint no longer bind")).

[150] Ex. 1 (Majure Tr. at 71:12–14).

[151] *See, e.g.*, Salop VS ¶¶ 36–39.

[152] *See id.*, ¶¶ 101–105.

[153] APP Vol. 2 at 23, Majure VS ¶ 31.

the combined company. In short, his analysis says nothing about whether the proposed merger is in the public interest, and instead casts significant doubt on that conclusion.

C. A Presumption That Certain Categories of Mergers Are Procompetitive Is Inconsistent With Current Antitrust Enforcement Policy.

Dr. Majure's formulaic reliance on the one-lump theory is also inconsistent with evolving economic thinking surrounding vertical mergers. To be clear, UP is not suggesting all vertical mergers are anticompetitive, all end-to-end railroad mergers are anticompetitive, or all vertical mergers are pro-competitive. UP's position is simply that it would be inappropriate to presume any of those outcomes in the merger currently before the Board. As Professor Salop notes, vertical mergers can generate efficiencies and lead to pro-competitive benefits for shippers, but the conditions that would be necessary to produce such an outcome are not present here.

And those facts matter, which is why presuming that the proposed merger has no anticompetitive effects would be inconsistent with current competition enforcement policy and the modern economic analysis that supports it. The Vertical Merger Guidelines issued by the DOJ and the FTC in 2020 ("2020 VMGs"), for example, note that a "vertical merger may diminish competition by allowing the merged firm to profitably use its control of the related product to weaken or remove the competitive constraint from one or more of its actual or potential rivals in the relevant market."[154] Of note, the 2020 VMGs make *no* mention of a presumption that vertical mergers are pro-competitive. Dr. Majure provided comments on the draft 2020 VMGs, and did not recommend that they include any such presumption.[155]

[154] U.S. Dep't of Just. & F.T.C., *Vertical Merger Guidelines* at 4 (June 30, 2020).

[155] *See generally* Hatzitaskos et al., *Comments on the January 2020 Draft Vertical Merger Guidelines* (Feb. 19, 2020).

Dr. Majure's comments on the draft 2020 VMGs reflect an evolving view that vertical mergers should be reviewed as carefully as horizontal mergers. Before they were issued, FTC Chairman Joseph Simons commented that one of the goals of the draft 2020 VMGs was to "make clear that anticompetitive vertical mergers are not unicorns," and that "there should not be a presumption that all vertical mergers are benign."[156] Even after their issuance, there has been substantial disagreement on whether the 2020 VMGs went far enough in expressing concerns about vertical mergers.[157] In July 2021, the President issued an executive order on competition, specifically encouraging the Attorney General and the Chair of the FTC to review and consider whether to revisit the horizontal and vertical merger guidelines.[158] On September 15, 2021, the FTC voted 3-2 to rescind the 2020 VMGs. As noted by then-Commissioner Rohit Chopra, "[v]ertical integration, as we all recognize, can lead to foreclosure of rivals and increased barriers to entry."[159] And while the 2020 VMGs remain in place at DOJ, they are nonetheless under review, and the Department plans to seek public comment on issues such as the burden-shifting framework and range of circumstances considered that can lead to harm of competition.[160]

[156] Prepared Remarks of Chairman Joseph Simons, *Fordham Speech on Hearings Output* (Sept. 13, 2019).

[157] *See, e.g.*, Dissenting Statement of Commissioner Rebecca K. Slaughter regarding FTC-DOJ Vertical Merger Guidelines (June 30, 2020) ("The Vertical Merger Guidelines are inexplicably mute on the well-known and well-supported fact that the potential anticompetitive harms from raising rivals' cost and foreclosure are also 'distinct considerations' in vertical-merger analysis.").

[158] *See Biden Competition Order*, Sec 5(c).

[159] Prepared Remarks of Commissioner Rohit Chopra regarding 2020 FTC-DOJ Vertical Merger Guidelines (Sept. 15, 2021); *see also* Statement of Chair Lina M. Khan and Commissioners Rohit Chopra and Rebecca K. Slaughter on the Withdrawal of the Vertical Merger Guidelines, (Sept. 15, 2021).

[160] *See* Press Release, U.S. Dep't of Just., *Justice Department Issues Statement on the Vertical Merger Guidelines* (Sept. 15, 2021).

Recent enforcement actions, along with the increasing scrutiny previously discussed, reflect this reality. For example, in *United States of America v. AT&T, Inc.*, the Department of Justice argued that vertical mergers can lessen competition "where the merging parties—by means of their control of an input that their competitors need—have the incentive and ability to substantially lessen competition by withholding or raising the price for that input."[161] This concern is also reflected in recent enforcement actions brought by the FTC to block vertical transactions, including its challenges to Illumina's attempted acquisition of GRAIL,[162] Nvidia's attempted acquisition of Arm,[163] and Lockheed Martin's attempted acquisition of Aerojet Rocketdyne.[164] Presuming that the proposed transaction is procompetitive—instead of requiring Applicants to demonstrate its likely net competitive effects—would put the Board squarely at odds with the other agencies participating in the Administration's efforts to scrutinize vertical mergers and promote effective competition.

IV. Other Transportation Alternatives Will Not Prevent Anticompetitive Effects.

Because Applicants essentially assume the proposed transaction does not raise any competitive issues relating to cross-border traffic, they did not meaningfully address whether other transportation options would prevent anticompetitive effects. KCS's Chief Executive Officer says CPKC could not raise rates on KCSM movements that "would shift to motor or water carriage," but he never addressed whether any KCSM traffic *could* shift if CPKC tried to

[161] Complaint at 7, *United States of America v. AT&T, Inc.*, 310 F. Supp. 3d 161 (D.D.C. 2018) (No. 1:17-cv-02511).

[162] *See* Complaint, *Illumina, Inc.*, Docket No. 9401 (F.T.C. Mar. 30, 2021).

[163] *See* Complaint, *Nvidia Corp.*, Docket No. 9404 (F.T.C. Dec. 6, 2021).

[164] *See* Complaint, *Lockheed Martin Corp.*, Docket No. 9405 (F.T.C. Jan. 25, 2022).

raise rates.[165] Similarly, Dr. Majure opines that CPKC could not force inferior terms on a shipper "who can readily switch to another railroad or mode of transportation." [166] But Dr. Majure was addressing a "hypothetical shipper."[167] He never actually looked to see whether any such shippers are served by KCSM. In discovery, Applicants said Dr. Majure's discussion of shippers with "ready alternatives" was "not based on a contention regarding any particular shipper's actual competitive options" but rather "was presented to illuminate the range of possibilities envisioned by economic theory and analysis."[168] When asked to produce documents discussing whether KCSM rates are constrained by competitive pressures from other rail options, Applicants responded that KCS "has no responsive documents."[169] CP's Chief Marketing Officer was the only one of Applicants' witnesses to discuss actual competitive options available to shippers, and he agreed that their options are limited: "many of the commodity flows in the[] lanes [targeted for diversion]—like LPG, grain, finished autos and others—are not well suited to long-distance movement by truck."[170]

As Mr. Rocker explains, a substantial number of shippers currently using UP-KCSM service do not have viable intramodal or intermodal alternatives to KCSM service in Mexico.[171] If CPKC tried to divert their traffic by raising KCSM-UP rates or degrading KCSM-UP service,

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[165] APP Vol. 1 at 208, Ottensmeyer VS at 22.

[166] APP Vol. 2 at 19, Majure VS ¶ 25.

[167] *Id.*

[168] Ex. 12 (KCS and CP's Supplemental Joint Responses and Objections to CSXT's Second Set of Discovery Requests, Response to Interrog. No. 13).

[169] Ex. 3 (KCS and CP's Joint Responses and Objections to UP's First Set of Discovery Requests, Response to Request No. 101).

[170] APP Vol. 1 at 226, Brooks VS ¶ 26.

[171] *See* Rocker/Turner VS at 16–17.

they would have no choice but to pay more, shift their business to CPKC, or both.[172] Most UP-KCSM traffic originates or terminates at points served exclusively by KCSM. Other traffic moves to or from points served by FXE, but FXE lacks an efficient route to the border.[173] In addition, truck and water service are not viable options for the vast majority of traffic that Applicants say they will target for diversion to KCSM.[174] Some shippers would have options, but those options would not protect the large number of shippers dependent on KCSM.

V. Mexico's Regulatory Regime Will Not Prevent CPKC From Engaging In Anticompetitive Acts Affecting U.S. Shippers.

Applicants suggest Mexican law would prevent CPKC from engaging in anticompetitive conduct because Mexican law would "restrict[] the combined CP/KCS network from providing only a single-line rate on international through traffic."[175] Dr. de la Calle, former Undersecretary for International Trade Negotiations in Mexico's Ministry of the Economy and former Trade and NAFTA Minister at the Mexican Embassy in Washington, D.C., explains that Mexican law and regulations would not effectively prevent CPKC from engaging in anticompetitive behavior.

As Dr. de la Calle explains, Mexican law would not prevent CPKC from foreclosing competition using the rate tactics described by Messrs. Rocker and Salop: raising KCSM rates between Laredo and KCSM-served points on a non-discriminatory basis, while reducing the U.S. portion of CPKC rates as needed. Mexican law does not impose a practical limit on how high KCSM could raise its rates in Mexico to carry out this strategy.[176] Mexican law and the KCSM

[172] *See id.* at 16.

[173] *See id.*

[174] *See id.* at 16–17.

[175] APP Vol. 1 at 207, Ottensmeyer VS at 21 n.18.

[176] As Dr. de la Calle observes, a procedure exists though which certain parties may challenge a carrier's registered maximum rates at ARTF, but the party would first have to demonstrate to

Concession contain various provisions that purport to require KCSM to set rates in a non-discriminatory manner. However, as Dr. de la Calle explains, Mexican authorities likely would not address the overall CPKC rate for traffic moving between Mexico and the United States if KCSM's portion of the rate was offered in a nondiscriminatory manner.[177] In other words, a strategy involving across-the-board KCSM rate increases for traffic moving between Mexican points and Laredo, combined with CPKC rate reductions in the U.S., probably would not be actionable in Mexico.

CPKC may take the position that treating CPKC traffic differently from interline traffic is not discriminatory under Mexican law. In Mexico, jurisdiction over rail rates is split between two agencies, the Federal Economic Competition Commission ("COFECE") and the Railway Transport Regulatory Agency ("ARTF"). Neither COFECE nor ARTF appears to have ever investigated a case involving railroad rate discrimination, much less in the cross-border context, so there is no guidance available regarding how regulators would view the law as applied to a rate strategy of the kind described above.[178]

Even if UP or affected U.S. shippers could in theory challenge discriminatory conduct by CPKC, the process for obtaining a favorable resolution, then enforcing it against CPKC, would likely involve years of protracted litigation before administrative agencies and courts in Mexico. Turf battles between COFECE and ARTF could add to the protracted nature of any litigation.[179]

COFECE that effective competition does not exist in the relevant market. Both proceedings would take years to resolve and the agency decisions would be subject to multiple court challenges along the way. *See* de la Calle VS at 6, 9–12.

[177] *See id.* at 6.

[178] *See id.* at 7.

[179] *See id.* at 10.

In addition, all resolutions issued by Mexican administrative agencies are subject to complicated appeal and review by Mexican courts, and can be blocked by an "amparos" claim, a type of injunction proceeding available to parties seeking to contest the agency decision.[180] COFECE's recent experiences in investigating allegations of anticompetitive conduct in various economic sectors and ARTF's limited efforts to regulate domestic rail rate tariffs confirm the challenges UP or a shipper would face in seeking effective resolution of such matters in Mexico.[181] As a result, Mexican law cannot realistically protect U.S. shippers from anticompetitive effects of CPKC's control of traffic moving between the U.S. and Mexico.

Finally, Mexican regulators would not protect against anticompetitive foreclosure at the Laredo Gateway through their review of the proposed transaction. COFECE issued a four-page decision unconditionally clearing the transaction in November 2021. The four-page decision provides no indication that COFECE considered competition for cross-border traffic or the impacts of the transaction on shippers in the United States.[182]

VI. Applicants' Failure To Address The Proposed Transaction's Impacts On Facilities Applicants Share With Other Railroads Precludes The Board From Finding That An Unconditioned Transaction Would Be Consistent With The Public Interest.

The substantial anticompetitive risks created by the proposed transaction—and the absence of meaningful offsetting benefits—are reason enough for the Board to conclude that unconditioned CP control of KCS would not be consistent with the public interest. However, the Application is also fundamentally deficient in another respect: It fails to address both CPKC's planned operations on facilities owned by other railroads and other railroads' use of facilities

[180] *See id.* at 6 n.2.

[181] *See id.* at 9–12.

[182] *See id.* at 12–13.

owned by CPKC. As a result, Applicants fail to take into account the substantial investments in new capacity that would be required to implement their proposed transaction.[183] The Board cannot find the proposed transaction is consistent with the public interest without imposing conditions to ensure that Applicants bear responsibility for the costs of implementing their transaction.

Applicants share lines and terminal areas with other railroads all along their North-South corridor in the United States, from South Texas to Kansas City to the Twin Cities. Applicants' failure to provide for the additional capacity necessary to implement their transaction in these locations would harm the many shippers whose traffic moves over the shared lines and in the shared terminals.

Applicants' failure to address shared facilities stems from a critical flaw in their effort to identify capacity needs of a merged system. Applicants claim "[d]etailed capacity modeling was performed to identify the additional infrastructure needs required to support anticipated traffic growth while maintaining the improved level of services that will attract and retain traffic."[184] That claim is untrue. Applicants' workpapers show {{

}}

[183] *See* 49 C.F.R. § 1180.8(a) (2000) ("Submit a summary of the proposed operating plan changes, based on the impact analyses, that will result from the transaction, and their anticipated timing, allowing for any time required to complete rehabilitation, upgrading, yard construction, or other major operational changes following consummation of the proposed transaction.").

[184] APP Vol. 2 at 340, OP Plan ¶ 238.

At one point, Applicants apparently {{

}}[185] However, Applicants apparently never followed through by developing the information for their Application.

When Applicants were asked about {

}[186]

}[187] But as discussed below, {

}[188] In trying to explain {

[185] Ex. 14 (CP Board of Directors Meeting Materials (CP-HC-00010640–10678, at 10645)).

[186] Ex. 15 (Elphick/Orr Tr. 80:21–81:22) { } *see also id.* (Elphick/Orr Tr. 85:24–86:12) {

}

[187] Ex. 15 (Elphick/Orr Tr. 125:5–24); *see also id.* (Elphick/Orr Tr. 73:16–18 {

}

[188] APP Vol. 2 at 340, OP Plan ¶ 237.

}[189]

{

}

Applicants' claim that they engaged in detailed capacity modeling to identify additional infrastructure needs to accommodate their plans on lines owned and used by other railroads is not credible for another reason: Applicants identified $279 million in investments on lines they would use exclusively to accommodate their planned traffic growth, but they identified no investments needed on lines owned by others or shared with others.[190]

The sections below briefly address some of the areas ignored in the Application. UP has not performed the detailed analyses to specify additional infrastructure that should be required to support Applicants' anticipated traffic growth.

A. Applicants Failed to Address Their Operations on Lines Owned by UP

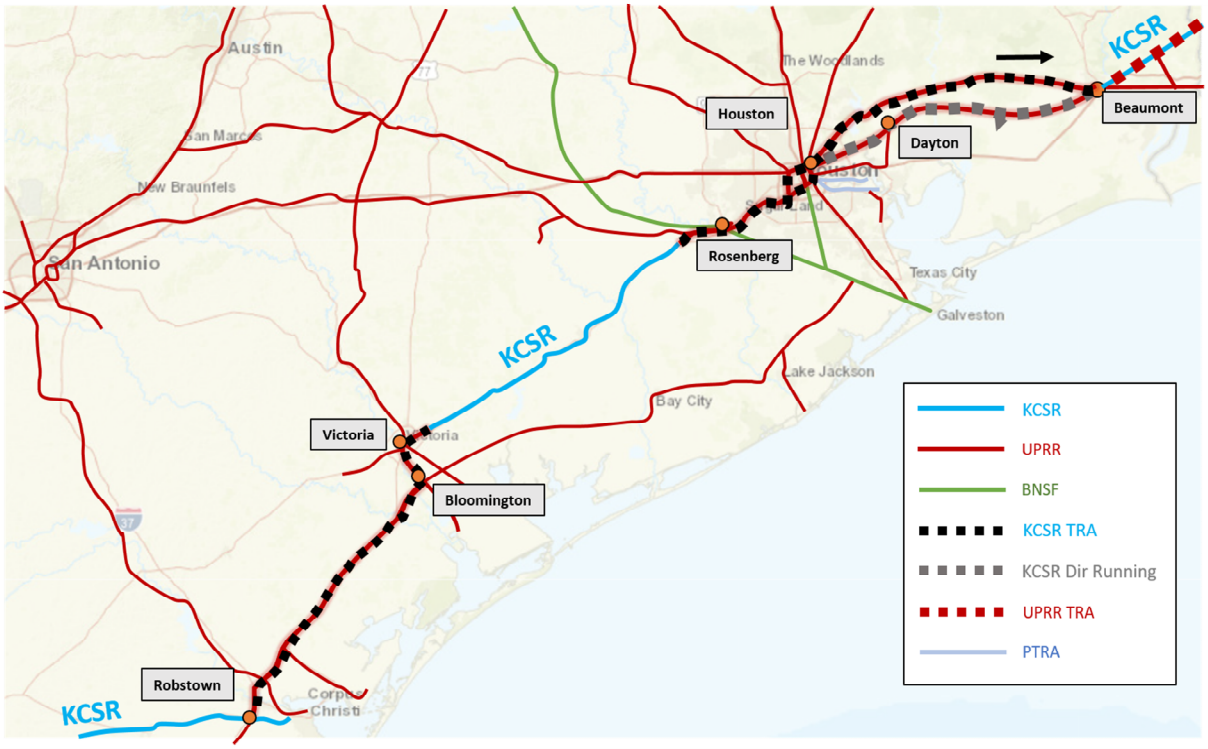
As shown in the figure below, large portions of KCS's route from Laredo to Shreveport, Louisiana, via Robstown/Corpus Christi, Victoria, Rosenberg, and Beaumont, Texas, including KCS's route through the busy Houston terminal, rely on trackage rights over UP lines that Tex Mex obtained in the *UP/SP* merger (the Tex Mex trackage rights lines).[191]

[189] Ex. 15 (Elphick/Orr Tr. 124:5–125:4).

[190] *See* APP Vol. 2 at 340–41, OP Plan ¶¶ 239–40 & Table 8.

[191] *See id.* at 276, OP Plan ¶ 52.

Figure 1: Texas Area KCS Trackage Rights



The Tex Mex trackage rights lines are critical to the merged CPKC's plans. They provide a necessary link in the North-South railroad transportation corridor connecting the United States, Canada, and Mexico that Applicants discuss throughout the Application. Applicants project they will more than double KCS's current use of the lines. At the southern end of the trackage rights, from Robstown to Victoria, CPKC traffic will increase from 7.7 trains per day to 16.8 trains per day, an increase of 9.1 trains per day, or 118%.[192] On the northern end, from Rosenberg through Houston to Beaumont, CPKC traffic will increase from 7.7 trains per day to 16.0 trains per day, an increase of 8.3 trains per day, or 108%.[193] Applicants do not identify any plan for investing in

[192] *See id.* at 364, OP Plan, App. A at 1.

[193] *See id.*

new capacity on any of the Tex Mex trackage rights lines.[194] However, accommodating their projected traffic growth will require new capacity on all these trackage rights lines.

Applicants' workpapers help explain why Applicants did not identify the need for any investments on the Tex Mex trackage rights lines: {

}

Applicants' capacity modeling for KCS lines is shown in one of Applicants' workpapers, Exhibit 2 in the deposition of Applicants' Operating Plan witnesses, Messrs. Elphick and Orr.[195] As Mr. Elphick explained, Applicants' capacity modeling process {

}}[196] The workpaper explains: {{

}}[197]

Applicant's capacity modeling workpaper shows {

}[198]

[194] APP Vol. 2 at 337, OP Plan ¶ 231, Fig. 11.

[195] Ex. 15 (Elphick/Orr Tr. 65:12–66:17).

[196] Ex. 15 (Elphick/Orr Tr. 60:21–62:12).

[197] Ex. 16 (Elphick/Orr Deposition Exhibit 2 (OP Plan workpaper "HC - Capacity - Methodology_docx.docx")).

[198] *See id.*; Ex. 15 (Elphick/Orr Tr. 72:18–73:2) {

As Mr. Turner explains, additional capacity would be required on the Tex Mex trackage rights lines to accommodate Applicants' planned traffic volumes.[199]

Robstown/Corpus Christi to West Junction. Additional capacity would be required on all UP's lines between Robstown and Beaumont to accommodate Applicants' planned traffic volumes. Currently, capacity on UP's lines between Robstown and Victoria is just sufficient to accommodate existing traffic, which includes not only KCS trains, but also UP trains moving between Houston, Corpus Christi, and Brownsville, and BNSF trains moving over the lines to interchange traffic with KCS at Robstown.[200] Any increased demand for capacity that would be created by Applicants' success in attracting traffic to the lines would not be offset by UP's loss of Mexico business. UP moves Laredo Gateway traffic using different lines—its lines via San Antonio.[201]

Accommodating CPKC's planned traffic growth would also require the addition of capacity on UP's Glidden Subdivision between Rosenberg and West Junction in Houston. The Glidden Subdivision, which runs between San Antonio and Houston, is a critical link in UP's Sunset Route and is also used by BNSF trackage rights trains and Amtrak. Again, the line has

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} *id.* (Elphick/Orr Tr. 85:24-86:1) {

} *id.* (Elphick/Orr Tr. 97:2–10) {

}

[199] *See* Rocker/Turner VS at 26–32.

[200] *See id.* at 28. To better accommodate existing traffic and growth projected before the CP/KCS transaction was announced, UP has been planning to construct a new siding just south of Bloomington that will be called the Linn siding. *See id.* at 29.

[201] *See id.* at 29.

sufficient capacity to accommodate current demand. However, Applicants' plan to add more than eight new trains per day would push use of the line above the line's fluid capacity.[202]

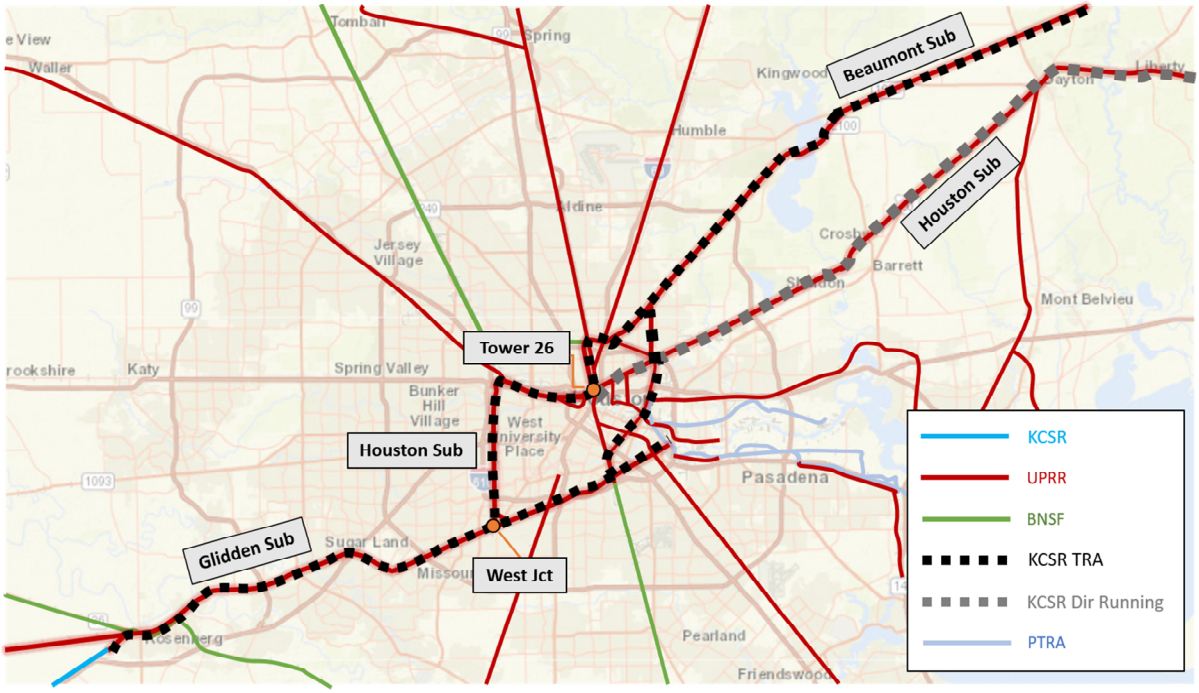
Houston terminal area. Applicants also fail to address the impact of their planned new traffic on operations in the Houston terminal. Houston is an extremely challenging area in the best of times, requiring careful operational coordination among UP, BNSF, KCS, Amtrak, and the Port Terminal Railroad Association (PTRA). UP has learned through hard experience how congestion in one part of Houston can rapidly spread throughout the terminal and ripple across its network.[203] As shown in the figure below, KCS has extensive trackage rights in Houston, allowing it to participate in the generally directional flow of traffic through the terminal and interchange traffic with the PTRA. KCS has trackage rights over UP's Houston Subdivision between West Junction and Tower 26, then over the West Belt, which provide KCS access to UP's Beaumont Subdivision. UP, BNSF, and KCS all use the Beaumont Subdivision for traffic moving eastbound towards Beaumont. Amtrak also uses the Beaumont Subdivision for its Sunset Limited train. KCS also has rights from the Beaumont Subdivision directly past UP's Settegast Yard on the East Belt, which connect to KCS's rights on the Glidden Subdivision. UP has also given KCS rights to move traffic westbound on UP's Houston Subdivision, which run past UP's Englewood Yard toward Tower 26.[204]

[202] *See id.*

[203] *See id.*

[204] *See id.* at 29–30.

Figure 2: Houston Area KCS Trackage Rights



Applicants plan to add more than eight trains per day to the mix of traffic in Houston, which could increase train counts on already busy lines by 25% or more.[205] However, Applicants provide no analysis of the impact their plans would have on terminal operations or the need for new capacity. As discussed above, { }

When Mr. Elphick was asked whether Applicants performed any formal evaluation of how increases in rail traffic from the proposed transaction would affect operations in Houston, he replied, { }[206] CP appears to believe there are no impediments to moving more trains through Houston. CP's Executive Vice-President Operations was recently quoted as saying, "you can get through Houston pretty quick."[207] However, as Mr. Turner explains,

[205] *See id.* at 30.

[206] Ex. 15 (Elphick/Orr Tr. 94:21–95:1).

[207] *See* Rocker/Turner VS at 30–31 & Rocker/Turner workpaper "P - Rail Group Interview.pdf."

additional capacity would be necessary at several locations in the terminal to prevent the projected jump in traffic from endangering operations in Houston.[208]

On the eastern end of the Houston terminal KCS has trackage rights on UP's Beaumont Subdivision and UP's Houston Subdivision between Houston and Beaumont. BNSF also uses those two lines to move its own traffic between Houston and New Orleans, and as noted above, Amtrak's Sunset Limited operates over the Beaumont Subdivision. These two lines are fluid at current traffic levels, but both would be at or above capacity if Applicants' traffic in the corridor grows by more than eight trains per day, as Applicants project in their Application.[209]

Applicants' complete failure to address the impacts of their planned traffic growth on the need for capacity investment on the Tex Mex trackage rights lines reflects a serious gap in their Application, especially given the essential role these rights play in their post-merger plans.

B. Applicants Failed to Fully Address Operations on Facilities They Own and Share With Others.

Applicants not only failed to evaluate the impacts of their planned traffic growth on lines CPKC would use but would not own, their analyses failed to account for the operations of other railroads with rights to use lines owned by Applicants. In some instances, {

} Three examples are discussed below.

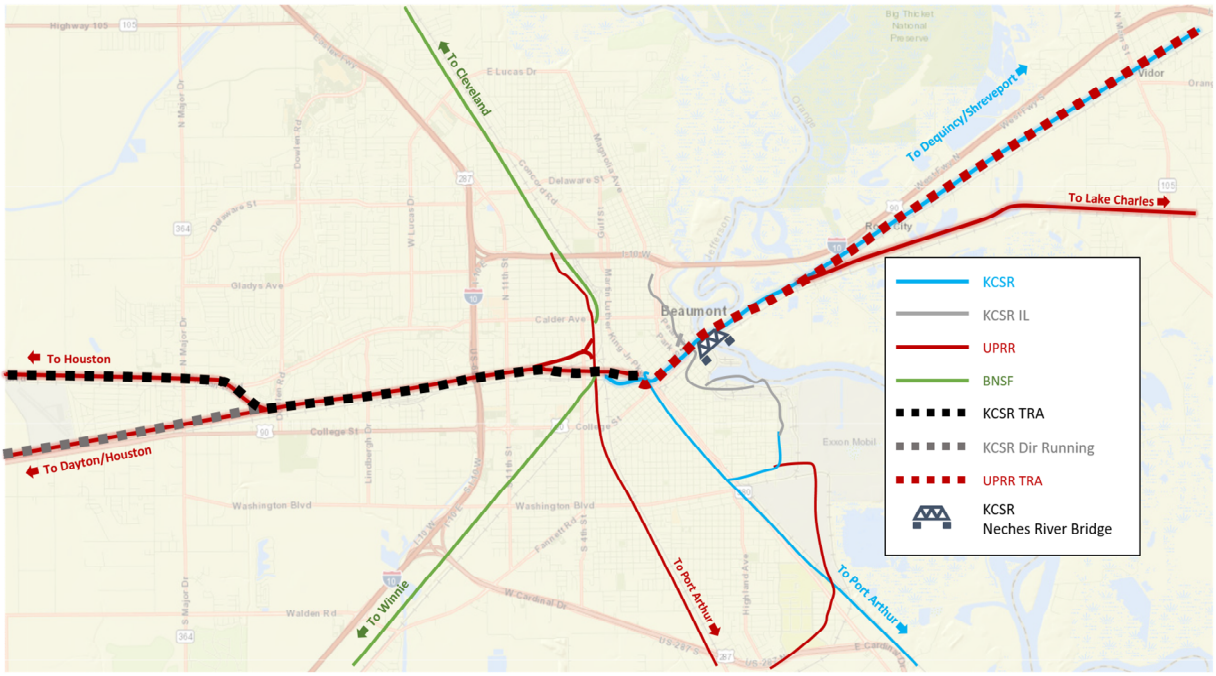
Neches River Bridge. UP is particularly concerned about the proposed transaction's impact on the Neches River Bridge. KCS owns the bridge, which spans the Neches River at

[208] *See* Rocker/Turner VS at 31.

[209] *See id.*

Beaumont.[210] UP's Beaumont and Houston Subdivisions converge at the bridge's west end. KCS's Beaumont Subdivision and UP's Lafayette Subdivision (also known as the 50/50 Line, because BNSF jointly owns the line) converge at the bridge's east end.[211] The bridge is a single-track choke point for UP, BNSF, and KCS, as shown in the figure below.

Figure 3: Neches River Bridge Area



As Mr. Turner explains, UP believes the Neches River Bridge is already near or at the limits of its fluid capacity. UP and BNSF currently operate approximately 25 trains per day over the bridge. Amtrak's Sunset Limited also uses the bridge. The bridge opens several times each day to allow river traffic to pass underneath. Bridge capacity is also limited by the nature of rail activity on each end of the bridge. On the east end, KCS blocks approach to the bridge when it

[210] *See* APP Vol. 2 at 320, OP Plan ¶ 175.

[211] *See* Rocker/Turner VS at 32.

moves unit trains into and out of the large Jefferson Energy Terminal. On the west end, trains must operate at reduced speeds over a series of converging and diverging tracks.[212]

Applicants plan to increase traffic on KCS's Beaumont Subdivision from 8.9 trains per day to 20.3 trains per day, an increase of 11.4 trains per day, or 128%.[213] However, Applicants did not identify any need for additional bridge capacity.

Applicants' workpapers reveal why Applicants did not identify a bridge capacity issue: {

}[214] {

}[215] {

}[216] {

}[217] {

}[218] {

[212] *See id*. at 33.

[213] *See* APP Vol. 2 at 364, OP Plan, App. A at 1.

[214] *See* Ex. 15 (Elphick/Orr Tr. 101:9–16).

[215] *See* Ex. 16 (Elphick/Orr Deposition Exhibit 2); Ex. 15 (Elphick/Orr Tr. 109:12–15) {

}

[216] *See* Ex. 16 (Elphick/Orr Deposition Exhibit 2); Ex. 15 (Elphick/Orr Tr. 108:3–11).
{{

}}

[217] *See* Ex. 16 (Elphick/Orr Deposition Exhibit 2); Ex. 15 (Elphick/Orr Tr. 108:3–11).

[218] *See* Ex. 15 (Elphick/Orr Tr. 108:19–109:4).

} When asked, Mr. Elphick ultimately {

}[219] Adding capacity to the route across the Neches River would be an expensive and time-consuming undertaking, but CPKC's plan requires that capacity to operate its North-South corridor.

Kansas City and the Polo Line. Applicants also failed to account for UP traffic that moves over a CP-UP joint facility north of Kansas City called the Polo Line. CP and UP access Kansas City from the north using paired tracks between Airline Junction in Kansas City and a location on CP's Kansas City Subdivision called Polo. UP operates approximately eight trains per day between Airline Junction and Polo.[220] Applicants plan to increase traffic on CP's Kansas City Subdivision from 2.9 trains per day to 16.9 trains per day, an increase of 14 trains per day, or nearly 500%.[221] However, Applicants do not identify the need for any investment between

[219] Ex. 15 (Elphick/Orr Tr. 113:3–12) {

}

{{

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{

} *See* Rocker/Turner VS at 34.

[220] *See* Rocker/Turner VS at 34.

[221] *See* APP Vol. 2 at 364, OP Plan, App. A at 1.

Airline Junction and Polo, even though UP has experienced challenges operating over the Polo Line with today's significantly lower volumes.[222]

{ } Applicants' capacity modeling for CP lines is addressed in a different workpaper than their modeling for KCS lines—Exhibit 3 in the deposition of Applicants' Operating Plan witnesses.[223] {

}[224] {

}[225]

{{ }}[226]

In discovery, Applicants produced { }

{{

}}[227] {

}[228] As Mr. Turner observes, the Polo Line is not truly a double-track

[222] *See* Rocker/Turner VS at 34–35.

[223] *See* Ex. 15 (Elphick/Orr Tr. 132:24–133:14); *see also* Ex. 17 (Elphick/Orr Deposition Exhibit 3 (OP Plan workpaper "HC – 2021 - 10-20 CP RJct-KCity and KCS KCity-Laredo.pdf")).

[224] *See* Ex. 15 (Elphick/Orr Tr. 136:11–15) {

}

[225] *See* Ex. 15 (Elphick/Orr Tr. 137:10–15).

[226] *See* Ex. 17 (Elphick/Orr Deposition Exhibit 3).

[227] *See* Ex. 15 (Elphick/Orr Tr. 137:25–139:15); *see also* Ex. 18 (Elphick/Orr Deposition Exhibit 7 (CP-HC-00007947.xlsx)).

[228] Ex. 15 (Elphick/Orr Tr. 139:22–140:21).

line.[229] {{

}} Applicants did not address the need for any investment on the Polo Line in their Application.

Twin Cities. Applicants' failure to account for the impacts of their proposed transactions on other railroads' operations extends to their plan to increase traffic moving through the Twin Cities. Applicants claim a benefit of the CP/KCS combination would come from options it gives shippers to bypass Chicago.[230] Applicants' plan to route traffic around Chicago would increase the number of trains moving through St. Paul, Minnesota, on CP's River Subdivision, from 11.9 trains per day to 18.1 trains per day, an increase of 6.2 trains per day, or 52%.[231] However, Applicants did not propose any capacity improvements in the St. Paul area.[232]

As shown in the figure below, UP, BNSF, and CP have significant, overlapping operations in St. Paul.

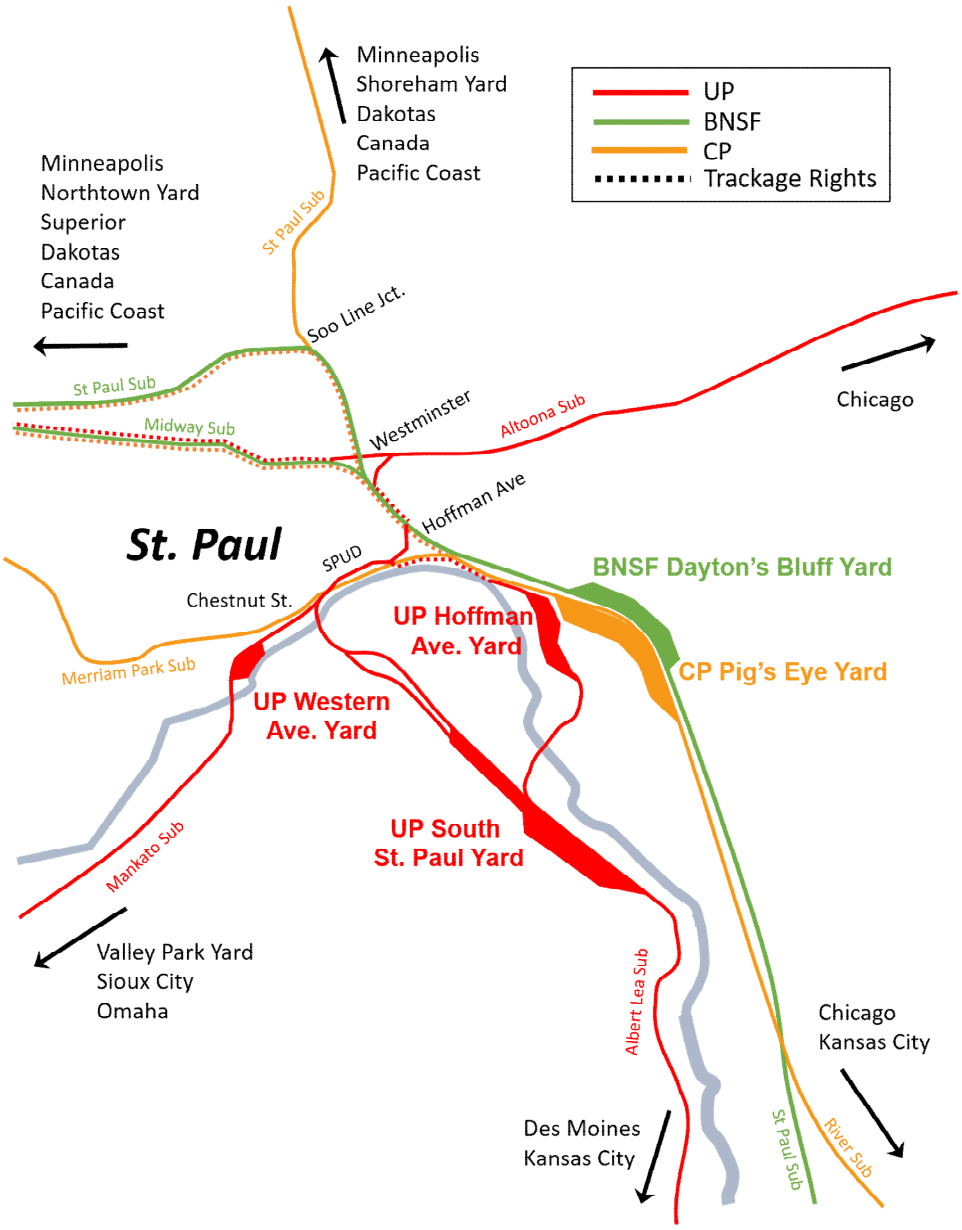
[229] *See* Rocker/Turner VS at 35.

[230] *See* APP Vol. 2 at 313, OP Plan ¶ 152.

[231] *See id.* at 364, OP Plan, App. A at 1.

[232] *See* APP Vol. 2 at 337, OP Plan ¶ 231, Fig. 11.

Figure 4: St. Paul Area



As a result, the St. Paul area can become extremely congested. CP's River Subdivision converges with BNSF's St. Paul Subdivision near CP's Pig's Eye Yard and BNSF's Dayton's Bluff Yard. North of those yards, CP and UP operate using trackage rights on BNSF to connect between their own lines through St. Paul. Specifically, CP uses the rights for its route between Canada, the Dakotas, and Chicago, while UP uses the rights for traffic moving between its Albert Lea Subdivision, Altoona Subdivision, and Mankato Subdivision and to reach several yards it

uses in St. Paul.[233] Amtrak's Empire Builder train also operates over CP's River Subdivision.[234] Applicants also say CP's yard in St. Paul "will see meaningful changes in classification demand" as a result of the proposed transaction.[235] {

}[236]

UP believes the increased traffic levels moving via CP's River Subdivision would require adding capacity to hold UP trains that would have wait longer for openings on CP and BNSF track to move through the St. Paul terminal between UP's lines.[237] Applicants apparently plan to impose these costs of accommodating their projected traffic growth on UP.

* * *

Applicants' failure to account fully in their Application for the impacts of their proposed transaction precludes them from carrying their burden of proving the transaction is in the public interest. The Board cannot find the proposed transaction would be in the public interest without evaluating a complete operating plan, and a complete operating plan must fully address changes in operations requiring new investment in capacity, the necessary investments in new capacity, and the time required to complete the projects.[238] The Application is plainly deficient because it ignores the need for new capacity at locations from north to south along the proposed CPKC network in the United States.

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[233] *See* Rocker/Turner VS at 35–36.

[234] *See* Ex. 15 (Elphick/Orr Tr. 145:14–16).

[235] APP Vol. 2 at 306; OP Plan ¶ 133.

[236] *See* Ex. 15 (Elphick/Orr Tr. 146:5–8) {

}

[237] *See* Rocker/Turner VS at 37.

[238] *See* 49 C.F.R. § 1180.8(a).

In addition, the Board cannot find the transaction to be in the public interest because it cannot accurately evaluate the transaction's net benefits without considering the cost of achieving the projected benefits. Here, Applicants seek credit for all the benefits they project, but they fail to acknowledge all the costs—or they plan to impose significant costs on others, which amounts to the same thing.

If the Board approves the transaction despite the significant deficiency in the Application, it should condition its approval to ameliorate the potential harms arising from the deficiency. As discussed in the next Part, the conditions must ensure other railroads and their customers are not forced to subsidize Applicants' implementation of their transaction.

VII. If The Board Approves The Proposed Transaction, It Should Impose Conditions To Protect Competition At The Laredo Gateway And Other Gateways And To Address Fully The Infrastructure Needed To Support Applicants' Planned Traffic Growth.

If the Board were to authorize the proposed transaction, it should impose conditions to mitigate the anticompetitive effects of the transaction and ensure it will be otherwise consistent with the public interest. An unconditioned transaction would produce effects that harm the public interest. UP's proposed conditions would ameliorate the harmful effects.[239] The conditions are designed to be concrete and enforceable, and to produce net public benefits.[240] They also are

[239] *See UP/SP*, 1 S.T.B. at 418 ("Conditions will not be imposed unless the merger produces effects harmful to the public interest (such as a significant loss of competition) that a condition will ameliorate or eliminate."); *Union Pacific Corp.—Control—Missouri-Kansas-Texas R.R.* ("*UP/MKT*"), 4 I.C.C.2d 409, 437 (1988) (conditions must "ameliorate or eliminate" a consolidation's "harmful effects").

[240] *See UP/SP*, 1 S.T.B. at 419 ("A condition must also be operationally feasible, and produce net public benefits."); *see also Union Pac. Corp.—Control—Mo. Pac. Corp.* ("*UP/MP*"), 366 I.C.C. 462, 565 (1982) ("conditions should not be imposed unless they will produce benefits outweighing their harm to the transaction").

narrowly tailored to remedy the transaction's adverse effects and nothing more.[241] They would not reduce the public benefits of the proposed transaction.[242] They would not prevent Applicants from achieving the legitimate objectives of increasing competition and reducing operating costs.[243]

Specifically, the Board should impose conditions to preserve effective competition for traffic moving over gateways, particularly the Laredo Gateway. It should also require Applicants to work with the railroads that own or use shared facilities affected by the transaction to identify investments required to accommodate Applicants' planned traffic growth, and to ensure the funding for such investments would not result in subsidization of Applicants' transaction.

UP's proposals for addressing these issues are described below.

A. The Board Should Impose Conditions to Protect Competition at Gateways.

Applicants have acknowledged the validity of concerns about the proposed transaction's effects on shippers' competitive options at gateways. They commit in a general way to keep the Laredo Gateway "and other affected gateways open both physically and commercially."[244] However, Applicants also recognize their commitments are not sufficiently "concrete" and "enforceable."[245] UP's proposed conditions are designed to convert Applicants' vague assurances into effective, concrete, enforceable remedial measures.

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[241] *See UP/SP*, 1 S.T.B. at 419 ("The condition must also be narrowly tailored to remedy [adverse] effects [of the transaction].").

[242] *Cf. UP/MKT*, 4 I.C.C.2d at 437 ("conditions [must] produce public benefits (through reduction or elimination of the possible harm) outweighing any reduction to the public benefits produced by the merger").

[243] *See UP/MKT*, 4 I.C.C.2d at 437 (conditions "must not frustrate the ability of the consolidated carrier to obtain the anticipated public benefits").

[244] APP Vol. 1 at 20–21, Application at 11–12.

[245] APP Vol. 1 at 233, Brooks VS ¶ 47.

Specifically, UP is asking the Board to:

1. Require Applicants to agree that when a customer asks CPKC to provide rates for (i) CPKC service for only former-CP, former-KCS, and/or former-KCSM portions of an origin-to-destination route, and (ii) CPKC single-line service on a competitive route, CPKC must provide the customer with a Rule 11 rate for the former-CP, former-KCS, or former-KCSM portions that reflects a mileage-based prorate of the CPKC single-line rate.

2(a). Require Applicants to adhere to KCS's pledges regarding operations for traffic moving over the Laredo Gateway and at the Laredo Bridge in the KCS/Tex Mex proceeding.

2(b). Require Applicants to provide UP access to any new railroad bridge constructed in Laredo on the same terms as UP's access to the existing bridge.

1. The Board Should Require CPKC to Offer Shippers "Commercially Reasonable" Rates to Gateways Based on a Mileage Prorate of CPKC Single-Line Rates.

Applicants' commitment to keep the Laredo Gateway and other gateways open by quoting "commercially reasonable" Rule 11 rates is neither concrete nor enforceable. Applicants promise that when a shipper asks for a gateway rate, CPKC will "provide the shipper with a Rule 11 rate to the gateway."[246] However, without some established method of evaluating whether the gateway rate provided is "commercially reasonable," the promise to provide a rate is worthless.

"Commercially reasonable" is not a concrete, enforceable standard for establishing rates. There is no mechanical definition of what it means for a rate to be "commercially reasonable."[247] Railroad business practice does not offer any standards. None of UP's contracts calls simply for

[246] APP Vol. 1 at 233, Brooks VS ¶ 46.

[247] Rocker/Turner VS at 19.

rates to be "commercially reasonable."[248] CP likewise does not have contracts that require CP to charge "commercially reasonable rates."[249] CP Chief Marketing Officer John Brooks announced Applicants' commitment to providing "commercially reasonable" gateway rates in a verified statement submitted with the Application.[250] When asked in discovery how a decision-maker would determine whether a rate was "commercially reasonable," Mr. Brooks responded that the process "would involve probably both parties describing why their case or rate was reasonable."[251] When asked whether Applicants proposed any standards a decision-maker could use to make a determination, Mr. Brooks simply said, "No."[252]

In response to written discovery, Applicants said "commercially reasonable" terms simply means terms "established by CPKC in good faith to provide customers with the option of continued movement of rail traffic via an affected pre-Transaction interline route."[253] However, Mr. Brooks recognized that CPKC and a shipper could disagree in good faith about whether a proposed rate is "commercially reasonable."[254]

Ultimately, Applicants made clear how meaningless their promise would be in practice. When UP sought discovery to test KCS's compliance with its commitment in the KCS/Tex Mex

[248] *See id.*

[249] *See* Ex. 7 (Brooks Tr. 98:7–24).

[250] *See* APP Vol. 1 at 233, Brooks VS ¶ 46.

[251] Ex. 7 (Brooks Tr. 100:25–101:6).

[252] Ex. 7 (Brooks Tr. 101:7–101:10). When CP acquired the Dakota, Minnesota & Eastern Railway in 2008, CP also promised to keep gateways open on "commercially reasonable terms." *Canadian Pac. Ry., et al.—Control—Dakota, Minn. & E. R.R., et al.*, FD 35081, slip op. at 5 (STB served Sept. 30, 2008). Mr. Brooks testified there was no training that told people how to adhere to the open gateway commitment. *See* Ex. 7 (Brooks Tr. 134:6–135:6).

[253] Ex. 3 (KCS and CP's Joint Responses and Objections to UP's First Set of Discovery Requests, Response to Request No. 40).

[254] Ex. 7 (Brooks Tr. 102:19–103:2).

merger to charge "commercially reasonable" rates, Applicants said evaluating compliance was impossible. They said the Board had never established any "metrics" or a "ruler" to determine whether a particular rate was "commercially reasonable," so any effort to prove rates offered by KCS were not "commercially reasonable," even "with full hindsight," would amount to "wild speculation":

> The Board did not define "commercially reasonable" in its 2004 Tex Mex decision. [Citation omitted.] There are no set metrics; there are no dollar caps. There is no ruler by which UP could even determine, at this later date and with full hindsight, whether a particular rate offered for one customer in 2019 for intermodal traffic between Mexico City and Kansas City is "commercially reasonable" without wild speculation.[255]

If UP could never tell, even "with full hindsight," whether a particular rate is "commercially reasonable" because the Board never established any "metrics" or "ruler," then it would be equally impossible for a shipper, an arbitrator, or the Board to enforce the identical commitment made here by Applicants.

In the Application, Applicants acknowledge the need to make "more concrete and readily enforceable" their commitment to charge "commercially reasonable rates."[256] However, they offer no concrete, enforceable proposal of their own.

UP has identified an appropriately concrete, enforceable approach: When a customer asks CPKC to provide rates for (i) CPKC service on only former-CP, former-KCS, and/or former-KCSM portions of an origin-to-destination route, and (ii) CPKC "single line"[257] service on a

[255] Ex. 19 (Applicants' Reply to UP's Motion to Compel at 12).

[256] APP Vol. 1 at 233, Brooks VS ¶ 47.

[257] The term "single-line" is used to simplify the discussion. The rule would apply even though KCSM might technically offer customers a separate Rule 11 rate for the Mexican portion of a movement that is transported north of the border by KCS, or KCS and CP. As discussed in the

"competitive"[258] route, CPKC must provide the customer with a Rule 11 rate for the former-CP, former-KCS, or former-KCSM portions that reflects a mileage-based prorate of the rate provided for the CPKC single-line service. Mr. Rocker and Professor Salop separately illustrate how such an approach would be applied.[259]

UP's proposed condition is narrowly tailored to address a specific merger-related harm identified by Applicants. It would place all the control in the hands of the shippers that the condition is intended to protect. Shipper control would ensure that the condition protects competition, not competitors:

- The ***shipper*** decides whether to request gateway rates from CPKC.
- The ***shipper***—and only the shipper—receives the gateway rates from CPKC.
- The ***shipper*** decides whether to ask other railroads for complementary Rule 11 rates to create a competitive through route.
- The ***shipper*** can easily determine whether CPKC accurately applied a mileage prorate and, if necessary, readily obtain enforcement at the Board.

By protecting competition and not competitors, UP's proposed condition embraces the dynamic nature of the railroad marketplace. CPKC is free to set rates according to its view of the market. Rates are not frozen. CPKC's Rule 11 rates will reflect CPKC's then-current judgment about commercially reasonable rates for the traffic at issue. Rates are not "equalized." CPKC is free to reduce its total rate below what other carriers can match when combining CPKC's Rule

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next note, the rule would also apply even if CPKC could not by itself provide "single-line" transportation from the origin to the destination and had to interchange with another carrier.

[258] The term "competitive" is used to mean CPKC and another railroad are competing for the same traffic, but the rule would apply even if CPKC and the other railroad did not serve the identical origin or destination facility—*e.g.*, if each serves a different intermodal facility in the same area—or if CPKC or the other railroad must interchange with yet another carrier to provide full origin-to-destination transportation.

[259] *See* Rocker/Turner VS at 20; Salop VS ¶¶ 117–19.

11 rates with their own Rule 11 rates. UP could not "cherry pick" business. CPKC would only provide a Rule 11 rate if a customer also requested a single-line rate. And the other carriers never see *any* rates provided by CPKC unless shippers choose to share them in an effort to further stimulate competition. As Professor Salop explains, this shipper-centric, market-based approach avoids the flaws of prior, discredited, gateway protective conditions.[260]

Applicants may quibble about the details of UP's proposal. They may say a mileage prorate might not precisely correspond to their costs or might not allow them to capture every last drop of efficiency benefits their transaction might create. However, UP's proposal ensures that any efficiencies CPKC does not capture will flow to shippers, not CPKC's competitors. Moreover, the prorate will only apply to a fraction of the total rate, so if CPKC can legitimately offer customers better rates and service than its railroad competitors, it will win the business.[261]

Use of a mileage prorate in this type of setting is not a novel idea. UP and BNSF agreed to a similar approach under their "I-5 Agreement" to keep the Portland Gateway open following the *UP/SP* merger.[262] UP's proposal here is more limited in objective, and thus less complicated, than the I-5 Agreement. UP's proposal applies only if a shipper decides to obtain a competitive rate from CPKC, so there is no need to develop a pre-set matrix of potential rates. CPKC would develop a new, confidential, market-based rate whenever a shipper asks for a CPKC rate and a Rule 11 interline rate, and the shipper could easily check compliance by knowing the rate and

[260] *See* Salop VS ¶ 121 (noting that "CRR is far narrower than the DT&I conditions and is formulated to preserve competition among the carriers. In particular, the CRR does not constrain the single-line rate of the merged firm; it simply bases the Rule 11 rate on the monopoly segment of the carrier's independently-determined rate." (footnote omitted)).

[261] *See generally id.*, ¶¶ 123–24.

[262] *See* Rocker/Turner VS at 22.

miles, and applying simple arithmetic.[263] UP's and BNSF's use of a mileage prorate in the *UP/SP* merger confirms use of a similar approach here would not undermine the legitimate benefits of a CP/KCS transaction.

UP has also used mileage prorates to address divisions of revenue between carriers in other settings. As Mr. Rocker explains {{

}}[264]

Also, Applicants' own documents show {

}[265] As Mr. Brooks described in his verified statement, the parties entered into the Ice Pick initiative in 2009 and carried it forward until 2012.[266] Ice Pick involved efforts to capture the same types of traffic at issue here. {

}

2. The Board Should Require CPKC to Comply with KCS's Promises Regarding Laredo Gateway Operations and the Laredo Bridge.

As discussed above, Applicants could reduce gateway competition not only by increasing rates but also by reducing service. In the Application, Applicants commit to keep gateways open physically by "maintain[ing] efficient operations serving existing gateways wherever traffic

[263] *See id.*

[264] *See id.* at 23.

[265] Ex. 7 (Brooks Tr. 66:3–14); *see also* Ex. 20 (Brooks Deposition Exhibit 8 (CP-HC-00006432–6439)).

[266] *See* APP Vol. 1 at 227–28, Brooks VS ¶¶ 30–33.

levels warrant – in terms of both the through train services to and from the gateways as well as the operational capabilities and infrastructure necessary to carry out efficient interchange."[267] Applicants also say they will "inherit and honor" operational commitments regarding the Laredo Bridge and traffic moving via the Laredo Gateway that KCS made when it acquired Tex Mex.[268]

If the Board approves the transaction, it should make CPKC's operational commitments more concrete in two ways. First, it should require CPKC to adhere to the specific commitments KCS made in *Tex/Mex.* The specific commitments (as applied to CPKC) include:

- CPKC will not change the basic structure and operations of KCSM except through negotiations. CPKC's carriers (including KCSM) will continue to cooperate closely and fairly with UP, BNSF and other rail carriers on interline services such as pre-blocking rail cars, improving automated customs pre-clearance procedures, supplying cars for shipments, accommodating run-through train service, providing excellent service, and promptly quoting rates.

- CPKC will honor the terms of all existing Tex Mex and KCSM agreements and will allow such agreements to continue to their full term and not seek to cancel them early, even if it has the legal right to do so.

- CPKC will treat all carriers fairly at the Laredo Bridge. CPKC will abide by the existing dispatching and operating practices over the Bridge, will not make any unilateral changes in the way the Bridge is dispatched and operated, and KCS, Tex Mex, and KCSM will continue to be bound by the contracts and agreements that now govern operations over the Bridge.

- CPKC will ensure safety remains a top priority with regard to CPKC operations at the Laredo Gateway.[269]

By directly requiring CP's compliance with the *KCS/Tex Mex* operational commitments, the Board would appropriately memorialize these significant commitments and avoid potential misunderstandings or confusion.

[267] *Id.* at 233, Brooks VS ¶ 45.

[268] *Id.* at 232, Brooks VS ¶ 43.

[269] *See KCS/Tex Mex*, FD 34342, slip op. at 13–14; *id.* at 18–19; *see also* APP Vol. 1 at 207, Ottensmeyer VS at 21.

Second, to make the commitments more concrete, the Board should expressly require CPKC to provide UP access to any new bridge CPKC constructs at Laredo on the same terms as it provides UP access to the existing International Bridge. As discussed above, the long-term interests of shippers using the Laredo Gateway require that CPKC continues to have an incentive to cooperate with UP with regard to service and capacity on the bridges used by the two railroads.

B. The Board Should Impose Conditions to Remedy Applicants' Failure to Address Investment in Joint Facilities.

Applicants' failure to address the impact of their planned traffic growth on capacity needs of joint facilities is a separate reason the Board could not conclude the proposed transaction is consistent with the public interest. If the Board approves the transaction despite that significant omission, it should impose conditions to ensure the transaction's implementation is in the public interest, and that CPKC cannot inappropriately force UP and other railroads—and their customers—to subsidize the transaction.

To address these issues, the Board should establish three principles governing Applicants' ability to move forward with their plans: *First*, Applicants must work with owners and users of rail lines and other facilities that would be used jointly by CPKC to identify investments in new capacity necessary to accommodate CPKC's planned traffic growth. *Second*, Applicants must commit to fund necessary investments in new capacity, with other railroads paying their fair share to the extent they use the new capacity in the future. *Third*, Applicants must commit not to increase CPKC operations on affected lines above pre-merger CP or KCS levels until the owners and users of the lines agree sufficient capacity has been added to accommodate the traffic growth. The Board would remain available to resolve disputes at any stage of the process.

UP recognizes these conditions could potentially delay implementation of the plans set forth in the Application. However, Applicants' plans are incomplete, and if Applicants begin to implement them without fully accounting for their effects, the costs will be borne by other railroads and their customers. That would not be consistent with the public interest.

VIII. Conclusion

An unconditioned combination of CP and KCS would likely cause a significant loss of competition, especially for traffic moving via the Laredo Gateway. Applicants also fail to take into account the substantial investments in new capacity required to implement their transaction. UP's proposed conditions would partially mitigate the harms that would result from approval of the transaction. If the Board does not impose UP's proposed conditions, it should deny the Application.

Respectfully submitted,

/s/ Michael L. Rosenthal

CRAIG V. RICHARDSON
JAMES B. BOLES
TONYA W. CONLEY
WHITNEY LARKIN
Union Pacific Railroad Company
1400 Douglas Street
Omaha, Nebraska 68179
(402) 544-7004

MICHAEL L. ROSENTHAL
DEREK LUDWIN
JAMES J. O'CONNELL
PRATIK AGARWAL
SAHEL SRA
Covington & Burling LLP
One CityCenter
850 Tenth Street, NW
Washington, D.C. 20001
(202) 662-6000

Attorneys for Union Pacific Railroad Company

February 28, 2022

CERTIFICATE OF SERVICE

I hereby certify that on this 28th day of February, 2022, I caused a copy of the foregoing document to be served electronically or by first-class mail, postage prepaid, on all parties of record on the service list for Finance Docket No. 36500.

/s/ Michael L. Rosenthal

BEFORE THE
SURFACE TRANSPORTATION BOARD

Finance Docket No. 36500

CANADIAN PACIFIC RAILWAY LIMITED; CANADIAN PACIFIC RAILWAY COMPANY; SOO LINE RAILROAD COMPANY; CENTRAL MAINE & QUEBEC RAILWAY US INC.; DAKOTA, MINNESOTA & EASTERN RAILROAD CORPORATION; AND DELAWARE & HUDSON RAILWAY COMPANY, INC.
—CONTROL—
KANSAS CITY SOUTHERN; THE KANSAS CITY SOUTHERN RAILWAY COMPANY; GATEWAY EASTERN RAILWAY COMPANY; AND THE TEXAS MEXICAN RAILWAY COMPANY

VERIFIED STATEMENT

OF

KENNY ROCKER

AND

JOHN TURNER

TABLE OF CONTENTS

I. Introduction And Summary 1

A. The CP/KCS Transaction Presents a Significant Threat to Competition. 2

B. Applicants Failed to Fully Address the Investments in Capacity Necessary to Implement the Transaction. 3

II. CP Control Of KCS Threatens Competition For U.S.-Mexico Rail Traffic. 4

A. The Laredo Gateway Is Critical to U.S.-Mexico Rail Transportation. 4

B. CP Control of KCS Would Harm Competition. 8

1. Shippers Benefit From Choice and Competition at the Laredo Gateway. 9

2. CPKC Would Be Incentivized to Deprive Shippers of the Price and Service Benefits of UP-KCSM Routings. 11

3. CPKC Would Be Able to Use Its Control of KCSM to Make More Efficient UP-KCSM Options Less Attractive to Customers. 12

4. The Availability of UP-FXE Routes Via Eagle Pass or Other Transportation Options Would Not Allow Shippers to Avoid the Transaction's Anticompetitive Effects. 16

C. UP's Proposed Gateway Rate Remedy and Laredo Operational Conditions Are Narrowly Tailored to Remedy the Adverse Competitive Effects of an Unconditioned Transaction. 17

1. The Gateway Rate Condition 18

2. The Laredo Gateway Service Condition 24

III. CP Control Of KCS Threatens To Impose And Shift Costs Of Implementing The Transaction On Other Railroads And Their Customers. 26

A. Applicants Failed to Evaluate the Impacts of Their Planned Operations Where They Operate Over Other Railroads. 26

B. Applicants Failed to Evaluate the Impacts of Their Planned Operations Where Other Railroads Share Applicants' Lines. 32

C. UP's Proposed Capacity Investment Condition Is Narrowly Tailored to Ensure the Proposed Transaction Is in the Public Interest. 38

VERIFIED STATEMENT

OF

KENNY ROCKER AND JOHN TURNER

My name is Kenny Rocker. I am Executive Vice President, Marketing and Sales, for UP.[1] I joined UP in 1994 and have held my current position since 2018. Since joining UP, I have held various positions of increasing responsibility in the Marketing and Sales Department, including assignments in Automotive, Chemicals, and the Market Development and Sales Center. I hold a Bachelor's degree in Finance from Tuskegee University.

My name is John Turner. I am Vice President, Network Planning and Operations, for UP. I joined UP in 1998 and have held my current position since 2020. Since joining UP, I have held various positions of increasing responsibility in the Operating Department, including time spent as Director Transportation Service, Superintendent, and General Superintendent. Immediately prior to my promotion to Vice President, I was Assistant Vice President for Network Integration and Scheduling. I hold a Bachelor's degree in Transportation and Logistics from Iowa State University and a Master's in Business Administration from the University of Notre Dame.

I. Introduction And Summary

We are submitting this statement because CP's proposal to acquire control of KCS presents a significant threat to competition for rail traffic moving between the United States and Mexico. We are also submitting this statement because Applicants appear to be expecting other railroads to pay for substantial investments in capacity that would be necessary to implement

[1] In this statement, we use the abbreviations the Board used in Decision No. 11, served November 23, 2021.

their transaction. If the Board were to authorize the proposed transaction, it must impose conditions addressing both issues.

A. The CP/KCS Transaction Presents a Significant Threat to Competition.

Many shippers rely on KCS and its Mexican subsidiary, KCSM, to cooperate with UP and BNSF to provide competitive options for traffic moving between the United States and Mexico via the Laredo Gateway. Currently, KCS has strong incentives to cooperate. KCS must cooperate with UP and BNSF to sustain and grow business on KCSM because its network in the United States has limited reach. CP, however, serves many of the same important U.S. origins and destinations as UP and BNSF. A combined CPKC would be emboldened to *force* shippers to use CPKC single-line routes, rather than *allow* them to use competitive interline routes with UP and BNSF. The proposed transaction would thus reduce the competitive options currently available to shippers at the Laredo Gateway and other gateways in the United States.

We want to be clear at the outset: UP is not opposed to increased competition for U.S.-Mexico traffic or any other traffic that could be served by CPKC. UP is concerned because Applicants' plans for CPKC suggest they would *not* compete for business simply on the merits. Applicants' plans require CPKC to divert significant volumes of traffic from both UP and BNSF using longer, less efficient routes, and without reducing rates. If CPKC could win business by making its service more efficient and attractive, UP would regard the results as procompetitive. However, UP believes CPKC would divert traffic by using methods that reduce shippers' competitive options and compel them to use inferior routes.

Applicants themselves have recognized the very real nature of the concerns the proposed transaction raises for the preservation of shippers' competitive options at gateways, including the Laredo Gateway. Attempting to address those concerns, they promise to keep existing gateways

open on commercially reasonable terms.[2] They also acknowledge that they will inherit the commitments to preserve competition via the Laredo Gateway that KCS made in 2003 when it acquired the Texas Mexican Railway (Tex Mex) and Transportación Ferroviaria Mexicana (TFM) (which is now KCSM).[3]

Applicants' commitments do not go nearly far enough. In Part II.C of this statement, we discuss conditions the Board must impose to protect competition at the Laredo Gateway and other gateways if it were inclined to approve the proposed transaction.

B. Applicants Failed to Fully Address the Investments in Capacity Necessary to Implement the Transaction.

When reviewing the Application, we noticed a significant omission: Applicants failed entirely to address the need for investment in jointly-used infrastructure that would be necessary to implement their proposed transaction. Applicants project substantial traffic growth in a three-year period. Their Application addresses the investment needed to accommodate that growth on lines owned by CP and KCS. But CPKC would also operate on lines owned by UP. For example, CPKC's route between the Laredo Gateway and Shreveport operates over approximately 250 miles of UP-owned lines between Robstown and Beaumont, Texas, including lines through the crowded Houston terminal. BNSF also uses these lines. Applicants made no attempt to address capacity improvements on UP lines that would be necessary to accommodate their planned traffic growth. Applicants also appear to have overlooked the need for additional investment on lines they own but share with UP (and BNSF), acting as if other railroads must accommodate their changes, regardless of the impact on our service and therefore our customers.

[2] *See* APP Vol. 1 at 232, Brooks VS ¶ 42.

[3] *See id.*

We do not believe the Board could conclude the proposed transaction is in the public interest without fully understanding the impacts of Applicants' plans on other carriers and their customers. If the Board authorizes the transaction, it should not allow Applicants to increase operations above pre-merger levels until they reach agreements with railroads with whom they share capacity that identify and provide for funding of investments necessary to accommodate the traffic levels projected in the Application.

II. CP Control Of KCS Threatens Competition For U.S.-Mexico Rail Traffic.

The Laredo Gateway is *critical* to U.S.-Mexico rail transportation. Shippers who rely on rail service via the Laredo Gateway benefit today from a healthy competitive environment. But CP control of KCS threatens competition for rail traffic at the Laredo Gateway.

A. The Laredo Gateway Is Critical to U.S.-Mexico Rail Transportation.

In 1996, the Board recognized that "Laredo is the principal rail gateway between the United States and Mexico,"[4] and it imposed conditions aimed at preserving effective two-railroad competition north of the border for U.S.-Mexico rail traffic moving via Laredo.[5] The Board again recognized the importance of the Laredo Gateway in 2004, when it conditioned its approval of KCS's acquisition of Tex Mex and TFM on KCS's adherence with a set of pledges to "guarantee that traffic will continue to flow fairly and efficiently at the Laredo Bridge and through the Laredo gateway."[6]

The Laredo Gateway is still the dominant rail gateway between the United States and Mexico. In 2019, rail traffic moving via Laredo accounted for approximately 54% of all rail

[4] *Union Pacific/Southern Pacific Merger*, 1 S.T.B. 233, 410 (1996).
[5] The Board granted Tex Mex extensive trackage rights over UP, allowing Tex Mex to connect with KCS at Beaumont. *See id.* at 422–26.
[6] *Kansas City S.—Control—The Kansas City S. Ry., et al.*, FD 34342 ("*KCS/Tex Mex*"), slip op. at 19 (STB served Nov. 29, 2004).

traffic (by dollar value) between the United States and Mexico.[7] Even this figure understates the importance of the Laredo Gateway. Geography plays an important role in limiting most shippers' gateway options. For example, movements between UP points in the western Unites States and points in western Mexico naturally flow via the three gateways in western Mexico: Calexico, Nogales, and El Paso. Traffic moving between points in the central and eastern United States (and Canada) and points in eastern and central Mexico cannot effectively use these western gateways.

Of the three rail gateways in eastern Mexico—Laredo, Eagle Pass/Piedras Negras, and Brownsville/Matamoros—Laredo is used by most shippers. In 2019, Laredo accounted for approximately 67% of all rail traffic (by dollar value) moving via these three gateways.[8] The primary alternative to Laredo is the Eagle Pass/Piedras Negras gateway where UP and BNSF connect with Ferromex ("FXE"). Eagle Pass accounted for 32% of rail traffic (by dollar volume) moving via the three eastern gateways in 2019.[9] Brownsville, where UP and BNSF connect with KCSM, accounted for the remaining traffic. UP uses Brownsville principally for traffic moving to points just across the border in the Mexican states of Tamaulipas and Nuevo Leon, which cannot be reached as efficiently via Laredo or other gateways.

The Laredo Gateway's high share of rail traffic is especially notable considering UP's incentives to establish alternative routes via the Eagle Pass Gateway. Over time, and especially after KCS acquired control of KCSM in 2004, UP has worked with FXE to make Eagle Pass a more attractive alternative for customers to reduce reliance on KCSM at the Laredo Gateway.

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[7] *See* Rocker/Turner workpaper "P - Bureau of Transportation Statistics Data.pdf."

[8] *See id.*

[9] *See id.*

UP has an added incentive to encourage movements over FXE: it owns a 26% passive equity interest in FXE.[10] Despite UP's incentives to promote Eagle Pass, in 2019, the Laredo Gateway's share of UP traffic moving via the Laredo and Eagle Pass gateways was 57%.[11]

Focusing on overall traffic shares also understates Laredo's importance, because the gateways handle a different mix of traffic. For certain types of traffic, Laredo's share is even higher. For traffic CPKC is primarily targeting for diversion—that is, finished vehicles, auto parts, and intermodal—the Laredo Gateway's share of UP traffic moving via the Laredo and Eagle Pass gateways is approximately 62%.[12]

In certain geographic markets, Laredo's share is even higher. As an example, Applicants plan to offer service between CP-served points in the Upper Midwest and KCSM-served points in the industrialized regions of central and eastern Mexico. Laredo handles over 90% of all UP movements from origins in Michigan and Illinois (the two largest origins for Mexican rail traffic moving on UP) to destinations in Mexico Distrito Federal and the industrialized Mexican states of San Luis Potosí and Querétaro.[13]

The Laredo Gateway's importance is mostly due to the access it provides to KCSM's network. KCSM and FXE were formed as a result of the Mexican government's decision to privatize its national rail system in the mid-1990s. KCSM was given what was referred to as the "Northeast Concession." FXE operates primarily in western Mexico. KCSM lines run from the Laredo and Brownsville gateways south into the most populous and industrialized regions of

[10] UP has no control over FXE's operations or pricing.

[11] *See* Rocker/Turner workpaper "HC - UP Mexico traffic.xlsx," tab "Gateways."

[12] *See id.*

[13] *See* Rocker/Turner workpaper "HC - UP Mexico traffic.xlsx," tab "States."

Mexico. KCSM directly serves most leading rail freight centers in Mexico, including Monterrey, Saltillo, San Louis Potosí, Querétaro, Toluca, Mexico City, and Veracruz.

A significant portion of current cross-border traffic though Laredo moves to or from points in Mexico served exclusively by KCSM. For example, KCSM has the only service to the major industrial centers of San Luis Potosí and Toluca, and the only access to many locations in Nuevo Leon. Of the more than 300,000 cars and containers that UP interchanged with KCSM in 2019, UP estimates that more than half moved between Laredo and points served exclusively by KCSM. Much of this exclusively served traffic is the finished vehicles, auto parts, and intermodal business CPKC is primarily targeting for diversion. The remainder is mostly traffic Applicants also have squarely in their sights: grain, petroleum products, chemicals, and plastics.

In addition, although KCSM and FXE both serve a number of the same Mexican points, KCSM's route has geographic advantages for movements between eastern Mexico gateways and much of eastern and central Mexico. A comparison of the KCSM and FXE routes between the border and the Valle de México region surrounding Mexico City—Mexico's largest population and consumption center—is illustrative. KCSM and FXE both can access shippers in the Valle de México through a jointly owned railroad, Ferrocarril y Terminal del Valle de México. However, FXE's route from the Mexico City area to Eagle Pass is 55% (392 miles) longer than KCSM's route to Laredo.[14] As one might expect, given the mileage difference, nearly 80% of UP's traffic between the United States and the Mexico City area moves via the Laredo Gateway.[15]

[14] *See* Rocker/Turner workpaper "HC - UP Mexico traffic.xlsx," tab "Mileage." For example, KCSM's route from Laredo to Cuautitlan is 711 miles. FXE's route from Eagle Pass to Cuautitlan is 1,103 miles. *See id.*

[15] *See* Rocker/Turner workpaper "HC - UP Mexico traffic.xlsx," tab "Mexico City."

In sum, KCSM's route structure ensures that competitive access to the Laredo Gateway will remain critical to U.S.-Mexico cross-border rail transportation.

B. CP Control of KCS Would Harm Competition.

The proposed CP/KCS transaction raises red flags that signal the transaction will cause substantial harm to competition for traffic moving over gateways, especially the Laredo Gateway.

Applicants projected a very high level of merger-related benefits to justify the hefty price CP paid to acquire KCS. They will be under tremendous most-merger pressure to produce results. Applicants will have to generate almost all the benefits from increased revenues. The end-to-end nature of their transaction means they cannot generate significant cost savings from rationalizing routes and facilities in the same ways seen in many prior rail mergers. In addition, Applicants' growth projections rely to a large extent on attracting entirely new traffic to the CPKC system—for example, through explosive growth of international intermodal traffic at the Port of Lázaro Cárdenas, and through conversion of truck traffic to rail intermodal traffic.

As a result of these factors, CPKC will aggressively leverage revenue from the one source largely under its control: traffic moving over the Laredo Gateway. In fact, Applicants have projected diverting substantial amounts of traffic from UP-KCSM and BNSF-KCS-KCSM interline routes. If CPKC could divert that traffic by competing with UP and BNSF on the merits, UP would not object. However, Applicants presented no plan for competing on the merits. They say they do not plan to reduce rates. They acknowledge their routes for this traffic will be longer than existing routes. Their only option is using their control of KCSM to *force* traffic to use the CPKC network north of the border—that is, to undermine the competitive options currently available to shippers.

1. Shippers Benefit From Choice and Competition at the Laredo Gateway.

Today, shippers using cross-border rail service via the Laredo Gateway generally have at least two competitive options for the portion of the movement within the United States. UP and BNSF participate in interline movements with KCSM (in BNSF's case, via KCS and, to some extent, via KCSM at the Brownsville Gateway) and compete against each other north of the border. UP and BNSF also interchange cross-border traffic with carriers serving the Eastern United States and Canada to provide competition to points they do not serve directly. In some cases, shippers also have the option to use KCS's network in the United States.

When UP and BNSF compete, each relies on KCSM to handle its traffic between the border and points in Mexico. UP and BNSF traffic moving between KCSM's Sanchez Yard, located just south of the border, and points in Mexico is typically handled in the same train, ensuring equitable treatment. KCSM and UP have cooperated on a wide range of operational matters to provide efficient cross-border transportation offerings to customers, including directional handling of empties and coordination of operations at the Laredo Bridge. KCSM and UP have also worked together on projects to streamline the border crossing process, such as data exchange for blocking and customs purposes. KCSM has also helped UP support customer requirements though the supply of railcars and other services. UP understands that KCSM has coordinated on similar matters with BNSF. Untethered to CP, KCSM has powerful incentives to cooperate with both UP and BNSF on these and other operational matters.

Shippers also benefit from competition for traffic moving via the Laredo Gateway. Most UP cross-border traffic moves under what are referred to as "Rule 11" rates. {{

}} When a shipper requests Rule 11 rates, each carrier participating in an interline route provides the shipper with a confidential rate offer for its portion of the movement. UP and BNSF thus compete to provide service in the United States through their rates and by addressing non-price factors important to the customer, such as transit time, equipment supply, or reliability. KCSM's rates for its portion of the move are constrained by its concern that the combined price might exceed what the customer is willing to pay, and its lack of detailed knowledge about conditions in U.S. markets that are not served by KCS.

UP believes some shippers may not be experiencing the full benefit of competition at the Laredo Gateway. UP believes KCSM may set rates to discourage shippers from using UP, or to earn extra revenue when shippers use UP, where KCS can offer a viable single-line alternative. We never actually know what Rule 11 rates and single-line rates KCS/KCSM offers customers, and many shifting factors can affect railroad ratemaking, which makes discrimination extremely difficult for a customer to detect, much less prove.[16]

Currently, KCS's incentive and ability to engage in anticompetitive strategies are limited. For nearly all UP's cross-border traffic, KCS provides less efficient routes north of the border. KCS has apparently concluded that its interests are best served by setting rates for KCSM-UP traffic to build business on KCSM. CP control of KCS would not make potential CP/KCS routes any more efficient—in fact, Applicants admit that CPKC routes would be, *on average*, 217 miles longer than existing routes for traffic they want to divert.[17] But CP's acquisition of KCS would change the balance of incentives, emboldening CPKC to adopt strategies that would expose a

[16] We recognize KCS/KCSM may technically offer customers a KCSM Rule 11 rate and a KCS Rule 11 rate and bill separately for the portions of the movement in Mexico and in the United States. To simplify our discussion, we refer to the total KCS/KCSM rate as a "single-line" rate.

[17] *See* APP Vol. 2 at 132, Brown/Zebrowski VS ¶ 30.

substantial amount of additional cross-border traffic to anticompetitive conduct and coercive outcomes for customers.

2. CPKC Would be Incentivized to Deprive Shippers of the Price and Service Benefits of UP-KCSM Routings.

Applicants' plans for CPKC traffic diversions show how significantly CPKC's incentives and opportunities to engage in anticompetitive conduct will differ from KCS's incentives today. Unlike KCS, CP serves the locations in the Upper Midwest where large volumes of U.S.-Mexico traffic originate or terminate, including Chicago and Detroit. A CP/KCS combination would give the merged railroad what neither CP nor KCS has today: the possibility of capturing all the profits on large volumes of rail traffic moving between the United States and Mexico.

CPKC's motivation to divert traffic to the merged system is undeniable. Applicants say CPKC would target for diversion the hundreds of thousands of carloads of finished automobiles and containers of intermodal freight currently moving between the Mexican border and points in the Upper Midwest and Canada on UP and BNSF, as well as thousands of cars of other cross-border traffic currently moving in interline service with KCSM. Before the proposed transaction, KCSM's incentive was to work with both UP and BNSF to offer shippers competitive options for moving this business. If CP acquired control of KCS, CPKC's would seek to divert as much of the volume as possible to CPKC single-line service to collect all the profits or make shippers pay CPKC extra if they use interline service with UP or BNSF. By increasing the costs of UP-KCSM and BNSF-KCS-KCSM options, or making those options less attractive from a service perspective, CPKC would be able to enhance its profits in ways detrimental to shippers. In shifting traffic to CPKC, allowing the merged carriers to earn additional profits north of the border, CPKC would deprive shippers of efficient UP-KCS service they enjoy today, and allow CPKC to increase its own rail rates to reflect the cost penalties it imposes on UP.

3. CPKC Would be Able to Use Its Control of KCSM to Make More Efficient UP-KCSM Options Less Attractive to Customers.

Continued competition for U.S.-Mexico traffic moving via the Laredo Gateway depends on KCSM's continued cooperation in providing competitive interline rates and service for traffic moving between Laredo and points in Mexico served by KCSM. If CP acquired control of KCS, CPKC could readily make UP-KCSM options that compete with CPKC routes less attractive to shippers by raising the costs of those options or reducing cooperation on service.

a) Anticompetitive Rate-Based Strategies

KCSM's rates are probably the most important factor in preserving competition at the Laredo Gateway. UP could have the most efficient routes north of the border, receive equal treatment at the Laredo Bridge, and have its traffic treated fairly in Mexico, but if the rates KCSM charges shippers for UP-KCSM movements are too high, shippers would lose the benefits of UP competition.

If CP acquired control of KCS, CPKC would have the power to manipulate KCSM's rates to make competing UP-KCSM service more expensive for shippers, forcing them to switch to less desirable CPKC offerings, or at least causing them to pay more to CPKC if they continued using UP-KCSM service.

A simple example helps illustrate how such a strategy might work: suppose that before CP gained control of KCS, KCSM provided a customer a Rule 11 rate from an origin in Mexico to the Laredo Gateway of $100, and UP and CP both serve the destination. UP has an efficient route and provides the customer a Rule 11 rate from Laredo to the destination of $100. KCS and CP could move the traffic via a longer, slower route with an interchange in Kansas City, but the customer prefers the KCSM-UP route, even assuming that the total rate for each alternative

would be the same. (In reality, the total price for the less efficient route would almost certainly be higher.)

After the transaction, CPKC could try to divert the traffic by raising KCSM's Rule 11 rate to $110, while offering the customer a single-line rate of $200. The customer would then have to choose between accepting the less preferred CPKC route to avoid a rate increase, or paying an additional $10 to KCSM to continue using UP. Either way, CPKC would generate more revenue—by diverting the entire movement and gaining $100 or by gaining an extra $10 for providing the same interline service it provides today. And either way, the shipper would lose—by losing its preferred routing or by paying an extra $10 for the exact same service it receives today.

Our understanding is that CPKC would have a great deal of latitude to increase KCSM's Rule 11 rates to implement anticompetitive rate-based strategies. Within the experience of UP's Mexico Group, statutory maximum rates published by the Mexican government are so high they are essentially unusable. We also understand that, at least in theory, Mexican law includes certain rate antidiscrimination principles, but we are not certain whether they require equal treatment of Rule 11 and single-line rates for cross-border traffic. In any event, CPKC could simply cause KCSM to raise rates for all similar traffic moving between Laredo and points in Mexico, then offset those increases by as much as necessary to attract traffic by reducing the portion of the rate assigned to CPKC north of the border. For shippers with better access to other transportation options, such as truck or barge, CPKC could offer even lower rates by reducing its factor north of the border by a greater amount. For traffic that UP could efficiently route via Eagle Pass in conjunction with FXE, CPKC may decide its best strategy would be to continue cooperating with UP so KCSM can keep its existing Mexican portion of the revenue. But for

significant amounts of traffic moving via the Laredo Gateway, shippers will be pressured to divert their business to CPKC.

CPKC's implementation of such a strategy would hurt shippers and competition, not just UP. CPKC would not be shifting $10 from UP's pockets to CPKC's pockets. In our example, the shipper is forced to choose between (i) receiving inferior service, and (ii) paying more to KCSM while paying the same amount to UP. As we explained above, use of Rule 11 pricing stops KCSM from extracting every last dollar of revenue that might be available due to its market power. As part of a combined CPKC, CP and KCSM would no longer be charging Rule 11 rates for the alternate route. Their additional insight into each other's costs and pricing for the movement, and their combined knowledge regarding the customer's specific circumstances and demand factors, would allow KCSM to more effectively differentiate among customers and better exploit its market power within Mexico.

b) Anticompetitive Service-Based Strategies

Although rate-based strategies would provide the most direct opportunities for CPKC to force traffic diversions, CP control of KCS would also provide opportunities to divert traffic by making UP-KCSM transportation offerings more costly or less attractive in other ways. As explained above, today's competitive UP-KCSM service is built upon, and continues to depend upon, cooperation between the two carriers on a wide variety of operational matters. KCSM would have radically different incentives with respect to cooperation as part of CPKC.

CPKC's potential strategies for making KCSM-UP service less attractive would be as broad and as simple as reducing the high level of cooperation that exists today. With regard to operational cooperation, KCSM could give lower priority to trains carrying UP traffic, especially relative to trains carrying only CPKC traffic. KCSM could deprioritize last-mile service—spotting empty equipment and pulling loaded cars—when traffic is coming from shippers who

use UP service north of Laredo. As we discussed above, KCSM currently has strong incentives to provide excellent service to expand its overall business and because UP traffic is handled on the same trains as its other traffic. However, if CPKC increased its Mexico business as projected, it would be moving more trains with only CPKC traffic and would not have the same interest in providing high quality service for customers choosing UP, rather than CPKC north of Laredo.

CPKC could also reduce competition by giving preferential treatment to its own traffic moving over the International Bridge at Laredo. KCS controls the bridge through its ownership of Tex Mex and KCSM. Operations over the bridge are governed by a 1951 agreement between Tex Mex and a UP predecessor. The agreement provides general terms about Tex Mex's obligations to perform service "impartially," and with "no preference . . . to movements of cars by one of the parties."[18] UP and KCS have implemented the agreement by establishing alternating directional "windows" for moving trains over the bridge. Applicants have indicated they may want to change the current process.[19] UP is always willing to reduce operational delays and improve capacity at the bridge. However, changes to operations that would permit a more subjective interpretation of Tex Mex's contractual obligation must be carefully addressed by the parties to ensure they would not create opportunities to restrict UP's use of the bridge in ways that would harm UP's customers.

Any of these steps would degrade the competitive rail transportation options that shippers enjoy today. Applicants claim that "cooperating with UP at Laredo . . . will be in the self-interest

[18] *See* Rocker/Turner workpaper "C - International Bridge Agreement.pdf."

[19] *See* APP Vol. 2 at 317, OP Plan ¶ 162.

of the CP/KCS system."[20] However, they make clear throughout their Application that their interests lie in diverting traffic from UP-KCSM service to CPKC single-line service.

4. The Availability of UP-FXE Routes Via Eagle Pass or Other Transportation Options Would Not Allow Shippers to Avoid the Transaction's Anticompetitive Effects.

In reviewing the Application, we did not see any detailed discussion about transportation options available to shippers served by KCSM. A substantial number of shippers currently using UP-KCSM service do not have viable intramodal or intermodal alternatives to KCSM service in Mexico. If CPKC tried to divert their traffic by raising KCSM-UP rates or degrading KCSM-UP service, they would have no choice but to pay more, shift their business to CPKC, or both.

UP-FXE service does not provide a competitive option for most of the traffic targeted by Applicants. As we discussed above, more than half of UP-KCSM traffic moves between Laredo and points in Mexico served exclusively by KCSM. Additional traffic moves on UP-KCSM routes to or from points served by both FXE and KCSM where FXE lacks an efficient route to the border. FXE's ability to provide some shippers with competitive options would not protect the large number of shippers without similar options.

In addition, truck and water service are not viable options for the overwhelming majority of traffic Applicants say they will target for diversion to CPKC. Applicants said almost nothing of substance regarding non-rail options for the traffic they will target, and we agree with the only factual statement we saw: "many of the commodity flows in these lanes—like LPG, grain, finished autos, and others—are not well suited to long-distance movement by truck."[21] The only other statement we noted was the substance-free claim that "if the combined CP/KCS tried to

[20] APP Vol. 1 at 232, Brooks VS ¶ 43.

[21] APP Vol. 1 at 226, Brooks VS ¶ 26.

raise rates on KCSM movements that are not rail dependent, the traffic would shift to motor or water carriage."[22] Much of the traffic moving in UP-KCSM service, especially the traffic targeted by Applicants, *is* rail dependent, so motor and water carriage *are not* viable options.

For example, truck is not a viable option for finished automobiles moving from Mexico to the United States. Water transport is an option for some automobiles manufactured near ports and moving to the East Coast. But for finished automobiles moving from Mexican locations to U.S. points that are not on the coast, rail is the only option. As another example, truck can be an attractive option for shippers and receivers of relatively small quantities of auto parts—typically parts moving to a third-party supplier in Mexico. However, for large volume shipments moving directly from parts manufacturers or consolidation centers in the Upper Midwest and East to automobile manufacturers in Mexico, the economics of boxcar and intermodal service are vastly superior to truck service. Many other shippers also rely on rail to transport products to inland points in Mexico in volumes that make trucking inefficient, including shippers of petroleum products, soda ash, grain, steel, and specialized minerals (like ball clay and specialized sand). Again, the fact that some shippers might have truck and water options does not protect large number of shippers dependent on KCSM.

C. UP's Proposed Gateway Rate Remedy and Laredo Operational Conditions Are Narrowly Tailored to Remedy the Adverse Competitive Effects of an Unconditioned Transaction.

Applicants recognize there are valid concerns about the adverse effects of their proposed transaction on competition for traffic moving over gateways, particularly the Laredo Gateway. However, Applicants' proposed solutions are not sufficient to protect against potential harms—as they themselves appear to acknowledge. Applicants commit to keeping the Laredo Gateway

[22] APP Vol. 1 at 208, Ottensmeyer VS at 22.

and other gateways "open," both physically and commercially, but key elements of those commitments are vague, ephemeral, and essentially unenforceable.

UP urges the Board to condition any approval of the transaction on CPKC's use of a concrete, enforceable pricing methodology to ensure the Laredo Gateway and other gateways remain commercially "open." Specifically, when CPKC provides a Rule 11 rate to a gateway at the request of a shipper, the rate should reflect a mileage-based prorate of the rate offered to the shipper for CPKC "single-line" service.[23] As we explain below, UP's proposed approach would allow CPKC to compete vigorously for new business and pursue whatever efficiencies it might obtain as a result of the transaction, while preserving competition for traffic moving over gateways, including the Laredo Gateway.

UP also urges the Board to impose on CPKC the operational commitments relating to the Laredo Bridge and Laredo Gateway undertaken by KCS when it acquired Tex Mex. This would help avoid potential disputes about what it means for CPKC to "inherit" KCS's commitments. As we also explain below, the Board should make clear the commitments apply to operations over any new bridge at Laredo.

1. The Gateway Rate Condition

Applicants recognize their promise to keep gateways open is meaningless if the rate they set for their portion of an interline movement is too high for interline service to be competitively viable. They try to address the concern by promising that the rates and terms they establish will

[23] We put "single-line" in quotes because we recognize that CPKC might technically offer customers a KCSM Rule 11 rate and a CPKC Rule 11 rate and bill separately for the portions of the movement in Mexico and in the United States. To simplify our discussion, we refer to the total CPKC/KCSM rate as a "single-line" rate.

be "commercially reasonable.[24]" However, they never define what it means for rates to be "commercially reasonable." Instead, they say they will try to "find ways to make these commitments more concrete and readily enforceable."[25]

We understand the problem. We are not aware of any mechanical definition of what it means for a rate to be "commercially reasonable." It is not a concept UP uses in pricing traffic. None of UP's contracts call simply for rates that are "commercially reasonable." Railroads and customers operating in good faith may well disagree about whether a particular rate is appropriate in light of market circumstances.

If the Board were to approve the transaction, however, the Board would need to define in *concrete* terms the maximum amount CPKC can charge for their portion of an interline route via a gateway. Applicants' promise would be meaningless if it is not enforceable.

Applicants plainly recognize their promise to charge "commercially reasonable" rates is illusory and unenforceable. We understand that when UP tried in this proceeding to test whether KCS was complying with the commitment it made when it acquired Tex Mex to charge "commercially reasonable" rates, Applicants told UP such efforts amounted to "wild speculation" because the Board never established any "metrics" or "ruler" to determine whether a particular rate was "commercially reasonable":

> The Board did not define "commercially reasonable" in its 2004 Tex Mex decision. [Citation omitted.] There are no set metrics; there are no dollar caps. There is no ruler by which UP could even determine, at this later date and with full hindsight, whether a particular rate offered for one customer in 2019 for intermodal

[24] APP Vol. 1 at 232, Brooks VS ¶ 42.

[25] *Id.* at 233, Brooks VS ¶ 47.

> traffic between Mexico City and Kansas City is "commercially reasonable" without wild speculation.[26]

If Applicants' view is that UP could not, even "with full hindsight," address whether a particular rate is "commercially reasonable," how is a customer, or an arbitrator, or the Board expected to be able to enforce the commitment made here by Applicants?

UP urges the Board to adopt a simple, straightforward approach to defining for purposes of this proceeding what it means for a rate to be "commercially reasonable": When CPKC provides a Rule 11 rate to a gateway at the request of a shipper, the rate should reflect a mileage-based prorate of the rate CPKC provides for its portion of a competing route.

Here is how the prorate would work: a customer wants to ship finished automobiles from Toluca to Chicago. KCSM serves the facility in Toluca; UP and CP have different but competing auto facilities in Chicago. KCSM's route between Toluca and Laredo is approximately 760 miles long. The KCS-CP route between Laredo and Chicago is approximately 1,400 miles long. CPKC provides the customer a single-line rate of $3,000 (net of refunds, rebates, allowances, ancillary charges, etc.), and the customer requests a Rule 11 rate from Toluca to the Laredo Gateway.[27] To calculate the "commercially reasonable" Rule 11 rate, CPKC would simply calculate its mileage-based share (760 miles of a total 2,160 miles) of the total revenue, resulting in a Rule 11 rate of $1,056 ($3,000 x (760 ÷ 2,160)). CPKC would tell the shipper (a) the CPKC miles for both parts of the route (Toluca-Laredo; Laredo-Chicago) and (b) the Rule 11 rate. The customer could then ask UP for its Rule 11 rate from Laredo to Chicago, and decide whether the CPKC rate from Toluca to Chicago provides better overall value than the combination of Rule 11 rates.

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[26] *See* Rocker/Turner workpaper "P - Applicants' Reply to UP's Motion to Compel.pdf."

[27] As noted above, we recognize CPKC might technically offer customers separate KCSM and CPKC Rule 11 rates, but we refer to the total rate offered to the shipper a "single-line" rate to simplify our discussion.

UP's proposed approach is concrete, enforceable, and gives complete control of the process to shippers. The condition is designed to protect shippers, not the railroad competitors of CPKC. The shipper decides whether to even request a gateway rate from CPKC. The shipper (and only the shipper) receives the gateway rate from CPKC. The shipper decides whether to request a Rule 11 rate from another railroad. And the shipper can readily determine whether CPKC accurately applied the mileage prorate and seek to enforce the condition, if necessary—if the shipper has any questions about mileages, it can always ask the competing railroad (or seek out one the many railroad pricing consultants with access to rail mileage data).

UP's condition would not undermine Applicants' incentives to pursue whatever pro-competitive benefits might arise from combining CP and KCS. UP's condition would allow the market to determine the commercially reasonable rate. CPKC would be free to set rates based on to its view of the market and change its rates at any time as market conditions allow. In other words, CPKC's rates would not be frozen.

UP's condition would not produce "equalized" rates. CPKC would have a strong incentive to improve its efficiency and reduce costs. If CPKC is more efficient or willing to accept lower margins than its railroad competitors, CPKC could reduce its single-line rate below what others could match in setting their own Rule 11 rates. In most cases, CPKC's Rule 11 rate would account for only a small portion of the total move. As a result, if CPKC could legitimately offer customers better rates and service than its railroad competitors, it would win the business.

UP's condition also would not allow competitors to "cherry pick" attractive business. CPKC would not be required to establish free-standing Rule 11 rates. CPKC would only provide Rule 11 rates after a customer requests a CPKC single-line rate, so CPKC would know about all potential business opportunities. The competitor railroad would only know about the business if

the customer seeks an alternative to CPKC. The competitor would never be entitled to learn what single-line rate or what Rule 11 rate CPKC quoted a particular customer.

Use of a mileage-based prorate in this type of setting is not a novel idea. UP and BNSF agreed to a similar approach under their "I-5 Agreement" to keep the Portland Gateway open following the *UP/SP* merger. In that merger, UP sold BNSF a line in northern California that created a new BNSF single-line route between the Canadian border and the U.S. Southwest (the so-called "I-5 Corridor"). However, the railroads recognized that BNSF would no longer have incentives to work with UP on an interline basis via the Portland, Oregon gateway for traffic moving between BNSF points north of Portland and points served by UP and BNSF south of Portland. BNSF and SP had previously cooperated closely on such movements. To preserve a UP-BNSF interline option as an alternative to BNSF single-line routes, the parties essentially use a mileage-based prorate of BNSF single-line rates to develop and update a rate factor that UP can use to offer UP-BNSF interline service.[28] UP's and BNSF's agreement to a mileage-based prorate approach in the *UP/SP* merger demonstrates that use of a mileage-based prorate here would not undermine the benefits of a CP/KCS transaction.

UP's proposal here is much more limited in objective, and thus much less complicated, than the actual I-5 Agreement. UP's proposal applies only if a shipper decides to obtain a single-line rate from CPKC, so there is no need to develop a detailed matrix of rates or a system of third-party audits to ensure compliance. CPKC would develop a new, confidential, market-based rate whenever a shipper asks for a single-line rate and a Rule 11 interline rate, and the shipper could readily check compliance by knowing the rates and miles, and applying simple arithmetic.

[28] *See* Rocker/Turner workpaper "HC - I-5 Agreement.pdf."

UP has also used mileage-based prorates to address divisions of revenue between carriers in other settings. {{

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Although Applicants provide no concrete guidelines for setting rates at a "commercially reasonable" level, they identify *when* they would offer shippers "commercially reasonable" rates. They say they will provide a shipper with a Rule 11 rate to a gateway "when a customer requests a rate for only the former-CP or former-KCS portion of an origin-to-destination routing."[29] As we understand Applicants' position, CPKC would provide a Rule 11 rate whenever CPKC would move traffic over a route that includes some combination of premerger CP, KCS, and KCSM lines, and when a competitor railroad (or a combination of competitor railroads) could move the same traffic using an interline route that includes portions of the premerger CP, KCS, and/or KCSM. Thus, for example, the commitment would apply in the example discussed above, where CPKC and another railroad compete by serving facilities in the same area (*e.g.*, intermodal ramps, auto ramps, transloading facilities), even if both railroads do not serve precisely the same facility. As another example, the commitment would apply when multiple railroads interline to compete with CPKC, such as when UP interlines with CSXT or NS to move traffic to the East in

[29] APP Vol. 1 at 233, Brooks VS ¶ 46.

competition with CPKC (or CPKC and NS or CSX). As still another example, the commitment would also apply when a customer wants to move traffic between Mexico and the Meridian Speedway via the Laredo Gateway, and the choice is between a KCSM-UP routing and a KCSM-KCS routing. UP also understands Applicants' commitment would apply when CPKC would eliminate a bridge movement provided by another railroad—for example, when UP would need to interline with KCSM at Laredo and CP at St. Paul for traffic moving between Mexico and Canada.

If our understandings are correct, Applicants would apply a remedy to the right traffic—but a more concrete condition is needed to make the remedy meaningful and enforceable. UP's mileage-based prorate proposal would be an appropriately concrete, enforceable condition.

2. The Laredo Gateway Service Condition

Applicants recognize the same anticompetitive incentives that could lead them to foreclose competition by manipulating KCSM rate factors could also lead them to foreclose competition by reducing the quality of service or cooperation KCSM provides on interline movements. Applicants have committed to keep gateways open by continuing "to maintain efficient operations serving existing gateways wherever traffic levels warrant—in terms of both the through train services to and from the gateways as well as the operational capabilities and infrastructure necessary to carry out efficient interchange."[30] Applicants also say they will "inherit and honor" the specific operational commitments regarding the Laredo Bridge and traffic moving via the Laredo Gateway that KCS made when it acquired Tex Mex.[31]

[30] APP Vol. 1 at 233, Brooks VS ¶ 45.

[31] *Id.* at 232, Brooks VS ¶ 43.

CPKC's operational commitments would be sufficiently concrete and enforceable with two minor additions. First, the Board should expressly condition any approval of the proposed transaction on CPKC's adherence to the specific commitments KCS made in *KCS/Tex Mex*. A condition holding CPKC to its commitment to honor KCS's pledges would be unnecessarily confusing and could potentially lead to future disputes. Also, imposing an express, direct condition would drive home the significance of those commitments.[32]

Second, the Board should make one application of those commitments more concrete. In general, UP believes the operational conditions are clear enough to provide a basis for resolving any disputes that may arise in the future, without unreasonably confining CPKC's flexibility to respond to changing circumstances. However, one aspect of the conditions can and should be made more concrete: ensuring UP's access to any new bridge constructed at Laredo. In 2021, KCS received a Presidential Permit authorizing construction of a second international railroad bridge adjacent to the existing International Bridge in Laredo.[33] KCS and UP have been engaged in constructive discussions about the project. UP expects constructive engagement to continue if the Board approves the proposed transaction. However, for the reasons discussed above, access to the Laredo Gateway is too important to be subject to uncertainty and potential anticompetitive actions. If the Board approves the proposed transaction, it should require CPKC to provide UP access to any new railroad bridge constructed in Laredo on the same terms as UP's access to the existing bridge.

[32] *See* Rocker/Turner workpaper "C - Brooks Deposition Excerpt.pdf."

[33] *See* Rocker/Turner workpaper "P - Presidential Permit.pdf."

III. CP Control Of KCS Threatens To Impose And Shift Costs Of Implementing The Transaction On Other Railroads And Their Customers.

When we reviewed the Application, particularly the Operating Plan, we were surprised by what we did *not* see: Applicants barely discuss the impacts of their proposed transaction on lines and other critical facilities they share with other railroads. Applicants identify additional infrastructure necessary to support projected traffic growth on lines owned by CP and KCS. They describe the new investments needed to ensure their lines continue to "operate fluidly" as one of their "highest priorities."[34] But Applicants never address the new capacity that would be needed to support their projected traffic growth on the lines of other railroads—particularly UP. Nor do they commit to paying for the capacity needed to ensure their transaction does not impair fluid operations on lines owned by other railroads, much less commit to making the issue one of their highest priorities. Applicants also appear to disregard the capacity needs of other railroads operating on lines owned by KCS and CP that would experience significant traffic growth as a result of the proposed transaction. In these circumstances, the Board could not conclude the proposed transaction is in the public interest.

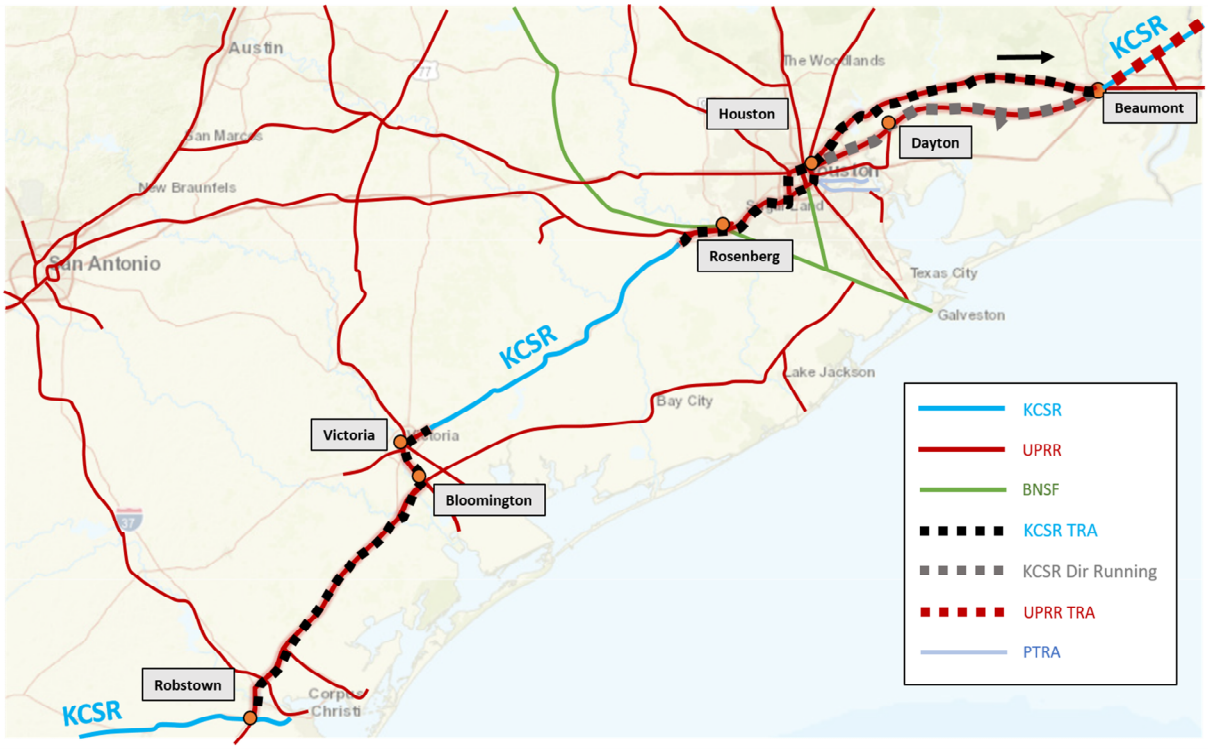
A. Applicants Failed to Evaluate the Impacts of Their Planned Operations Where They Operate Over Other Railroads.

Applicants' failure to address the impacts of their proposed transaction on joint railroad facilities is a major omission from their Application. Applicants share lines and terminal areas with other railroads all along their North-South corridor in the United States. Most significantly, KCS operations between the Laredo Gateway and the center of its hub-and-spoke operations in Shreveport, Louisiana, require use of approximately 250 miles of trackage rights over UP's lines

[34] APP Vol. 2 at 340, 344, OP Plan ¶¶ 238, 244.

between Robstown and Beaumont, Texas, including rights to operate through the crowded Houston terminal area, as shown in the figure below.

Figure 1: Texas Area KCS Trackage Rights



Applicants' post-merger plans depend critically on their use of the Robstown-Beaumont trackage rights over UP. The trackage rights are an essential link in Applicants' route between Mexico and the United States. Applicants project they will more than double KCS's current use of the lines. At the southern end of the trackage rights, from Robstown to Victoria, CPKC traffic will increase from 7.7 trains per day to 16.8 trains per day, an increase of 9.1 trains per day, or 118%.[35] On the northern portion, from Rosenberg through Houston to Beaumont, CPKC traffic will increase from 7.7 trains per day to 16.0 trains per day, an increase of 8.3 trains per day, or

[35] APP Vol. 2 at 364, OP Plan, App. A at 1.

108%.[36] Applicants do not identify any plans to invest in new capacity on any of the trackage rights lines between Robstown and Beaumont.[37] However, accommodating the traffic growth projected in the Application would require new capacity on many or all of these lines.

Robstown/Corpus Christi to West Junction. We can only conclude Applicants never studied the need for additional capacity on the trackage rights lines. Accommodating CPKC's projected traffic growth would require adding substantial new capacity on UP's lines between Robstown and Victoria and between Rosenberg and West Junction in Houston.

On the Robstown-Bloomington segment of UP's lines between Robstown and Victoria, KCS trains must share capacity with UP trains travelling between Houston, Corpus Christi, and Brownsville, and with BNSF trains moving between Houston and Robstown, where BNSF and KCS interchange Laredo Gateway traffic. UP's line between Rosenberg and West Junction is part of UP's Glidden Subdivision, which runs between San Antonio and Houston. The Glidden Subdivision is an important link in UP's Sunset Route between Southern California and New Orleans, and the Rosenberg-West Junction segment is also used by BNSF and Amtrak trains moving to and from Houston.

Currently, capacity on these lines is just sufficient to accommodate the multiple users. Over the past several years, UP has worked cooperatively with KCS to expand capacity on these lines. Since 2015, as part of an agreement with KCS, UP designed and constructed a new 9,595-foot siding near Rosenberg, a 10,100-foot siding at Placedo, Texas, extended its existing Greta and Inari sidings to 10,000-feet, constructed new run-around track at Sinton, Texas, and added Centralized Traffic Control ("CTC") between Robstown and South Odem, and between Victoria

[36] *Id.*

[37] APP Vol. 2 at 337, OP Plan ¶ 231, Fig. 11.

and Placedo. In the same timeframe, UP also constructed the 10,400-foot Cranell siding. UP is currently planning to construct a new 15,000-foot siding called the Linn siding.

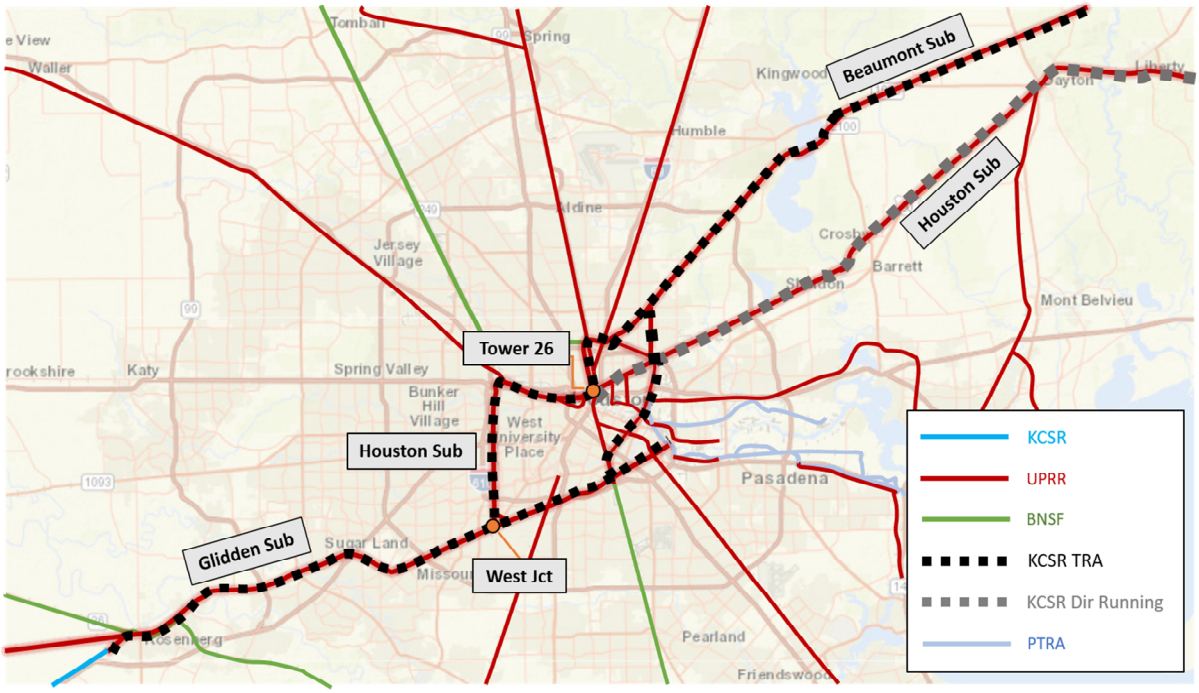
UP's recent and planned expansions of capacity on the trackage rights lines will not be enough to accommodate Applicants' additional traffic. Applicants plan to add eight or nine trains per day on the lines, more than doubling KCS's current use. To put the issue into perspective, the list of projects described above added three or four trains per day of capacity between Robstown and West Junction. Applicants would be adding new, unanticipated traffic. The additional traffic would not be offset by reductions in UP traffic, even if Applicants divert Mexico business from UP. UP moves Laredo Gateway traffic via San Antonio on routes that avoid adding congestion to the Houston terminal area. Applicants will be routing the new trains through Houston.

Houston terminal area. Applicants also fail to address the impact of their projected new traffic on operations in the Houston terminal. Houston is an extremely challenging rail operating environment, even when everything is running smoothly. Operations must be carefully coordinated among UP, BNSF, KCS, Amtrak, and the Port Terminal Railroad Association (PTRA). Time and again, UP has seen how congestion in one part of Houston can rapidly spread throughout the terminal and then across its network. UP devotes a substantial amount of time and attention to planning and executing our operating plan in Houston to prevent local and broader network issues from developing.

KCS has extensive trackage rights in Houston, allowing it to participate in the generally directional flow of traffic through the terminal and interchange traffic with the PTRA. As shown in the figure below, KCS has rights over UP's Houston Subdivision between West Junction and Tower 26, then over the West Belt, which provide KCS access to UP's Beaumont Subdivision. UP, BNSF, and KCS all use the Beaumont Subdivision for traffic moving eastbound towards

Beaumont. Amtrak uses the Beaumont Subdivision for its Sunset Limited train. KCS also has rights from the Beaumont Subdivision directly past UP's Settegast Yard on the East Belt, which connect to KCS's rights on the Glidden Subdivision. UP has also granted KCS rights to move traffic westbound on UP's Houston Subdivision, which runs past UP's Englewood Yard towards Tower 26. This provides UP's dispatchers options to move trains through Houston as efficiently as possible.

Figure 2: Houston-Area KCS Trackage Rights



Applicants plan to add more than eight trains per day to the mix, which could increase train counts on already crowded lines by 25% or more. But Applicants say nothing about how their additional trains will affect operations in Houston. They appear not to have even considered the problem. They make no commitment to invest in the capacity necessary to accommodate their expansion of service. They apparently plan simply to increase their operations and let others address the consequences. We noted that CP's Executive Vice-President Operations, Mark Redd,

was recently quoted as saying, "you can get through Houston pretty quick."[38] That is not true in our long experience with Houston, and his glib statement suggests CP does not fully appreciate the complexities of rail operations in the Houston terminal.

Additional capacity would be needed at several locations in Houston to prevent Applicants' planned jump in traffic from endangering operations in the terminal. UP has not begun to study how to most effectively mitigate the additional demands CPKC's plans would place on operations in Houston. We know from experience, however, that the terminal could not sustain the pressure of an additional eight trains per day—which would equal record volumes—on a constant basis, especially while also addressing normal surges and disruptions. Authorizing such a dramatic growth in train traffic in one of the most sensitive rail operating environments in the country without any plan or commitment to invest in new capacity would be irresponsible.

Applicants' additional trains will also impair service on the eastern end of the Houston terminal. On the eastern end, KCS has trackage rights on UP's Beaumont Subdivision and UP's Houston Subdivision between Houston and Beaumont. BNSF also uses those two lines to move its own traffic between Houston and New Orleans, and as noted above, Amtrak's Sunset Limited train operates over the Beaumont Subdivision. These two lines are fluid at current traffic levels, but both would be at or above their limit if Applicants' traffic in this corridor grows by more than eight trains per day, as is Applicants' plan.

* * *

Applicants' plan to double their train operations between Robstown and Beaumont in just three years would make addressing capacity issues even more challenging. We question whether it would be possible to complete the analysis, design, planning, permitting and construction

[38] *See* Rocker/Turner workpaper "P - Rail Group Interview.pdf."

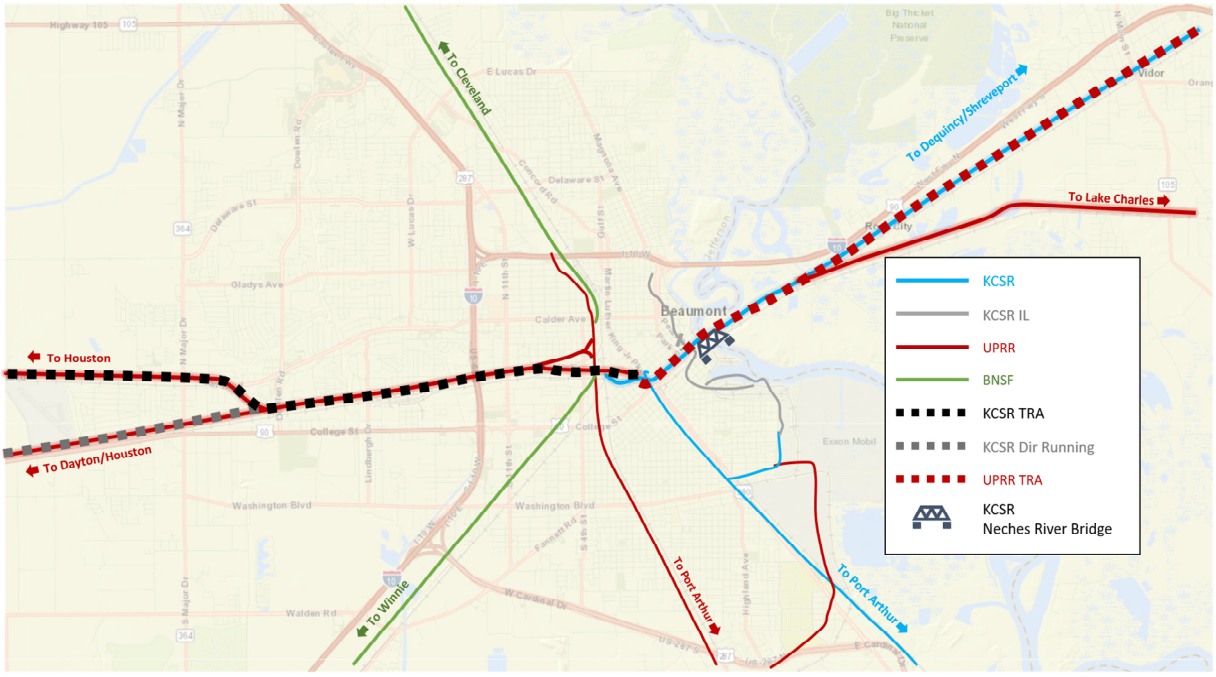
process in the timeframe set forth in the Application. As owner of the lines, our participation is critical. If the Board were to approve the proposed transaction, UP would be willing to work with Applicants to determine how to meet their need for new capacity, and we would be willing to construct new capacity and pay our fair share for any portion of the capacity we use in the future. However, UP should not be required to *subsidize* Applicants' implementation of their merger, either directly by financing the new capacity or indirectly through interference with our own service if Applicants increase their traffic before the new capacity is operational.

B. Applicants Failed to Evaluate the Impacts of Their Planned Operations Where Other Railroads Share Applicants' Lines.

Applicants' disregard for the impacts of their planned operations on others appears to extend to locations where other railroads operate on lines owned by one of the Applicants. UP is concerned by Applicants' lack of plans to add capacity in many locations, and we are particularly concerned about three locations: the Neches River bridge, the paired tracks north of Kansas City between Airline Junction and Polo, and the Twin Cities area. We discuss these three examples below.

Neches River Bridge. KCS owns the Neches River bridge. The bridge spans the Neches River at Beaumont. As shown in the figure below, UP's Beaumont and Houston Subdivisions converge at the western end of the bridge. KCS's Beaumont Subdivision and UP's Lafayette Subdivision (known as the "50/50 Line," because BNSF jointly owns the line) converge at the eastern end of the bridge. The bridge is a single-track choke point.

Figure 3: Neches River Bridge Area



UP believes the Neches River bridge is near or at the limits of its fluid capacity. UP and BNSF operate approximately 25 trains per day over the bridge. Amtrak's Sunset Limited train also uses the bridge, which limits freight operations. The bridge opens several times each day to allow river traffic to pass underneath, further reducing the time available for rail operations. Bridge capacity is also limited by the nature of railroad activity adjacent to the bridge. To the east, UP and KCS move unit trains to the Jefferson Energy Terminal. KCS trains entering and exiting the terminal block the eastern approach to the bridge. To the west, trains operate at reduced speeds over a series of converging and diverging tracks.

Applicants plan to increase traffic on KCS's Beaumont Subdivision from 8.9 trains per day to 20.3 trains per day, and increase of 11.4 trains per day, or 128%.[39] However, Applicants did not identify any need for additional bridge capacity. We believe adding more than eleven

[39] *See* APP Vol. 2 at 364, OP Plan, App. A at 1.

trains per day to the bridge would put the bridge above any reasonable measure of fluid capacity. {

} In addition, as noted above, the bridge is not available 24-hours a day because it opens for river traffic. We also pause freight rail traffic to accommodate Amtrak trains. Applicants may be reluctant to acknowledge the issue. Adding capacity to the Neches River bridge might be a costly, time-consuming undertaking. But even if Applicants were willing to accept poor service due to an over-capacity bridge, they should not be allowed to impose and shift those costs on UP, BNSF, and Amtrak as the price of their transaction.

Kansas City and the Polo Line. UP has similar concerns with Applicants' failure to provide for capacity investment on the Polo Line. CP and UP access Kansas City from the north using paired tracks over approximately 42 miles between Airline Junction in Kansas City and a location on CP's Kansas City Subdivision called Polo. UP operates approximately eight trains per day on the Polo Line. Applicants plan to increase traffic on CP's Kansas City Subdivision from 2.9 trains per day to 16.9 trains per day, an increase of 14 trains per day, or nearly 500%.[40] However, Applicants did not identify any plan to add capacity on the Polo Line.

CP controls dispatching of the Polo Line. Recently, UP has been forced to invoke the parties' contractual dispute resolution procedure to address persistent dispatching issues. UP is concerned that the problems it experiences when CP operates only three trains per day over the

[40] *See* APP Vol. 2 at 364, OP Plan, App. A at 1.

line would multiply if CPKC operated nearly 17 trains per day over the line. Most lines serving the Kansas City terminal are dispatched by the Kansas City Terminal Railway from a joint dispatching center. The Polo Line is dispatched by a CP employee from a drawbridge near Airline Junction. Although the Polo Line consists of two tracks, the tracks are not operated like double-track lines. Over a long portion of the joint facility, the two tracks are far apart, so trains cannot cross from one line to the other to maximize efficient use of both lines. Each line is generally operated in one direction only. In addition, although the line has a version of Centralized Traffic Control, the system does not allow for full CTC operations, which prevents true centralized dispatching and prevents UP and CP from maximizing capacity on one of the paired tracks when the other is out of service. In light of Applicants' plan to increase traffic by more than 14 trains per day on the Kansas City Subdivision, UP expected some provision for improving the Polo Line. This appears to be another situation in which Applicants have not accounted for shared facilities in planning the proposed transaction.

Twin Cities. Applicants' apparent failure to account for the impacts of their proposed transactions on other railroads' operations extends to their plan for operations in the Twin Cities. Applicants tout their plan to route traffic around Chicago. However, Applicants' plan to route traffic around Chicago will increase the number of trains moving through St. Paul on CP's River Subdivision from 11.9 trains per day to 18.1 trains per day, an increase of 6.2 trains per day, or 52%.[41] But Applicants do not propose adding capacity in St. Paul.[42]

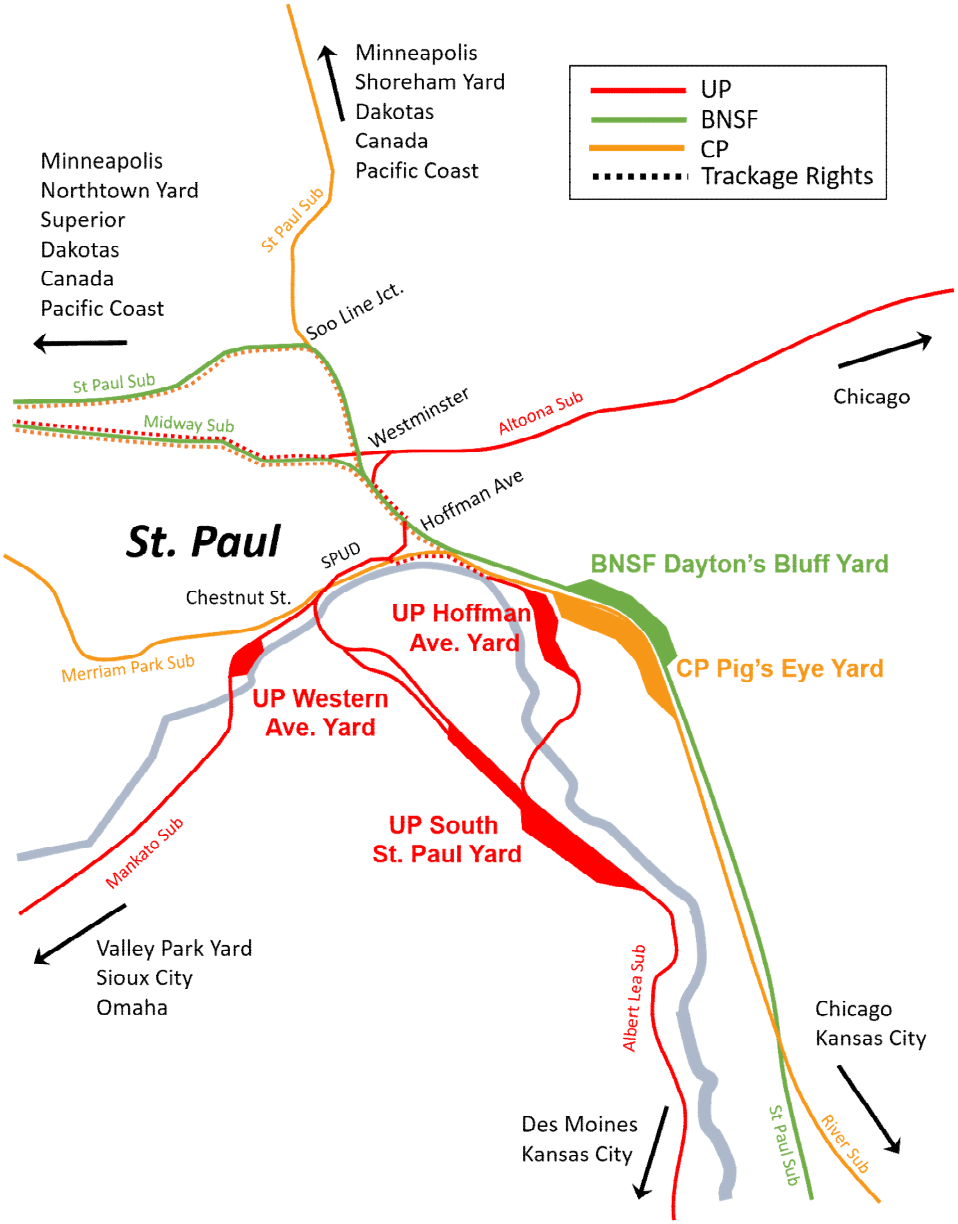
St. Paul can become extremely congested under current conditions. As shown in the figure below, CP's River Subdivision converges with BNSF's St. Paul Subdivision near CP's

[41] *See* APP Vol. 2 at 364, OP Plan, App. A at 1.

[42] *See* APP Vol. 2 at 337, OP Plan ¶ 231, Fig. 11.

Pig's Eye Yard and BNSF's Dayton's Bluff Yard. North of those yards, CP and UP operate using trackage rights on BNSF to connect between their own lines through St. Paul. Specifically, CP uses the rights for its route between Canada, the Dakotas, and Chicago, while UP uses the rights for traffic moving between our Albert Lea Subdivision, Altoona Subdivision, and Mankato Subdivision, and to reach several yards we use in St. Paul.

Figure 4: St. Paul Area



Unless Applicants construct additional capacity, something will have to give. Applicants would be unable to route as many new trains through St. Paul as they plan, because their trains would be blocked by other trains moving through the area. If Applicants did get their new trains through, they would be blocking UP (and BNSF) movements through St. Paul, forcing UP to add capacity to prevent its waiting trains from interfering with our other operations in the terminal. The Board should require Applicants to address the impacts of their proposed transaction in St. Paul, rather than allowing them to ignore the issue and potentially saddle others with the costs.

Other locations. UP's concerns about Applicants' lack of planning, or their lack of regard for the impacts their proposed transaction would have on UP and other railroads, are not limited to the specific areas discussed above. Applicants project significant traffic growth in Shreveport—nearly twelve additional trains per day moving through the terminal[43]—which they describe as the central "hub" of KCS's U.S. operations.[44] Both UP and BNSF use trackage right over KCS in Shreveport as part of their North-South routes between Houston and Chicago. Applicants do not address the impact of their projected traffic growth on the capacity available to UP and BNSF. Applicants also project significant traffic growth on CP's Davenport Subdivision, which crosses UP's Transcontinental main line in Clinton, Iowa, just after UP's main line passes west over the Mississippi River. Applicants do not address how their 300% growth in traffic, from 7.1 trains per day to 21.6 trains per day,[45] would affect this busy spot. In these and other

[43] APP Vol. 2 at 364, OP Plan, App. A at 1.

[44] APP Vol. 2 at 275, OP Plan ¶ 49.

[45] APP Vol. 2 at 364, OP Plan, App. A at 1.

locations where Applicants' merger-related traffic growth would impinge on the operations of other railroads, Applicants ignore the problem.

C. UP's Proposed Capacity Investment Condition Is Narrowly Tailored to Ensure the Proposed Transaction Is in the Public Interest.

Applicants have not provided sufficient information about their operating plans for the Board to conclude the proposed transaction is in the public interest. They have not acknowledged the harmful impacts of their merger-related traffic growth, much less committed to mitigating those impacts by investing in new capacity required to implement their plans.

If the Board nonetheless authorizes the CP/KCS transaction, UP urges the Board to impose a condition to ensure Applicants' plans are in the public interest. The condition should establish three principles: *First*, Applicants must work with owners and other users of rail lines and other rail facilities that will be used jointly by CPKC to identify investments in new capacity necessary to accommodate Applicants' planned traffic growth. *Second*, Applicants must commit to fund necessary investments in new capacity, with other railroads paying their fair share to the extent they also use the new capacity in the future. *Third*, Applicants must commit not to increase CPKC operations on affected lines above pre-merger CP or KCS levels *until* the owners of the lines agree sufficient capacity has been added to accommodate the traffic growth. The Board would remain available to resolve disputes at any stage of the process.

UP's request is narrow. It would not prevent Applicants from implementing any plans set forth in their Application. However, Applicants failed to address a critical aspect of their plans—the costs they would impose on others. UP's proposed condition would ensure it is not required to subsidize Applicants' transaction.

VERIFICATION

I, Kenny Rocker, 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 February 27, 2022.

/s/ Kenny Rocker

VERIFICATION

I, John Turner, 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 February 27, 2022.

/s/ John Turner

BEFORE THE
SURFACE TRANSPORTATION BOARD

Finance Docket No. 36500

CANADIAN PACIFIC RAILWAY LIMITED; CANADIAN PACIFIC RAILWAY COMPANY; SOO LINE RAILROAD COMPANY; CENTRAL MAINE & QUEBEC RAILWAY US INC.; DAKOTA, MINNESOTA & EASTERN RAILROAD CORPORATION; AND DELAWARE & HUDSON RAILWAY COMPANY, INC.

—CONTROL—

KANSAS CITY SOUTHERN; THE KANSAS CITY SOUTHERN RAILWAY COMPANY; GATEWAY EASTERN RAILWAY COMPANY; AND THE TEXAS MEXICAN RAILWAY COMPANY

VERIFIED STATEMENT

OF

STEVEN C. SALOP

Table of Contents

1. QUALIFICATIONS AND ASSIGNMENT 1

1.1 Qualifications 1
1.2 Assignment 2

2. INTRODUCTION AND EXECUTIVE SUMMARY 2

3. MODERN ECONOMIC ANALYSIS REJECTS THE APPLICATION OF THE ONE-LUMP THEORY TO THE PROPOSED MERGER 7

3.1 The Limited Applicability of the One-Lump Theory 10
3.2 The One-Lump Theory Does Not Hold When the Carriers Have Imperfect Information About Each Other's Costs and Rates 14
3.3 The One-Lump Theory Does Not Hold When the Competing Carriers Sell Differentiated Products 16
3.4 Implications for the Board's Analysis of the Proposed CPKC Merger 23

4. MODERN ECONOMIC ANALYSIS REJECTS THE ASSUMPTION THAT THERE IS NO INCENTIVE OR ABILITY TO FORECLOSE WHEN THERE IS A COMPETING CARRIER FOR EACH SEGMENT 24

5. EMPIRICAL ANALYSIS CONFIRMS THAT THE CPKC MERGER RAISES SERIOUS FORECLOSURE CONCERNS 27

6. DR. MAJURE'S ANALYSIS OF TRAFFIC FLOWS AT LAREDO LACKS PROBATIVE VALUE 32

6.1 Dr. Majure's Traffic Share Data Does Not Disprove the Existence of Foreclosure Concerns 32
6.2 Analysis of Southbound Traffic Through the Laredo Gateway Does Not Support Dr. Majure's Conclusion that There Are No Foreclosure Concerns 35
6.3 Dr. Majure's Data Do Not Provide Evidence of a Preference for Single-Line Service 37
6.4 Dr. Majure's Flawed Argument that There Are No "Pre-Existing Constraints" on Foreclosure 38

7. A SPECIFIC COMMERCIALLY REASONABLE RULE 11 RATE METHODOLOGY FOR CPKC'S MONOPOLY SEGMENTS CAN AVOID FORECLOSURE CONCERNS 40

7.1 Applicants' Commitments are Vague and Insufficient 40
7.2 A Proposed Commercially Reasonable Rate Formula for CPKC Monopoly Segments 44
7.3 The CRR Formula Will Not Reduce Competition 45

APPENDIX A. PROFESSOR SALOP'S CURRICULUM VITAE A-1

APPENDIX B. NUMERICAL EXAMPLE OF FORECLOSURE WITH IMPERFECT INFORMATION B-1

APPENDIX C. EQUILIBRIUM SIMULATION MODEL WITH UPSTREAM MONOPOLY AND DIFFERENTIATED PRODUCTS, DOWNSTREAM DUOPOLY: TAKE-IT-OR-LEAVE-IT OFFERS C-1

APPENDIX D. EQUILIBRIUM SIMULATION MODEL WITH UPSTREAM MONOPOLY AND DIFFERENTIATED PRODUCTS, DOWNSTREAM DUOPOLY: INTER-CARRIER NEGOTIATIONS D-1

APPENDIX E. MATERIALS RELIED UPON E-1

List of Figures

Figure 1: Illustration of Railroad Interconnection With a Monopolist on One Segment.. 11
Figure 2: Duopoly Competition 25
Figure 3: B&Z Estimated Potential and Likely Diversions Through Laredo..... 28
Figure 4: CPKC Foreclosure Incentives: Finished Automobiles 30
Figure 5: CPKC Foreclosure Incentives: Automobile Parts..... 31
Figure 6: Reproduction of Dr. Majure's Exhibit 2..... 33
Figure 7: Pre-KCS/TFM/TM Shares of Movements via All U.S./Mexico Gateways..... 34
Figure 8: Shares of Southbound Traffic Interchanged at Laredo Gateway with KCSM... 36
Figure 9: Northbound Finished Automobile Shipments through Laredo to Kansas City-2019..... 37

1. Qualifications and Assignment

1.1 Qualifications

1. I am Professor of Economics and Law and Georgetown University Law Center, where I teach courses in antitrust economics and law. I am also a Senior Consultant at Charles River Associates. My research and consulting focuses on antitrust, competition and regulation. I have written articles in various areas of antitrust and competition economics, law and policy with various co-authors. These articles have analyzed various economic, policy and legal issues in vertical and horizontal mergers, joint ventures, exclusionary and coordinated conduct. I have also written articles with various co-authors on the competitive effects of imperfect information, oligopoly interaction, network effects and monopolistic competition.

2. My work on the economic analysis and competitive effects of vertical mergers, as well as vertical merger enforcement policy and law, includes articles with various co-authors published in the American Economic Review, Yale Law Journal, Antitrust Law Journal, and the Review of Industrial Organization, among others. I was the lead panelist on the Vertical Merger panel at the FTC antitrust hearings in 2018. Along with several co-authors, I provided comments on the draft Vertical Merger Guidelines in March 2020. I have also written about the shortcomings of those Guidelines, which are now in the process of being revised. I have provided economic consulting on numerous vertical mergers with the Antitrust Division of the Department of Justice, merging parties, and third parties concerned with adverse competitive effects of specific vertical mergers.

3. I earned a BA degree at University of Pennsylvania, Summa Cum Laude in 1968 and a PhD in Economics from Yale University in 1972. Before joining the faculty of the Georgetown Law Center, I was a staff economist at the Federal Reserve Board, the Civil Aeronautics Board, and the Federal Trade Commission (FTC). At the FTC, I also served as the Assistant Director for Industry Analysis and the Associate Director for Special Projects. I have been honored with lifetime achievement awards from the Association of American Law Schools (AALS) Section on Antitrust & Economic Regulation (in 2019) and the American Antitrust Institute (in 2010). My Curriculum Vitae is attached at Appendix A.

1.2 Assignment

4. I am providing this statement at the request of Union Pacific Railroad Company (UP) in connection with the Surface Transportation Board's review of the proposed acquisition of control of Kansas City Southern (KCS) by Canadian Pacific (CP). I have been asked to focus on the effects of the transaction on competition for rail movements between the United States and Mexico through the Laredo gateway. UP relies on a KCS subsidiary, Kansas City Southern de México (KCSM), to transport a significant amount of U.S.-Mexico cross-border rail traffic south of Laredo.

5. I have been asked by counsel for UP to address several issues: (a) the applicability of the one-lump theory to the proposed merger; (b) whether the proposed merger raises substantial concerns of causing anticompetitive effects from foreclosure; and (c) whether there is an administrable methodology that the Board could require the post-merger firm to employ in order to set commercially reasonable interline rates, to prevent anticompetitive foreclosure.

2. Introduction and Executive Summary

6. This proceeding involves the proposed combination of CP and KCS. CP's network in Canada extends from the Port of Vancouver on the Pacific Coast to the Port of Saint John on the Atlantic Coast, and its network in the United States includes connections to Minneapolis, Chicago, Detroit, and Kansas City. KCS's operations center is in Shreveport, and its lines extend north to Kansas City, west to Dallas, east to Meridian, southeast to New Orleans, and south to Beaumont, Corpus Christi, the Laredo gateway, and Mexico. The rail networks of KCS and CP connect at Kansas City.

7. KCSM operates between Laredo (and Brownsville) and the industrial heartland of Mexico under a franchise obtained from the Mexican government. In 2005, KCS acquired a controlling interest in KCSM's predecessor, Transportación Ferroviaria Mexicana (TFM). At about the same time, KCS acquired control of the Texas Mexican Railway (TM). TM had rights to operate on UP lines between a connection with KCS in Beaumont and Corpus Christi, and TM owned its own line between Corpus Christi and Laredo.

8. UP has routes throughout the western United States, including an independent route between Laredo and the Upper Midwest. UP owns a 26% passive interest in Ferrocarril Mexicano (FXE), but has no control over FXE's operations or pricing.

9. UP and KCSM interchange a substantial amount of traffic at Laredo, including large quantities of finished automobiles and automobile parts moving between Mexico and the Upper Midwest. UP does not have its own rail lines in Mexico, and relies on KCSM's lines. At the same time, KCS's route north of Laredo is less efficient than UP's, and KCS does not have lines serving the Upper Midwest. KCS also has an alternative to UP: it moves traffic between Laredo and Corpus Christi, where it interchanges with BNSF Railway. BNSF has its own extensive network in the western United States. Shippers also can use KCS to move traffic between Laredo and Kansas City, where KCS can hand it off to CP. KCS also connects with other railroads at other points on its network.

10. In seeking authority to merge, CP and KCS emphasize the combined company's potential ability to divert a significant amount of traffic from KCSM-UP routes and KCSM-KCS-BNSF routes to single-line routes of the combined railroad (CPKC). My analysis mainly focuses on how CPKC can achieve such diversion by foreclosure arising from higher rates being charged to customers of carriers interlining with KCSM on movements between Mexico and the U.S., via the Laredo gateway.

11. Although the Board has traditionally relied on the "one-lump" theory to presume that end-to-end mergers are procompetitive, my economic analysis summarized in this report leads to the conclusion that the one-lump theory does not support such a presumption in this matter. Modern economic theory has recognized that the one-lump presumption does not apply under certain market conditions, in particular, when (a) the market participants sell differentiated products (i.e., products that shippers do not view as perfect substitutes at equal rates), or (b) the carriers set their rates based on imperfect information about each other's costs and rates. Both of these deviations from the conditions that are necessary to sustain the one-lump theory are present in the markets that will be affected by the proposed transaction. My report provides a series of models and examples based on the economics literature to illustrate these market conditions under which the theory does not apply and the impact that deviations from those conditions will have on the reliability of the presumption in this matter.

12. When the one-lump theory does not apply, an end-to-end merger between a monopoly carrier on one segment and one of the competing carriers on the other segment may have anticompetitive effects. I further conclude that this merger raises serious concerns about the likelihood of such effects on rates and service for shippers using the Laredo gateway. Absent an effective remedy, the merged firm will have both the incentive and the ability to implement anticompetitive strategies that foreclose competitors such as UP and BNSF that rely on interlining with KCSM. Specifically, CPKC will have the incentive and ability to drive traffic to CPKC by raising the rates that KCSM charges for interline movements on

routes where KCSM has an effective monopoly and CPKC competes with UP. As a result of the merger, foreclosure will generate incremental revenue and profits earned by the merged firm on those routes where KCS can interline with CP, over and above what KCS would earn before the merger if it foreclosed UP and BNSF with higher rates. By foreclosing competition from UP and BNSF with these higher rates, CPKC also will be able to raise its own rates and harm shippers. Thus, the post-merger foreclosure incentives rise above the level of any pre-merger incentives.

13. The evidence presented later in this report indicates substantial foreclosure concerns from the proposed CPKC merger. Two examples focused on movements between Chicago and Mexico of finished automobiles and automobile parts show that a hypothetical foreclosure strategy of KCSM charging UP prohibitive rates for these interline movements would be profitable for the merged firm. The merged CPKC would have an increased incentive and ability to raise KCSM interline rates due to the addition of the revenue and profits earned on the CP portion of diverted shipments.

14. Applicants attempt to allay concerns about foreclosure through the expert report of Dr. Robert Majure. He concedes that an end-to-end merger is capable of impairing competition in some circumstances. But Dr. Majure does not describe or explain those circumstances, nor does he analyze foreclosure concerns in depth to demonstrate that those concerns are not present here. Instead, Dr. Majure seems to assume that there must be *no incentive* for a vertically integrated monopolist to foreclose in this case because it must already be capturing all the monopoly profits without foreclosure and without the merger. But Dr. Majure provides no data or analysis to support that assumption. Instead, he attempts to dismiss the possibility of foreclosure by claiming that the prior acquisition by KCS of TM and KCSM's predecessor, TFM, which brought KCS control of the Laredo gateway, did not result in foreclosure. But the only data that Dr. Majure provides to support this claim is a snapshot of northbound traffic shares from 2019, fifteen years after the merger. Dr. Majure's analysis of that limited data sample lacks probative value, however, because it is equally consistent with a finding of "some foreclosure" as with "no foreclosure." Dr. Majure specifically does not address whether the shares he observes would have been different but-for the merger. He also fails to explain why the merger would not increase the foreclosure incentives in light of the ability to capture additional revenue and profits on the CP portion of diverted movements.

15. Dr. Majure also asserts that a vertically integrated merged carrier would have no *ability* to foreclose an unintegrated rival carrier to the detriment of shippers, if that rival can obtain interline service from another unintegrated carrier. To support this assertion, Dr. Majure suggests that shippers could discipline anticompetitive behavior by a post-merger KCSM by

turning to FXE for movements between Mexico and the U.S. However, he offers no evidence that FXE actually provides a viable option for all (or even most) shippers using KCSM. He also fails to address Applicants' economic incentive to raise rates on interline routes, even when shippers might feasibly use FXE, because he fails to acknowledge that CPKC could reasonably anticipate that FXE would raise its own rates in response, thus accommodating CPKC's rate increase and providing CPKC with a reinforcing incentive to raise its rates.

16. Applicants' witnesses Brown and Zebrowski state that the merged firm will be able to divert traffic from UP and others by reducing its costs and increasing its service quality.[1] Their formulation also essentially concedes an ability to foreclose. That is, if a merged firm with a monopoly on one segment can divert traffic by reducing its own costs, then it normally also can divert traffic by raising its rivals' costs. Reducing its own costs allows the firm to gain traffic by decreasing its rates, while raising rivals' costs allows the firm to gain traffic by causing the rivals to increase their rates. After the merger, CPKC can raise rivals' costs by raising the rates it charges for interline movements with those rivals.

17. Vertical mergers can also lead to downward pricing pressure from elimination of double marginalization (EDM). However, to whatever extent EDM may be a significant factor in this matter — and Applicants' submissions, including Dr. Majure's statement, do not suggest that it will be a significant (if any) factor — there is no reason to expect that any such downward pricing pressure from EDM would completely offset and reverse the upward pricing pressure from foreclosure incentives. Although Applicants' experts Brown & Zebrowski have claimed that the merger will result in efficiency benefits, they also assume that diversions from competing interline routes will not be the result of rate decreases. Moreover, UP witnesses have opined that the efficiencies that the parties claim from the transaction are overstated and that the merged firm will have to grow their single-line traffic and revenues by foreclosing, rather than by increasing competition.[2]

18. If the Board is inclined to approve the transaction, it would need to impose a remedy to prevent such harms. One potential behavioral remedy would be to require that when a shipper asks the merged firm to provide a rate for KCSM service that could be used as part

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[1] *Verified Statement of Richard W. Brown and Nathan S. Zebrowski* (October 29, 2021) (*hereinafter*, Brown & Zebrowski V.S.) at ¶¶5, 7, 11 in CPKC Application, *Canadian Pac. Ry. Corp.—Control & Merger—Kansas City. S.* (F.D. 36500) (*hereinafter*, APP).

[2] *See generally Verified Statement of Thomas C. Haley* (February 25, 2022) (*hereinafter,* Haley V.S.); *Verified Statement of Kenny Rocker and John Turner* (February 27, 2022) (*hereinafter*, Rocker & Turner V.S.). These statements, along with this one, are being submitted as part of Union Pacific's Comments on the APP.

of an interline rate with UP and a rate for CPKC single-line service on a competitive origin-destination route, the merged firm must provide the shipper a rate for KCSM service using the type of formula presented in this report for developing competitively reasonable Rule 11 rates. The Board should also protect against non-rate-based methods of foreclosure by requiring the merged firm to refrain from unilaterally changing operations affecting interline traffic moving via the Laredo gateway.

19. Specifically, I suggest that the Board consider the following administrable, readily enforceable formula for developing competitively reasonable Rule 11 rates: The Applicants state that "when a customer requests a rate for only the former-CP or former-KCS portion of an origin-to-destination routing, we will provide the shipper with a Rule 11 rate to the gateway."[3] Using this language, when a shipper asks CPKC to provide a rate for CPKC service on only former-CP or former-KCS/KCSM portions of an origin-to-destination route, and a rate for CPKC single-line service on a competitive route, the merged firm must provide a Rule 11 rate for the former-CP or former-KCS/KCSM portions that reflects a mileage-based prorate of its CPKC single-line rate. The prorate would be equal to the ratio of (a) the miles of the merged firm from the origin point to the interchange point to (b) the miles of the merged firm from the origin to the interchange *plus* the miles of the merged firm from the interchange point to the destination point. As I explain in detail below, this remedial approach allows the merged firm and shippers to obtain the benefits of the transaction, while at the same time protecting shippers from harm.

20. The remainder of this report is organized as follows. Section 3 explains why modern economic analysis rejects the one-lump theory in the circumstances presented by the proposed transaction. It also sets out general conditions under which end-to-end mergers have anticompetitive effects and the reasons why there are serious concerns of anticompetitive effects on routes where there is a monopolist on one segment and competition on the other, so that a procompetitive policy presumption would not be appropriate in this matter. Section 4 briefly explains why modern economic analysis does not support the view that the presence of a competing interline option like FXE would eliminate the ability and incentive of an integrated carrier to foreclose competition from a downstream rival. Section 5 provides empirical analysis that confirms that the merger raises substantial foreclosure concerns. Section 6 explains why Dr. Majure's analysis of the likely competitive effects of the proposed CPKC merger lacks probative value. Section 7 describes a prescribed formula for developing commercially reasonable Rule 11 rates for the monopoly segment of interline movements. The Appendices present details of the technical

[3] APP., *Verified Statement of John Brooks* (October 29, 2021) (*hereinafter*, Brooks V.S.) at ¶46.

economic analysis and models, as well as my Curriculum Vitae and a list of materials relied upon.

3. Modern Economic Analysis Rejects the Application of the One-Lump Theory to the Proposed Merger

21. The Board historically has relied on the "one-lump" theory to presume that end-to-end mergers with a monopolist in one segment and competition in the other segment will *not* cause competitive harm. In fact, the theory assumes that an end-to-end merger will have no economic effects on profits or rates. In analyzing petitions in opposition to the merger of the Burlington Northern Railroad and the Atchison, Topeka and Santa Fe Railway in 1997, the D.C. Circuit characterized the one-lump theory as a "broadly accepted economic proposition."[4] However, as discussed in detail in this section, the one-lump theory is not broadly accepted today. In fact, modern economic analysis makes it clear that it applies only under very limited market conditions that are not present in the case of the CPKC merger.

22. The economic underpinning of the one-lump theory in rail transport is the so-called "single monopoly profit" theory developed in the early industrial organization economics literature analyzing tying[5] and then applied to vertical mergers.[6] In this economic model applied to vertical mergers, one firm has a monopoly in producing an "input," while there is perfect competition among the competing firms, (*i.e.*, two or more firms with perfect information producing an undifferentiated (homogeneous) "output") that use the input and sell that output to consumers.[7] According to this theory, the monopolist would not need to acquire one or both of the competitors in the output market in order to be able to extract all of its input monopoly profits from consumers. That is, the acquisition does not change anything,

[4] Western Resources, Inc. v. Surface Transp. Bd., 109 F.3d 782, 788 (D.C. Cir. 1997).

[5] Ward S. Bowman, *Tying Arrangements and the Leverage Problem*, 67 YALE L. J. 19 (1957). *See* also Aaron Director & Edward H. Levi, *Law and the Future: Trade Regulation*, 51 NW. U. L. REV. 281 (1956); M.L. Burstein, *The Economics of Tie-in Sales, 42* REV. ECON. & STAT. 68 (1960).

[6] R.H. Bork, THE ANTITRUST PARADOX 229 (1978).

[7] The logic of this "vertical" merger model also applies to mergers of complementary products. In that version, there is a monopoly producer of one of the complements and multiple competitors for the other complement. Consumers purchase a bundle of the two complementary products.

absent efficiencies, because there is only "one lump" of monopoly profits that can be extracted by the monopolist, and it can do so either with or without the acquisition.[8]

23. Even assuming that the theory could apply in some circumstances, it is important to recognize that the theory relies on several very restrictive assumptions about markets that greatly limit its applicability to transactions such as the proposed CPKC merger. Modern academic work has confirmed these limitations.[9] As detailed in this report, when there is an upstream monopolist, there are market conditions in which the single monopoly profit theory is upended. These involve conditions under which the competing downstream firms earn a positive margin over costs, arising from the fact that the companies are selling differentiated products or operating with imperfect information regarding each other's prices and costs.[10]

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[8] As stated by the ICC in a 1982 decision, "[A] carrier with a destination monopoly will likely push the through rate as high as possible and keep the monopoly profits to itself by playing off competing connecting carriers against one another in setting divisions. That is, the through rate will be at the level maximizing net revenue for the traffic, subject to regulatory limits, and the destination carrier will establish favorable through service with the origin carrier willing to take the lowest division of the through rate for its segment of the movement." *See Union Pac. Corp. —Control— Missouri Pac. Corp*, 366 I.C.C. 462, 538 (1982). The Applicants in the Burlington Northern/Atchison Topeka and Santa Fe merger referred to this as the "one-lump" theory. *See Burlington Northern, Inc.—Control & Merger—Santa Fe Pac. Corp.*, 10 I.C.C.2d 661,749 (1995). *See* also *Western Resources, Inc. v. Surface Transp. Bd.*, 109 F.3d 782, 787 (D.C. Cir. 1997).

[9] *See, e.g.,* Louis Kaplow, *Extension of Monopoly Power through Leverage*, 85 COLUM. L. REV. 515 (1985); Michael D. Whinston, *Tying, Foreclosure, and Exclusion*, 80 AM. ECON. REV.837 (1990); Michael H. Riordan & Steven C. Salop, *Evaluating Vertical Mergers: A Post-Chicago Approach*, 63 ANTITRUST L.J. 513 (1995); Dennis W. Carlton & Michael Waldman, *The Strategic Use of Tying to Preserve and Create Market Power in Evolving Industries*, 33 RAND J. ECON.194 (2002).

[10] Another general situation involves contractual negotiations with pre-payments, when the upstream monopoly firm negotiates input prices that contain lump sum payments (or take-or-pay contracts or large volume rebates) with each of the two competing downstream firms selling homogeneous products and the price terms offered to one competitor are not observed by the other competitor. In this negotiation structure, the monopoly carrier may be unable to implement the monopoly outcome in the pre-merger market because each firm will fear that the monopolist will opportunistically offer the other firm a better deal, which makes each firm unwilling to agree to the contract terms. However, by acquiring one of the competing carriers and foreclosing the unintegrated carrier, the vertically integrated carrier is able to charge the full monopoly price and earn monopoly profits. Hart & Tirole (1990) describe this result when the monopoly carrier makes take-it-or-leave-it contract offers, rather than engaging in bilateral bargaining. *See* Oliver Hart & Jean Tirole, *Vertical Mergers and Market Foreclosure*, BROOKINGS PAPERS ON ECONOMIC ACTIVITY – MICROECONOMICS 208 (1990). For a scenario with differentiated products and two-part tariffs, *see* R. Preston McAfee & Marius Schwartz, *Opportunism in Multilateral Vertical Contracting: Nondiscrimination, Exclusivity and Uniformity*, 84 AM. ECON. REV. 219-21 (1994).

24. Moreover, the results of modern economic analysis lead to greater concerns that vertical mergers will result in anticompetitive effects.[11] This highlights the need to take the limitations of the one-lump theory into account when determining whether to apply its presumption in a given case.

25. Similarly, vertical merger enforcement today also avoids presuming, based on the single monopoly profit theory, that all such mergers are procompetitive. For example, there have been three recent FTC vertical merger enforcement actions – Illumina/Grail,[12] NVIDIA/ARM,[13] and (most recently) Lockheed Martin/Aerojet Rocketdyne[14] – and a previous DOJ investigation (LAM/KLA) [15] that each involved allegations that the upstream

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[11] *See, e.g.*, Marissa Beck & Fiona Scott Morton, *Evaluating the Evidence on Vertical Mergers*, 273 REV. IND. ORG. (2021); Steven C. Salop, *Invigorating Vertical Merger Enforcement*, 127 YALE L.J. 1962 (2018); Gregory S Crawford, Robin S. Lee, Michael D. Whinston & Ali Yurukoglu, *The Welfare Effects of Vertical Integration in Multichannel Television Markets*, 86 ECONOMETRICA 891 (2018); Jonathan B. Baker, *Taking the Error out of "Error Cost" Analysis: What's Wrong with Antitrust's Right*, 80 ANTITRUST L.J. 1, 15-17 (2015); Jonathan B. Baker, *Exclusion as a Core Competition Concern,* 78 ANTITRUST L.J. 527 (2013); Serge Moresi & Steven C. Salop, *vGUPPI: Scoring Unilateral Pricing Incentives in Vertical Mergers,* 79 ANTITRUST L.J. 185 (2013); Jay Pil Choi, *Mergers With Bundling in Complementary Markets*, 61 J. IND. ORG. 553, 556 (2008); Yongmin Chen, *On Vertical Mergers and Their Competitive Effects*. 32 RAND J. ECON 667 (2001); Patrick Rey & Jean Tirole, *A Primer on Foreclosure*, *in* 3 HANDBOOK OF INDUSTRIAL ORGANIZATION 2145 (Mark Armstrong & Robert H. Porter eds., 2007); Michael H. Riordan, *Competitive Effects of Vertical Integration*, *in* HANDBOOK OF ANTITRUST ECONOMICS 145 (Paolo Buccirossi ed., 2008); Michael H. Riordan & Steven C. Salop, *Evaluating Vertical Mergers: A Post-Chicago Approach*, 63 ANTITRUST L.J. 513 (1995); Janusz A. Ordover, Garth Saloner & Steven C. Salop, *Equilibrium Vertical Foreclosure*, 80 AM. ECON. REV. 127 (1990); Michael Salinger, *Vertical Mergers and Market Foreclosure*, 103 Q.J. ECON. 345 (1988); Thomas G. Krattenmaker & Steven C. Salop, *Anticompetitive Exclusion: Raising Rivals' Costs to Achieve Power over Price*, 96 YALE L.J. 209 (1986).

[12] *FTC Challenges Illumina's Proposed Acquisition of Cancer Detection Test Maker Grail*, Federal Trade Commission Press Release (March 30, 2021), https://www.ftc.gov/news-events/press-releases/2021/03/ftc-challenges-illuminas-proposed-acquisition-cancer-detection.

[13] *FTC Sues To Block $40 Billion Semiconductor Chip Merger—Vertical deal between chip supplier Nvidia and chip design provider ARM*, Federal Trade Commission Press Release (December 2, 2021), https://www.ftc.gov/news-events/press-releases/2021/12/ftc-sues-block-40-billion-semiconductor-chip-merger.

[14] *FTC Sues to Block Lockheed Martin Corporation's $4.4 Billion Vertical Acquisition of Aerojet Rocketdyne Holdings Inc*. Federal Trade Commission Press Release (January 25, 2022), https://www.ftc.gov/news-events/press-releases/2022/01/ftc-sues-block-lockheed-martin-corporations-44-billion-vertical.

[15] *Lam Research Corp. and KLA-Tencor Corp. Abandon Merger Plans*, Department of Justice Press Release, October 5, 2016, https://www.justice.gov/opa/pr/lam-research-corp-and-kla-tencor-corp-abandon-merger-plans; *See* also *The Interesting Case of the Vertical Merger*, Jon Sallet, Deputy Assistance Attorney General for Litigation at Department of Justice Antitrust Division, Remarks as

firm was dominant and that the post-merger firm could use foreclosure strategies to undermine downstream rivals, to the detriment of consumers. The DOJ and FTC also issued new Vertical Merger Guidelines (VMGs) in June 2020 that did not adopt the single monopoly profit theory and did not presume that vertical mergers involving a monopolist in one market are procompetitive, merger guidelines that now are being revised to correct what the Agencies have characterized as legal and economic errors.[16]

3.1 The Limited Applicability of the One-Lump Theory

26. In this section, I illustrate the one-lump theory and its limitations in a concrete way, by considering the situation where one railroad has a monopoly on one segment of a through movement and merges with one of the two railroads that compete on the other segment to complete the movement. This scenario is illustrated below in Figure 1, which shows a through movement from an origin (O) through a common interchange point (I) to a destination (D). I denote Railroads X and Y as the "originating" carriers, each having routes from O to I. Railroad A is the "destination" carrier. It is a monopolist on the segment from I to D. In the through pricing model,[17] the shipper asks the originating Carriers X and Y for through rate quotes for the entire movement, and X and Y each obtains a (dollar) "division" from destination Carrier A for carriage on the destination segment.[18] Following the use of

Prepared for Delivery at ABA Fall Forum (November 17, 2016), https://www.justice.gov/opa/speech/file/938236/download.

[16] U.S. Department of Justice and The Federal Trade Commission, *Vertical Merger Guidelines* (June 30, 2020), available at https://www.ftc.gov/system/files/documents/reports/us-department-justice-federal-trade-commission-vertical-merger-guidelines/vertical_merger_guidelines_6-30-20.pdf. U.S. Department of Justice and The Federal Trade Commission, *Request for Information on Merger Enforcement* (January 18, 2022) at n.3, available at https://www.justice.gov/opa/press-release/file/1463566/download.

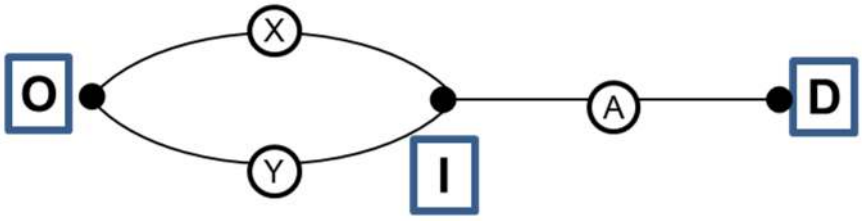
[17] This through pricing framework is the typical economics framework for vertical mergers. In this framework, the monopoly carrier is providing an "input" to the competing carriers, who then sell an "output" (i.e., interline service from O-to-D) to the shippers. Applying the jargon of inputs and outputs, the economics framework typically would refer to the monopoly carrier as "upstream" (*i.e.*, selling an input) and the competing carriers as "downstream" (i.e., selling the "output" to the customer). Most of the economic literature on vertical mergers applies this through pricing (e.g., upstream monopolist and downstream competitor) framework. The economic analysis of mergers of firms producing complementary products is analogous. *See* U.S. Department of Justice and The Federal Trade Commission, *Vertical Merger Guidelines* (June 30, 2020) at 9.

[18] This same framework obviously would carry over exactly to a movement in the opposite direction where the shipper asks Railroads X and Y for through rate quotes.

the term in the industry, Carrier A's *division* is the price or rate it gets for carrying the freight from I to D. [19]

27. If the one-lump theory holds, an acquisition by Carrier A of (say) Carrier X, will not have any anticompetitive effects. This is because Carrier A is presumably already extracting its full monopoly profit by charging a high (dollar) division for its I-to-D segment that is equal to the "one monopoly lump," and the acquisition therefore cannot increase its ability to exploit its market power.

Figure 1:
Illustration of Railroad Interconnection With a Monopolist on One Segment



28. Referring to Figure 1, assume that the two competing carriers (X and Y) on the originating segment O-I sell a homogenous product with identical marginal costs and compete solely on the basis of rates. Also assume that each carrier has perfect information about the other carriers' rates and costs for the movement at issue. Monopoly Carrier A has a marginal cost of $150.[20] Further suppose the competing Carriers X and Y, provide undifferentiated transportation, do not conspire with each other, and have identical marginal costs of $100. Assume also that the shipper has an alternative to rail transport that it would choose if the cost of rail transport were more than its "reservation price" of $400.[21] Thus, the $400 reservation price is the "monopoly" through rate.

[19] The division is treated as a dollar amount, not an agreed-upon fraction of whatever through rate is charged by the destination carrier. I understand the terminology developed when railroads used to establish divisions as a percentage of the through rate charged to the shipper.

[20] The marginal cost includes a competitive return on investment.

[21] The shipper's reservation price thus is the maximum through rate it is willing to pay, and would shift to another transportation mode or corridor if the quoted through rate exceeds this level.

29. Under these assumed conditions, competition between Carriers X and Y would drive their rate down to their marginal costs of $100.[22] Because Carrier A knows that Carriers X and Y will set their rates at $100 and also knows the shipper's reservation price, monopoly Carrier A would maximize its profits by charging a rate of $300 for its segment. The shipper would pay a total through rate equal to $400 (i.e., A's $300 monopoly price plus X's or Y's $100 rate).[23] This is equal to the shipper's reservation price. The monopoly carrier would earn a profit (i.e., price less marginal costs) of $150 (i.e., $300 - $150).

30. Under these assumed, perfect conditions, Carrier A's acquisition of Carrier X (and/or Carrier Y) would affect neither the total through rate paid by the shipper, nor Carrier A's profit.[24] Carrier A/X would earn the same profit regardless of whether it offered a single-line rate at $400 or its former division rate of $300 for its segment. In the case of a single-line rate, Carrier A/X would earn $400, while incurring the variable costs of $250 (i.e., $100 +$150) from handling the traffic on both segments, for a profit of $150 (i.e., $400 - $250) — the same amount it could earn by agreeing to its former division of $300 and costs of $150 to move the traffic over the I-to-D segment. Thus, according to the one-lump theory, Carrier A would not increase its profit if it foreclosed competition from Carrier Y, either by refusing to interline with Carrier Y or by raising its required division.[25]

31. This example rests on several assumptions, however, that make it apply only to very limited market conditions. It assumes that Carrier A is, in fact, already extracting its single monopoly profit, that is, there are no obstacles that prevent the pre-merger Carrier A from successfully earning that monopoly profit. To reach these results, it assumes that the

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[22] If either carrier offers a rate at some level above $100, the other carrier would undercut it. The model assumes that there is no collusion. The marginal costs include a competitive return on investment.

[23] The economics literature generally uses the term "prices" instead of "rates." I will use the terms interchangeably in this report.

[24] When all the other assumption are made, the one-lump theory still can apply if the shipper has elastic demand. For example, suppose that the shipper would choose to move two units by train if the total through rate were $390 per unit. Then, the monopoly carrier would set the division equal to $290 per unit and the two competing carriers would set through rates of $390 per unit. Because there is perfect competition between the two competing carriers, the monopoly carrier has no incentive to merge with one of the two competing carriers and, if it did, the merger would have no effect on the total through rate paid by the shipper.

[25] In this report, I often will focus on the use of price to foreclose, which I sometimes will refer to as "pricing foreclosure," rather than other non-price forms of foreclosure, such as causing delays, or an outright refusal to interline. Total foreclosure also may involve setting such a high division that interlining is prohibitively expensive for Carrier Y. I will discuss the profitability of a hypothetical total foreclosure strategy in a later section.

carriers are operating with perfect information about each other's costs and prices. And it also assumes that Carriers X and Y are selling homogenous (i.e., undifferentiated) products.

32. Modern economic analysis has confirmed that the one-lump theory does not apply in circumstances that deviate from these assumptions. In addition, absent these assumptions, foreclosure by the post-merger firm often is profitable and harmful to shippers. As I explain in more detail in the next two sections, both types of deviations from the assumed conditions— imperfect information and differentiated products — likely are present in the proposed transaction. Either of them would be sufficient to render the one-lump theory inapplicable in most real-world markets and specifically in this matter.

33. When the one-lump theory does not hold and there is monopoly in one segment but competition in the other segment (or competition in both segments), an end-to-end merger can lead to foreclosure and reduce competition, which in the rail context could take the form of increased divisions or segment fees levied by the monopoly carrier and increased interline rates charged by the competing carriers, higher single-line rates and harm to shippers. Thus, a procompetitive policy presumption also would be inappropriate in this matter.

34. In the absence of a one-lump presumption, these likely anticompetitive effects need to be balanced against any procompetitive benefits. In the polar case of a purely end-to-end merger between two monopoly carriers each protected by prohibitive entry barriers, neither of which faces any actual or potential competition, economic analysis suggests that the merger often can lead to lower rates.[26] This competitive benefit is referred to as "elimination of double marginalization" (EDM) and is driven by the idea that a lower price by one carrier benefits the other carrier by expanding its sales.

35. However, economic analysis demonstrates that the analysis and potential effects of vertical mergers differ substantially when there is competition at one or both levels. In those cases, EDM tends to be smaller because margins are lower. Even in the case of a monopoly carrier on one segment, when prices on the competitive segment exceed marginal costs due to product differentiation or imperfect information, the downward pricing pressure from EDM

[26] Absent cooperation, each carrier's rate setting would not take into account the benefits accruing to the other carrier from it setting a lower rate. By merging, the carriers would take these benefits into account and charge lower rates. There are two important exceptions, however. When there are monopolists at each level, they may be able to achieve the benefits of cooperation without a merger, relying instead on a contractual agreement or mutual trust, which means that the merger would not lead to lower prices. The role of entry barriers also is important: if these carriers were likely advantaged potential entrants (or entry sponsors) into each other's market, that fear of potential entry might have constrained their pre-merger prices all the way down to the competitive level. If so, the merger then would eliminate those constraints and so would lead to higher prices. See, e.g., Steven C. Salop, *Invigorating Vertical Merger Enforcement*, 127 YALE L.J. 1962, 1976-77 (2018).

often will be smaller than the upward pricing pressure from foreclosure. If a lower price by the merging competing carrier mostly diverts sales away from other competing carriers (that connect with the merging monopoly carrier), rather than expanding total market sales, the incentive to lower prices as a result of EDM could be quite small and is less likely to be the dominant pricing incentive generated by a merger. This is because the loss of profitable divisions on interline sales by the monopoly carrier is an "opportunity cost" of reducing the rate of the merging carrier on the competitive segment.[27] The relative magnitudes of the upward pricing pressure from foreclosure and the downward pricing pressure from merger-specific EDM are discussed below.

3.2 The One-Lump Theory Does Not Hold When the Carriers Have Imperfect Information About Each Other's Costs and Rates

36. Even if the competing firms sell homogenous products—that is, they compete only on price—the "one lump" theory does not hold in a market structure in which each pre-merger carrier faces imperfect information regarding the costs and rates of the other carriers. In such a market, the pre-merger monopoly carrier is generally unable to extract the full monopoly profit from the shipper, but is better able to do so after merging with one of the competing carriers. The merger creates an increased incentive and ability for the merged firm to foreclose rivals, leading to harm to both shippers and unintegrated carriers.[28]

37. This is not a minor exception to the conditions required for the one-lump theory. My understanding is that UP and KCS typically lack perfect information regarding each other's costs and rates offered to the shipper at the time that they quote their rates.[29] The costs incurred by the carriers for a particular shipment, and thus the rates offered by the carriers for that shipment, will differ according to numerous factors.[30] Similarly, where KCSM

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[27] This "opportunity cost" occurs whenever the increased sales resulting from the merged firm reducing its single-line rate to shippers involve diverting profitable sales away from a competing carrier that interconnects with the monopoly segment of the merged firm. For an example of this type of opportunity cost, *see* Carl Shapiro, *Vertical Mergers and Input Foreclosure: Lessons from the AT&T/Time Warner Case,* 59 REV. IND. ORG. 303, 325-26 (2021). *See* also Yongmin Chen, *supra* note 11; Moresi & Salop, *supra* note 11.

[28] This market structure is analyzed in detail in an economics article by Serge Moresi, David Reitman, Steven C. Salop & Yianis Sarafidis, *Vertical Mergers in a Model of Upstream Monopoly and Incomplete Information*, 59 REV. IND. ORG. 363 (2021).

[29] *See generally* Rocker & Turner V.S.

[30] *See* KCS and CP's Joint Responses and Objections to UP's Second Set of Discovery Requests, Response to Request No. 148. ("revenue and pricing are determined on a variety of factors and

provides its revenue requirements to UP and BNSF, KCSM typically does not know the costs of UP or BNSF or the rates they ultimately offer to shippers. Absent knowledge of the rates or costs of the other carriers, each carrier must base its rate offer on its expectations of the likely rates of the other carriers, as well as its own costs. This uncertainty creates the possibility that the monopoly carrier will not be able to set its pre-merger divisions at the monopoly level, which means that it is not earning its "one monopoly lump." Fearing that setting a high rate might lead to a total price above the shipper's reservation price and the loss of the traffic, the monopoly carrier will hold down its rate. A merger that reduces that uncertainty thus increases the likelihood that the merged firm will be able to profitably raise rates post-merger.[31]

38. In the pre-merger market, a monopoly carrier with imperfect information about the other carriers' costs and rates cannot obtain its "single monopoly profit" because it cannot set its own rate to ensure that the through rate is equal to, but does not exceed, the shipper's reservation price. Competition in the pre-merger market with imperfect information leads to the shipper obtaining a through rate below its reservation price some fraction of the time, in particular, when the competing carriers' costs are relatively low for the particular shipper's movement.[32] When their costs are higher, the shipper either pays its reservation price for the rail transport or chooses an alternative mode.[33] Combining the effects of the varied cost realizations for particular movements, the average through rate paid by the shipper in the pre-merger market will be less than its reservation price. In other words, some of the surplus accrues to the shipper and the competing carriers. In Appendix B, this analysis is illustrated with a numerical example.

39. Looking again at Figure 1, contrary to the one-lump presumption, a merger between the monopoly Carrier A and one of the carriers on the competitive segment —say, Carrier X— *does* change the incentives and ability of the merged firm to foreclose, by improving the

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considerations, including but not limited to the market, operating and cost considerations, the type of service, volume, risk premiums (such as hazardous materials or high- end commodities), asset availability, network capacity, competitive modes of transportation, and regulatory requirements. The same considerations apply to cross-border rates.")

[31] Moresi et. al., *supra* note 28. In the *Western Resources* case, *supra* note 4 at 791, the D.C. Circuit suggested that better information would not have an adverse effect on shippers. The Commission apparently did not contemplate the possibility that the monopoly carrier would recognize the risk that a high division might make it uneconomical for the competing carriers to set through prices at or below the shipper's reservation price; and that the monopoly carrier would respond to this risk by setting a lower division, and then the competing carriers would have sufficiently low costs such that they would compete the through price down to a level below the shipper's reservation price.

[32] For the general analysis, *see* Moresi et al., *supra* note 28.

[33] When the shipper chooses the alternative, it gains no surplus value, i.e., the shipper obtains the same value as if it paid a rate for rail transport on these carriers equal to its reservation price.

merged carrier's information. After, and as a result of, the merger, the merging carriers will now know each other's costs and prices, and thus will be able to set a single-line rate equal to the shipper's reservation price, extracting the full monopoly revenue from the shipper.[34] At the same time, the merged carrier will have increased incentives to act on its ability to foreclose by setting a high rate for interline service (or revenue requirement).[35] The shipper will end up worse off from the merger because it will always pay a through rate equal to its reservation price.

3.3 The One-Lump Theory Does Not Hold When the Competing Carriers Sell Differentiated Products

40. The previous model assumed the downstream competitors sold homogenous products—that they competed solely on price. However, the transport services provided by rail carriers are generally differentiated, not homogenous. The services can differ with respect to distance from a shipper's business to the origin and destination stations, the speed of the shipment, frequency and reliability, customer service, the likelihood of damage, payment terms, and so on. That differentiation leads rail transport rates to exceed marginal costs.[36]

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[34] The same reasoning and results apply for a Rule 11 rate since the shipper can obtain the rate from the monopoly carrier and then have the bidding competition between the two competing carriers. As with through rates, the shipper gains the benefit of pre-merger competition that allows it to pay a through rate that is, on average, below its reservation price and to earn a positive surplus. After the merger, the shipper is forced to pay a through rate equal to its reservation price and obtains zero surplus. At the same time, the merger increases the profits of the merging carriers and reduces the profit of the rival unintegrated carrier.

[35] The shipper is worse off because it will always pay a through equal to its reservation price, regardless of whether Carrier Y or Carrier X will win the competition post-merger. The merged carrier will set a division for its segment that is relatively high in the following sense. If the unintegrated rival Carrier Y has a sufficiently lower cost than Carrier X, then Carrier Y will win the competition for the shipper's business and the merged carrier will earn a higher profit from supplying interline service to Carrier Y than it would earn from its single-line rate (equal to the shipper's reservation price). This allows the merged firm to let Carrier Y serve the shipper when Carrier Y is significantly more efficient and, at the same time, to extract a portion of the efficiency rent of Carrier Y. See also the numerical example in Appendix B.

[36] *See*, e.g., Laurits R. Christensen Assoc. Inc., A STUDY OF COMPETITION IN THE U.S. FREIGHT RAILROAD INDUSTRY AND ANALYSIS OF PROPOSALS THAT MIGHT ENHANCE COMPETITION (2009) vol 2 at 10-5 ("estimate of the RPTM/MC ratio peaked at 217 percent in 1994 and has ranged in recent years between 150 and 170 percent"). *See* also Laurits R. Christensen Assoc. Inc., AN UPDATE TO THE STUDY OF COMPETITION IN THE U.S. FREIGHT RAILROAD INDUSTRY (2010) at 4-5.

41. When competing carriers sell differentiated products, the one-lump theory does not apply to an end-to-end merger involving a monopoly carrier and one of the competing carriers.[37] Because their products are not perfect substitutes, the competing carriers in the pre-merger market are able successfully to charge through rates that exceed their marginal costs. As a result, the monopolist cannot unilaterally achieve the monopoly outcome, and may have an incentive to merge with one of the two competing carriers. This basic structure applies to the CPKC merger.

42. In this matter, KCSM is a monopoly carrier for some UP movements originating or terminating in Mexico and KCS controls the Laredo gateway. UP and KCS today provide competing, differentiated service. Therefore, there already are foreclosure concerns involving movements on KCSM before this merger, and the CPKC merger exacerbates these foreclosure concerns. This is because the incremental revenue and profits on the CP segments of current actual and potential movement movements increases the financial gains to the merged firm of foreclosure of UP in the form of higher rates, even if the Laredo gateway is open.

43. In the post-merger market, a merged firm has greater ability to act on its incentive to foreclose unintegrated carriers in order to increase its division for the monopoly segment – to get closer to the monopoly profit it is unable to extract in the pre-merger market. This places upward cost pressure on the unintegrated carrier, which in turn places upward pressure on the carrier's through rate, ultimately harming shippers who prefer this interline movement. This also will permit and incentivize the merged firm to raise its single-line rate, thereby leading to harm to all shippers. Even taking into account the possibility of some EDM effects (which Dr. Majure does not suggest), there is certainly no economic basis for a general presumption that a vertical merger in such a market will be either procompetitive or competitively neutral, and there are strong reasons to expect net anticompetitive effects under the circumstances of the proposed transaction.

3.3.1 Simulation Model Analysis

44. When firms (or rail carriers) in vertically adjacent markets merge, the merger can involve foreclosure incentives that lead to upward pressure on prices. This occurs when the merged firm can cause customers of its unintegrated competitors to divert to the merging partner by raising the cost of using the unintegrated competitors. When one merging rail carrier has a monopoly position on its segment, it can foreclose the unintegrated competitors of its merging partner by eliminating their access to its segment or by raising the division it

[37] Economic analyses of vertical mergers with differentiated products dates back to Joseph J. Spengler, *Vertical Integration and Antitrust Policy*, 58 J. POL. ECON. 347 (1950). For more recent articles, *see* the articles cited in *supra* note 11, among others.

charges the unintegrated carrier for movements on its monopoly segment, or its Rule 11 rate for the segment.

45. In the first instance, the magnitude of the incentive to foreclose depends on the margins of the merging carriers and the diversion ratio from the foreclosed carriers to the merging partner. Foreclosure raises the costs of the carriers competing with the merging carrier, either directly if they pay the increased interline rate or indirectly if the increased interline division is paid by the independent carrier. In either case, foreclosure leads to upward pricing pressure on the rates paid by shippers. The merger also can lead to downward pressure on rates from merger-specific EDM, marginal cost savings or product quality improvements. The magnitude of the downward pricing pressure depends on the magnitude of the merger-specific benefits, as well as the opportunity cost discussed above, which also depends on margins and diversion ratios.[38]

46. The ultimate impact of the merger on shippers depends on the tension and magnitudes of these upward and downward pricing pressures. As a general matter, a vertical merger can lead to a diverse set of outcomes. In some cases, the merger can lead to higher rates borne by all shippers.[39] This is the expected outcome when the merger-specific efficiency benefits are small. The merger alternatively can lead to higher rates borne by the shipper customers that rely on interline movements with the foreclosed independent carriers, while leading to lower rates for the shippers that opt for single-line service by the merged carrier. The merger also can lead to lower rates charged to all shippers. This is most likely to occur when both merging parties have monopoly positions and the merger-specific EDM and merger-specific efficiencies are very large. Because carriers do not set uniform rates for all movements, a vertical merger can lead to a diversity of outcomes across commodity groups, routes and specific shippers.

47. What can be predicted is that the one-lump theory is rejected because the carriers' products and services are differentiated. (As explained above, the one-lump theory also is separately rejected because the carriers have imperfect information.) If there are only de minimis merger-specific EDM, marginal cost savings, and quality improvements, then one can predict with confidence that all shippers likely will be harmed. If there are no competitors on both segments, then one can predict that shippers will not be harmed.[40] But in the middle ground, the multitude of factors that enter into the determination of the impact of the merger on shippers means that it is not possible to make definitive general predictions that

[38] For technical analysis, *see* Moresi & Salop, *supra* note 11.

[39] This was the outcome in the imperfect information model, where the imperfect information plays a analogous role to product differentiation.

[40] However, even this prediction is subject to the caveat noted earlier, *supra* note 26.

all shippers will benefit or that the transaction will be competitively neutral or positive. The facts will matter.

48. With sufficient data, one approach could be to estimate the upward pricing pressure on the through rate for interline movements on unintegrated carriers arising from the foreclosure incentives and, similarly, estimate the downward (or possibly net upward) pricing pressure on the single-line rate of the integrated carrier from the combination of the opportunity cost, merger-specific EDM, and other efficiencies. If the disparity between upward and downward pricing pressure (in either direction) is large, then a confident prediction might be made.[41] In a real-world merger, this prediction could differ across product categories, routes, and shippers. Applicants (and Dr. Majure) did not conduct this analysis.

49. One also could extend this upward and downward pricing pressure analysis by combining those factors into an equilibrium merger simulation model. However, this approach raises the additional complexity of having to assume a specific demand curve and type of competitive interaction among the carriers. Even if the type of demand curve were known, it would be necessary to estimate the structural parameters of demand, which is not simple. It would also be necessary to have detailed information on carriers' margins for both a complete pricing pressure analysis and for simulation modeling. Again, Dr. Majure (and Applicants) did not conduct this analysis.

50. In Section 5, I take a simpler approach to showing the foreclosure concerns from the proposed merger. As described there, I analyze the profitability of a hypothetical total foreclosure strategy by the merged firm, that is, denying UP access to KCSM for movements of finished automobiles and automobile parts between Mexico and Chicago. The merged firm could carry out this hypothetical total foreclosure strategy by raising its rates on interline movements with UP. (While the concern here is more on smaller rate increases than closing the Laredo gateway, the analysis of a hypothetical total foreclosure strategy is a standard, conservative approach to gauging foreclosure incentives. If a hypothetical total foreclosure strategy after a merger is profitable at current rates, that indicates that the merged firm will have an incentive to raise its division or rate charged for the monopoly segment.) That analysis is only illustrative in that it involves only examples of certain movements. It also does not analyze the impact of merger-specific cost savings and quality improvements, although UP witnesses have concluded that those efficiencies are small.[42]

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[41] *See* Moresi & Salop, *supra* note 11. *See* also Serge Moresi & Steven C. Salop, *When Vertical is Horizontal: How Vertical Mergers Lead to Increases in "Effective" Concentration*, 59 REV. IND. ORG. 177 (2021).

[42] Haley V.S. at ¶¶18–36.

51. I have also constructed two versions of a general simulation model that I describe in the remainder of this subsection. They are intended for the limited purpose of showing that the one-lump theory does not apply and that vertical mergers can lead to a wide variety of impacts, even after taking EDM into account. These models demonstrate that there is no economic basis for presuming that end-to-end rail mergers involving a monopoly carrier are procompetitive or competitively neutral. I am not using these simulation models to claim that this particular vertical merger is anticompetitive. Instead, this analysis demonstrates that one cannot use such general simulation models to claim that the proposed merger is procompetitive or even competitively neutral.[43]

52. One version of the model assumes that the carriers quote take-it-or-leave-it prices. The monopoly Carrier A quotes take-it-or-leave-it divisions to the competing Carriers X and Y, and the latter carriers quote take-it-or-leave-it through prices to the shipper, which is a common assumption in economic models of vertical integration. This structure of the model also captures Rule 11 pricing, where the shipper obtains the rates on the monopoly segment (i.e., one rate if the shipper will use Carrier X and a possibly different rate if it will use Carrier Y) and then has a bidding competition between the competing Carriers X and Y, where the information on the monopoly carrier's rates is taken into account. A second version of the model assumes that there is inter-carrier bargaining between the monopoly Carrier A and each of the competing Carriers X and Y over the divisions.

53. The simulation models are designed to capture a variety of demand and cost conditions. These varying demand and cost conditions can be thought of as reflecting the variations in characteristics of shippers, commodities, and origin-destination routes. The simulations thus recognize the effects of a merger may differ across origin/destination markets and commodities.[44] Even within a single origin/destination market for a specific commodity, the fact that the carriers do not set the same rate for every shipper and every movement means

[43] In this regard, I want to emphasize that the models are not calibrated—that is, the values of the demand and cost parameters are not set to replicate any market shares or margins observed in this transaction. For one thing, every market is different. In addition, such calibration would be very difficult, if not impossible, to implement for this merger in an accurate way, and so would be subject to substantial criticisms. For an example of the controversial use of a vertical merger simulation model in litigation, *see* Shapiro, *supra* note 27; *United States v. AT&T, Inc.*, 310 F. Supp. 3d 161 (D.D.C. 2018); *United States v. AT&T, Inc.*, 916 F.3d 1029 (D.C. Cir. 2019).

[44] I also am not claiming that these are the only possible parameter assumptions. I expect that a different set of assumptions or a different demand structure could lead to different results. Such results would not undermine the validity of the conclusions I reach, as the simulation models are intended only to illustrate the diversity of effects of vertical mergers involving a monopoly carrier, the failure of the one-lump theory, and the potentially serious foreclosure concerns that can arise.

that a merger may harm some shippers while benefiting others with different demand characteristics or whose shipments have different costs.

54. The results of the simulation models show that some or all shippers can be harmed from foreclosure effects of end-to-end mergers. They also show the possibility that some shippers can be benefited. Because the simulations cover such a broad range of circumstances to capture different competitive interactions, the models indicate a wide range of possible results for particular shippers. This is precisely the point. While the one-lump theory implies that the price to shippers would not change as a result of a vertical merger when one of the merging parties appears to have a monopoly over certain routes, the simulations show that significant price changes are far from being the exception and, in fact, occur in a broad set of market conditions. Thus, these results make it clear that the one-lump theory does not apply when there is product differentiation in the competitive segment. An end-to-end merger can harm some or all shippers, even after taking any EDM into account. The simulation results thus also make it clear that a general procompetitive presumption cannot be justified with respect to the proposed merger on the basis of economic analysis.

3.3.1.1 Simulation Model with Carrier Take-It-or-Leave-It Pricing

55. The first version of the simulation model analyzes a scenario when the carriers face elastic demand from shippers and set take-it-or-leave-it rates. In the pre-merger market, the monopoly carrier sets divisions to the two competing carriers which then set interline rates. In the post-merger market, the unintegrated and integrated carriers compete for each shipper's movement. The integrated carrier sets a single-line rate and the independent carrier sets an interline rate, which depends in part on the division set by the integrated carrier for its monopoly segment.[45] The simulation model calculates a range of outcomes for a number of demand parameters and costs, which are combined to create a large number of diverse market conditions that lead in turn to a range of pre-merger market shares and rates for the two competing carriers, and divisions for the monopoly carrier. The model follows the railroad literature by assuming that the shippers' demand has a logit demand structure.[46]

[45] The structure of the technical model equivalently assumes that the monopoly carrier offers its service to its merger partner at a nominal price equal to marginal cost and the merger partner sets the through rate for the shipper, although the merger effects do not depend on the magnitude of this nominal transfer price.

[46] Yanyou Chen, *Network Structure and Efficiency Gains from Mergers: Evidence from U.S. Freight Railroads*, Working paper (2021); Daniel Coublucq, *Demand Estimation with Selection Bias: A Dynamic Game Approach with an Application to the US Railroad Industry,* 94 DICE Discussion Paper (2013); Bart Jourquin, *Estimating Elasticities for Freight Transport Using a Network Model: An Applied Methodological Framework*, 9 J. TRANSP. TECH. 1 (2019).

56. The technical details of the model are described in more detail in Appendix C.[47] In some scenarios, the two competing carriers increase their through rates after the merger and, therefore, all shippers are harmed by the merger. In other scenarios, the interline rate of the unintegrated carrier rises while the single-line rate of the now-integrated carrier falls. In this latter scenario, the shippers that use the unintegrated carrier are harmed but the shippers that use the single-line rate are benefited.[48] Specifically, in this model, the single-line rate of the merged carrier rises when the pre-merger volume share of the merging competing carrier is less than about 25%, and often also when its share is in the 25-40% range. But when its pre-merger share exceeds 40%, the single-line rate of the merged carrier typically falls. Thus, this version of the model illustrates how a vertical merger can harm some or all of the shippers, depending on the particular demand and cost conditions. For this reason, a general or conclusive presumption of no anticompetitive effects resulting from a vertical merger in these market conditions, in the context of imperfect information and/or differentiated products, would not be appropriate.

3.3.1.2 Simulation Model With Inter-Carrier Bargaining

57. In a 1982 order, the ICC suggested that inter-carrier bargaining could lead to market conditions that would support application of the one-lump theory.[49] I have also analyzed a version of the model where the divisions charged by the monopoly carrier to the two competing carriers are determined through bilateral negotiations in which the two negotiating parties have equal bargaining power.[50] (By contrast, the previous version of the model, which included take-it-or-leave-it divisions, effectively assumed that the monopoly carrier has all the bargaining power.) As before, the model assumes that the competing carriers set take-it-or-leave-it through rates to the shipper. The simulation results for this

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[47] The simulation model builds on the approach in Gopal Das Varma & Martino De Stefano, *Equilibrium Analysis of Vertical Mergers*, 65 ANTITRUST BULLETIN 445 (2020), which uses the equivalent of through pricing. This article analyzes both take-it-or-leave-it inter-firm pricing and bargaining, as I do in this report. However, that article provides only a single example for demand and cost conditions rather than a range of market conditions. Gleb Domnenko & David S. Sibley, *Simulating Vertical Mergers and the Vertical GUPPI Approach*, (May 15, 2020) https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3606641 also simulates vertical mergers for a range of market conditions, but with a different demand structure and more limited reporting of results.

[48] I am not claiming that it is impossible for both through rates to fall and all shippers to benefit from a hypothetical merger. As I describe in later sections, however, I conclude that the proposed CPKC merger is likely to lead to anticompetitive foreclosure, not lower rates for all shippers.

[49] *Union Pac. Corp. —Control— Missouri Pac. Corp*, 366 I.C.C. 462 (1982).

[50] Economists refer to this as "Nash Bargaining." *See* John Nash, *The Bargaining Problem,* 18 ECONOMETRICA 155 (1950); Ken Binmore, Ariel Rubinstein and Asher Wolinsky, *The Nash Bargaining Solution in Economic Modeling,* 17 RAND J ECON 176 (1986).

bargaining version of the model lead to a variety of pre-merger market shares and rates, as described in more detail in Appendix D.

58. In this bargaining version of the model, the impact of the vertical merger on shippers is more adverse. The merger always leads to an increase in the interline rate charged to shippers who opt for the unintegrated carrier. The merger also almost always leads to an increase in the single-line rate charged to shippers by the integrated carrier. When the single-line rate falls, it decreases only slightly. Moreover, the rate increases typically are larger than those in the previous model where the monopoly carrier sets take-it-or-leave-it divisions.

59. Thus, this inter-carrier bargaining version of the simulation model similarly demonstrates that the one-lump theory does not hold when carriers on the competitive segment offer differentiated products and services. It also indicates serious concerns about shipper harms from foreclosure in markets that have such characteristics. The likelihood and magnitude of shipper harms are higher in this scenario than those in the previous version of the model with take-it-or-leave-it divisions.

3.4 Implications for the Board's Analysis of the Proposed CPKC Merger

60. The economic analysis of vertical mergers carried out in this section shows the inapplicability of the one-lump presumption if the competing carriers are selling differentiated products or if the carriers have only imperfect information about each other's costs and rates. The one-lump theory fails for all but the polar case. Nor can one argue that the world is close to this polar case. Imperfect information and differentiated products are the norm, not the exception. And when there is imperfect information or differentiated products, end-to-end mergers can harm some or all shippers under normal conditions.

61. When the one-lump theory does not apply, there can be incentives to foreclose. Those foreclosure incentives already exist today, because KCS controls KCSM, and they will be enhanced by the merger with CP. This is because adding CP's revenue and earnings increases the financial benefits the post-merger firm will gain by diverting traffic to itself and away from rivals. While EDM might mitigate these foreclosure concerns, the results of the simulation model show how such benefits can and often do fall short. Nor have the Applicants provided any data or analysis to rebut the concerns, which the simulation models support, that the merger could result in anticompetitive foreclosure. Instead, as I discuss further in Section 6 below, Dr. Majure has essentially assumed away foreclosure and apparently has concluded that merger-specific EDM is not important.

4. Modern Economic Analysis Rejects the Assumption that There Is No Incentive or Ability to Foreclose When There Is a Competing Carrier for Each Segment

62. In this section, I briefly analyze the impact of the proposed merger on the portion of the traffic where FXE might be a feasible alternative for the Mexican leg of a rail movement.

63. In his statement, Dr. Majure discusses the situation where the potentially foreclosed rival has an alternative to the merged carrier, and concludes that the merged carrier has no ability (and hence no incentive) to foreclose. However, Dr. Majure does not carry out any actual economic analysis of this issue. Instead, he stops at the assumption that when there is an ostensible perfectly-substitutable alternative routing, this alternative will provide the same effective safeguard against rate increases after the merger as in the pre-merger market.[51] As Dr. Majure puts it,

> Next, consider the other hypothetical shipper, who can readily switch to another railroad or mode of transportation. Perhaps this second shipper can rely on FXE's network in Mexico as a suitable alternative to KCSM for originating its movements. For the shipper with ready alternatives, there would be no *ability* for a combined CP/KCS to force inferior terms on the shipper. Doing so would only lead to loss of the traffic – or failure to attract new traffic – contrary to the company's economic incentives.[52]

64. I understand that many shippers in fact cannot rely on FXE.[53] But, in addition, Dr. Majure fails to take into account that even where the second upstream carrier may provide a practical alternative to the merging carrier, the merger will change the economic incentives of the integrated carrier, as well as those of the unintegrated alternative carrier, in ways that reduce the effectiveness of the competitive safeguards that the alternative carrier provided before the merger.

65. I can explain this result with the following hypothetical scenario drawn from the economics literature. Instead of assuming that a railroad has a monopoly on one segment of a through movement, suppose there is a second carrier on that segment. This scenario is illustrated

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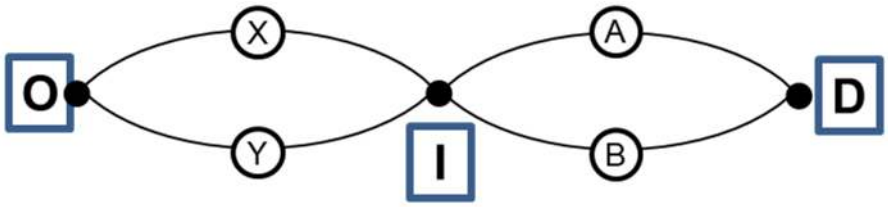
[51] Dr. Majure appears simply to rely on a quotation from the Board's BNSF 1995 merger decision that suggests that a merger will not weaken the "safeguards" provided by alternative carriers. (APP., *Verified Statement of W. Robert Majure* (October 29, 2021) (*hereinafter*, Majure V.S.) at ¶25.)

[52] Majure V.S. *supra* note 51 at ¶25 (emphasis in original).

[53] Rocker & Turner V.S. at 16.

below in Figure 2, where Railroads X and Y compete on the segment from O to I and Railroads A and B compete on the routes from I to D.

Figure 2: Duopoly Competition



66. Assume that Carrier B is not only a feasible alternative to Carrier A, but Carrier B has the same costs and product attributes of Carrier A, so it is a *perfect substitute* for Carrier A, and so there is intense pre-merger competition between Carriers A and B. Consider next the impact of a merger between Carriers A and X. Dr. Majure suggests that the existence of Carrier B would totally deter Carrier A from raising its fee to the unintegrated downstream Carrier Y (or to shippers that want to use Carrier Y).

67. But economic analysis of this simple model indicates that this conclusion is incorrect.[54] Despite the fact that Carrier B is a perfect substitute for the merging Carrier A, the merged carrier would still have a post-merger incentive to raise its division to Carrier Y. This is because the merged carrier would correctly anticipate that Carrier B would respond by raising the division it charges to Carrier Y. (Carrier B similarly would anticipate that Carrier A will have the incentive to raise its division.) This will lead to both carriers charging higher divisions. Thus, even if Carrier Y selects Carrier B for the origin segment, the higher division paid for that interline segment makes it more likely that the merged carrier will win the bidding, even when it sets a higher through rate than before the merger.

68. Thus, it is erroneous to focus solely on the technical "ability" to substitute. It is also necessary to analyze the impact of the merger on the "incentives" to foreclose. The mere technical "ability" to substitute does not eliminate the incentive of the merged carrier to foreclose by raising its division. To assume otherwise, as Dr. Majure appears to do, amounts to assuming that no vertical merger can raise competitive concerns when there are two carriers on both segments (or, more generally, two firms in each market).

[54] *See* Ordover et al., *supra* note 11.

69. When Carriers A and B are perfect substitutes with identical costs and quality, the pre-merger competition drives their rates down to marginal cost, so there is no EDM (put simply, there are no margins for the merger to eliminate). However, if they are imperfect substitutes, the carriers may be able to set pre-merger rates that are higher than their marginal costs, which means that a merger may permit some EDM. But there is no economic reason to think that downward pressure on rates will be the dominant factor. In fact, the greater is Carrier Y's ability to substitute between Carriers A and B, the lower is the likelihood that downward pricing pressure will be the driving factor in the merged carrier's incentives and the more likely it is that the rates offered to shippers by both carriers will rise. Moreover, the more inelastic is the aggregate demand for the service provided by Carriers X and Y, the greater will be the merged firm's opportunity cost of lowering its through rate. The opportunity cost also is higher if Carrier A charges a higher pre-merger rate to the independent Carrier Y than to its future merger partner, Carrier X.

70. Thus, economic analysis does not support a general proposition that an alternative upstream carrier eliminates the risk and potential shipper harms from pricing foreclosure that raises the cost of the unintegrated downstream rival. Even if there is a feasible "ability" to substitute, the merged carrier still may have an incentive to raise the fee it charges its unintegrated downstream competitor. This can lead to harm to shippers who end up paying higher rates and perhaps obtaining less preferred service. To the extent that the merged carrier has higher costs—for example, because it has inferior routings—efficiency also may suffer.

71. The structure of competition between UP and the merged CPKC on shipments to and from Mexico is somewhat more complicated than the hypothetical scenario just analyzed. Even when it is a feasible alternative, FXE is not a perfect substitute for KCSM.[55] KCS also currently has some power to raise its fees to CP on interline shipments, which means that there is potential for EDM if CP and KCSM merge. However, one cannot assume that the downward pricing pressure after such a merger will dominate the upward pricing pressure from foreclosure. In fact, if FXE and KCSM are very close competitors for UP, then foreclosure will tend to be more profitable, because the competition would have driven their pre-merger rates virtually down to marginal cost.

[55] The fact that UP has a partial ownership interest in FXE does not change the results. This is a passive ownership interest. UP does not have any control over FXE's prices. Thus, while UP would take into account that it recovers some fraction of FXE's overcharges on interline movements, that recovery does not make FXE a perfect substitute for KCSM and thus will not eliminate the effects of the foreclosure. Moreover, understanding that UP will "discount" the overcharges in this way gives FXE the incentive to raise its fees by even more than if there were no UP ownership interest.

72. In short, there are substantial foreclosure concerns even for shippers that view FXE as a possible substitute for KCSM. Simply observing that KCSM is not a monopolist, but faces FXE as a feasible alternative—and again, Dr. Majure presents that as a hypothesis, not an established fact—does not eliminate the ability or the incentive of the merged firm to engage in foreclosure strategies against UP on Mexican routes.

5. Empirical Analysis Confirms that the CPKC Merger Raises Serious Foreclosure Concerns

73. Brown and Zebrowski (B&Z) estimate divertible and likely diverted traffic that moves through the Laredo gateway. That is, they estimate a magnitude of traffic that they conclude potentially *could* be diverted from competitors to the merged CPKC. They then judged that a specific fraction of that divertible traffic likely *would* be diverted to the merged carrier as a result of post-merger quality improvements.

74. Figure 3 reports B&Z's estimates of the level of potentially divertible traffic to the merged firm that currently flows over the Laredo gateway as well as B&Z's estimates of likely diversion, with likely diversion being somewhat less than half of the potentially divertible traffic on average. Figure 3 reports the carloads, rather than the associated revenue. This analysis indicates substantial likely diversion, taking B&Z's assumptions at face value that there would be no foreclosure tactics by CPKC.

75. While B&Z assume that there is no foreclosure, their formulation essentially concedes an ability to foreclose by raising rivals' costs of competing interline movements. That is, if an integrated firm with monopoly power on one segment can divert traffic by reducing its own costs, then it normally also can divert traffic by raising its rivals' costs. Reducing its own costs allows the firm to gain traffic by decreasing its prices, while raising rivals' costs allows the firm to gain traffic by causing the rivals to increase their prices. After the merger, CPKC can raise rivals' costs by raising the KCSM rates it charges for interline movements with those rivals.

76. Even taking B&Z's estimates of likely diverted traffic at current rates as a given, the merged firm could further increase the traffic diversion rate by engaging in supplemental foreclosure tactics such as raising KCSM rates on interline movements or non-price foreclosure tactics. If those foreclosure tactics were to drive the diversion up to the level that B&Z viewed as potential diversion, that would involve more than twice the diversion rate they treated as likely. The merged firm has a greater incentive to engage in foreclosure than KCS does currently because shipments diverted from UP will allow the merged firm to capture the carloads (and associated revenue and profit) for the CP segments as well as the KCS segments.

Figure 3: B&Z Estimated Potential and Likely Diversions Through Laredo

Select Traffic Screened as Eligible For Diversion

Total Originated/Terminated at Laredo

	Potential Diversion (Carloads/ Containers)	Likely Diversion (Carloads/ Containers)	Percentage Likely Diverted
Intermodal	{{ }}	{{ }}	{{ }}
Automotive	{{ }}	{{ }}	{{ }}
Metals, minerals and consumer products	{{ }}	{{ }}	{{ }}
Energy, chemicals and plastics	{{ }}	{{ }}	{{ }}
Grain Products	{{ }}	{{ }}	{{ }}
Total	{{ }}	{{ }}	{{ }}

Source: Brown & Zebrowski V.S., workpaper "8 - Diversion Identification.xlsx"

77. Extending B&Z's analysis, a strategy of using foreclosure tactics to cause increased diversion likely would be profitable for the merged firm. I will use the illustrative example of diversion of movements of finished automobiles from Laredo to Chicago. I specifically will undertake the common analysis of evaluating the profitability of a hypothetical total foreclosure strategy of completely denying UP effective access to interlining with KCSM by raising KCSM's rates to prohibitive levels.[56] By this analysis, I am not predicting that CPKC will engage in such a total foreclosure strategy. Instead, I am using this analysis as a conservative gauge of the profitability of foreclosure by raising KCSM's rates.

78. To explain the basic methodology of this profitability analysis, suppose that the merged firm were to substantially raise the per carload rates charged for UP movements from Mexico origins to Laredo to prohibitively higher levels, where UP effectively would be totally foreclosed from using KCSM as a practical matter. To illustrate the impact of this hypothetical total diversion strategy on the profits of CPKC, assume initially in an overly optimistic way that UP were able to retain (say) half the movements subject to this foreclosure by trucking the merchandise to Laredo or using FXE instead, despite the higher cost of these alternatives. In that case, the merged firm would sacrifice the revenue and margin on half of the UP movements over KCSM (i.e., the movements that UP would retain by using trucks or FXE) but it would obtain the revenue and margin for carriage from

[56] Such a profitability analysis is routinely used in merger analysis. *See, e.g.,* Vertical Merger Guidelines (Example 2); Moresi & Salop, *supra* note 11 at 208. The profitability analysis is a conservative approach to foreclosure incentives. *Id.* at 208-10.

Laredo to Chicago on the half of the UP movements that it captures (i.e., the movements that it diverts from UP to itself).[57]

79. To estimate the increase in the revenue earned by the merged firm from this total foreclosure strategy, Figure 4 reports B&Z's estimates of the amount of revenue per carload that the merged firm would earn on movements diverted from UP and other carriers for finished automobile movements. If the merged firm would obtain the current UP rates on the Laredo-Chicago movement on diverted traffic, the merged firm would earn revenue of {{ }}.[58] KCS earns revenue of only {{ }} on KCSM movements that interline with UP at Laredo. Thus, if UP were able to retain as much as half the shipments after it was totally foreclosed from KCSM, the merged firm would gain {{ }} on the U.S. portion on the half of the shipments it captures, while losing the KCSM revenue of {{ }} on the half of the shipments that UP is able to retain. Thus, on balance, the total foreclosure strategy would dramatically increase CPKC's revenue.[59] Assuming that the percentage price/cost margins were not wildly different, the strategy would be highly profitable.[60] For other routes where the potential CPKC revenue gained is higher, foreclosure would be even more profitable.

80. Given these single line and KCSM rates, I next calculate the "critical percentage" of shipments that UP would have to retain in order for the total foreclosure strategy of the merged firm to be unprofitable. The critical percentage is about {{ }} to maintain the

[57] To keep the illustrative example simpler, I assume that BNSF is not a possible alternative carrier for these UP shipments. If it were, the merged firm also could foreclose BNSF from access to these or all Mexican shipments. That would make the analysis more complicated since the rate charged on shipments interlined to BNSF might be somewhat higher than that charged to UP. However, given the huge disparity between gains and losses from the foreclosure strategy, this simplification will not change the results.

[58] The mileage on CPKC would be about 300 miles longer than the UP mileage. However, B&Z assume that the merger would make the CPKC service competitive with UP (absent any foreclosure).

[59] Assuming that UP initially had 200 movements and the merged firm captures 100 of them, the merged firm would earn revenue of {{ }} in total on those 100 movements, while losing revenue of {{ }} on the lost KCSM movements.

[60] To show the profitability despite differential margins with an extreme (worst-case) example, suppose that the dollar margin on the KCSM movement is $1,000 (i.e., about {{ }} rate), while the dollar margin on the Laredo-Chicago movement is only $2,000 (i.e., about {{ }} rate). In this scenario, the merged firm would earn increased profits of $200,000 on those 100 movements gained, while losing profits of $100,000 on the 100 lost KCSM movements for a net increase in profits of $100,000 on those 200 original movements.

same revenue.[61] UP witnesses have explained that such a high retention rate is not viable.[62] While this analysis indicates that the merged firm would increase profits by totally foreclosing UP, it normally is more profitable to raise rates rather than totally foreclose.

81. As noted earlier, I am not suggesting that CPKC would close the Laredo gateway or charge such prohibitive rates so as to completely foreclose UP. Instead, the merger raises serious concerns that the merged firm would partially foreclose by raising KCSM rates on shipments through the Laredo gateway to Chicago and the upper Midwest in order to divert traffic to CPKC to some degree, and possibly also engage in some non-price foreclosure tactics that are difficult to detect.

Figure 4: CPKC Foreclosure Incentives: Finished Automobiles

CPKC Incremental Revenue from a UP Diverted Movement	{{ }}
Average KCSM Revenue for the Mexican Portion of a UP Movement	{{ }}

Sources:
1. Brown & Zebrowski V.S., workpaper "4 - Traffic Screening.xlsx"
2. Brown & Zebrowski V.S., workpaper "8 - Diversion Identification.xlsx"

82. Figure 5 provides a similar analysis for southbound automobile parts from Chicago to Laredo. UP would have to be able to retain at least a "critical percentage" equal to {{ }} of the shipments to prevent this total foreclosure strategy from increasing the net revenue of the merged firm.[63] Again, UP witnesses have explained that such a high retention rate is not viable.[64] And as discussed above, increasing rates by some amount is normally more profitable than totally foreclosing. This also shows a concern that the merger would lead to higher rates charged to UP. And, as with finished automobiles, it will be even more profitable for other movements when revenue gained is higher.

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[61] If UP retained { }} of the carloads, the merged firm's loss of the {{ }} per carload on this {{ }} of the shipments would equal the gain of {{ }} per carload on the {{ }} of shipments diverted by the merged firm. This assumes equal percentage margins on both segments. As noted above, if the percentage margins differ on the two segments, the critical percentage would be adjusted accordingly.

[62] Rocker & Turner V.S. at 11-16.

[63] If UP retained {{ }} of the carloads, the merged firm's loss of the {{ }} per carload on this {{ }} of the shipments would equal the gain of {{ }} per carload on the {{ }} of shipments diverted by the merged firm. This assumes equal percentage margins on both segments. As noted above, if the percentage margins differ on the two segments, the critical percentage would be adjusted accordingly.

[64] *See* Rocker & Turner V.S. at 11-16.

Figure 5: CPKC Foreclosure Incentives: Automobile Parts

CPKC Incremental Revenue from a UP Diverted Movement	{{ }}
Average KCSM Revenue for the Mexican Portion of a UP Movement	{{ }}

Sources:

1. Brown & Zebrowski V.S., workpaper "4 - Traffic Screening.xlsx"
2. Brown & Zebrowski V.S., workpaper "8 - Diversion Identification.xlsx"

83. The Applicants claim that the merger will lead to quality improvements and cost decreases.[65] They might try to argue that these would offset the foreclosure incentives indicated by this analysis. But UP witness Thomas Haley explains that a substantial portion of the single-line cost savings anticipated by Applicants is not merger-related.[66] Further, Mr. Haley explains that Applicants assume traffic will divert to longer, less efficient routes. His testimony suggests Applicants would have to grow their single-line traffic and revenues by foreclosing, rather than by increasing competition. In this regard, while B&Z attribute the diversion to cost and quality improvements, diversion alternatively could be achieved by raising the cost of UP interline movements by increasing the fee charged by KCSM to UP (or to shippers that want to use UP). Rate reductions for the purpose of inducing shippers to switch from UP to CPKC would be unnecessary if the merged carrier foreclosed competing carriers by raising the rate for KCSM's monopoly segment.

84. B&Z also are not claiming that rates on these competing movements will decline. For diverted traffic moving between Mexico and the United States through the Laredo gateway, B&Z apparently attribute all the diversions of traffic to quality improvements, not to rate decreases. This is because they assume that rate reductions are not needed to divert traffic away from UP's interline service on movements through Mexico, even though the diversion will move traffic to longer, less efficient routes. They assume that CPKC would offer rate reductions only "in order to attract traffic away from existing single-line service to CPKC single-line service."[67] Since UP will be interlining with KCSM, it will not be providing single-line service.[68] Thus, B&Z are effectively assuming that the merged firm's rates will

[65] *See*, e.g., APP., *Verified Statement of Dean Vargas* (October 29, 2021) (*hereinafter*, Vargas V.S.) at ¶41, Table 2.

[66] *See,* e.g., Haley V.S. at ¶¶13–17.

[67] Brown & Zebrowski V.S. at ¶32. ("[W]e considered it appropriate to assume that CP/KCS would be required to offer rate reductions averaging five percent in order to attract traffic away from existing single-line service to CP/KCS single-line service.") However, they do not treat movements that include KCSM as single-line. *See* Brown & Zebrowski V.S., workpaper "8 - Diversion Identification.xlsx".

[68] Brown & Zebrowski V.S., workpaper "8 - Diversion Identification.xlsx"

stay the same for all cross-border traffic diverted from UP. This assumption also suggests that shippers will not benefit from lower rates.

6. Dr. Majure's Analysis of Traffic Flows at Laredo Lacks Probative Value

85. Dr. Majure reports data on traffic shares for the northbound traffic that KCSM brought to the Laredo gateway from Mexico in 2019. Dr. Majure asserts that this analysis is "consistent" with the absence of foreclosure incentives at the Laredo gateway,[69] implies a preference for single-line service,[70] and demonstrates the potential benefits to shippers from a combination of CP and KCS.[71]

86. However, Dr. Majure's empirical analysis lacks probative value. This single snapshot of shares in 2019 (15 years after KCS's earlier acquisitions of TFM and TM) is equally consistent with the opposite of what Dr. Majure claims. Based solely on the analysis as presented, one cannot conclude one way or the other whether KCS's earlier acquisition resulted in any foreclosure of UP in the past, or whether the merged firm will foreclose UP in the future. Nor does this data provide evidence of a meaningful preference for single-line service or overall benefits to shippers from the merger.

6.1 Dr. Majure's Traffic Share Data Does Not Disprove the Existence of Foreclosure Concerns

87. In Exhibit 2 of his Verified Statement, Dr. Majure presents shares of northbound rail traffic passing through the Laredo gateway in 2019. Dr. Majure's exhibit is reproduced below in Figure 6.

[69] Majure V.S. at ¶30 ("That sizable percentage is consistent with KCS having an incentive to provide shippers with their preferred route and carrier…").

[70] Majure V.S. at ¶32-33.

[71] Majure V.S. at ¶34.

Figure 6: Reproduction of Dr. Majure's Exhibit 2

{{

}}

88. Dr. Majure reports that in 2019, KCSM interchanged {{ }} of shipments with UP at the Laredo gateway for which KCS can serve the final destination (Line 1 in Figure 6).[72] He claims that this "sizable percentage is consistent with KCS having an incentive to provide shippers [after the previous merger] with their preferred route and carrier – interchanging as necessary to meet the shipper's preference rather than forcing shippers to use KCS alone."[73]

[72] KCS also interchanges {{ }} of shipments with UP destined for areas that KCS cannot serve. (Line 2 of Figure 6). This equality in the percentage of shipments interchanged might be thought to suggest that KCS is not foreclosing any shipments to areas that it can serve. Dr. Majure properly does not make such a claim. This is because the commodity categories, shipment lengths and values and other factors are not constant. Nor is it likely that the equality would be found for apples-to-apples comparisons or for other years.

[73] Majure V.S. at ¶30.

89. This figure lacks probative value. This is because Dr. Majure provides no counterfactual against which to measure this {{ }} result. Without knowing what percent of carloads *would have been interchanged* with UP at Laredo had the KCS/TFM/TM transactions not been consummated (i.e., in the counterfactual "but-for" world), one cannot reasonably conclude that UP's {{ }} share in 2019 indicates that "interchange activity at the Laredo gateway demonstrates a combined CP/KCS would not have the ability and incentive to preclude its rivals' access to gateways."[74] These shares may be inconsistent with a claim of *complete foreclosure* of UP, but they do not establish that there has been *no foreclosure* arising from interline fee increases or higher KCSM divisions. For example, suppose that UP's share would have been 90% absent foreclosure resulting from the previous merger. In that case, a {{ }} UP share would be indicative of substantial foreclosure.

90. One possible benchmark might be to compare UP's share in 2019 to the level before all the effects of previous transactions occurred. That is, one might compare UP's share before the KCS/TFM/TM transaction versus 2019. As shown in Figure 7, UP's share of northbound shipments was 90% before the acquisitions. By 2019, the share had fallen to {{ }}, as discussed above. Similarly KCS share of southbound was only 9% and it is {{ }}much higher today, as shown in Figure 8 below. Thus, this is equally "consistent" with the acquisitions leading to foreclosure of UP.

Figure 7: Pre-KCS/TFM/TM Shares of Movements via All U.S./Mexico Gateways

Railroad	Northbound	Southbound
UP	90%	79%
KCSR/Tex Mex	3%	9%

Source: Kansas City Southern —Control— the Kansas City Southern Railway Company, Gateway Eastern Railway Company, and the Texas Mexican Railway Company, STB Finance Docket No. 34342 at 12 (2004).

91. As Dr. Majure recognized at his deposition,[75] there are other possible explanations that also are "consistent" with the decline in UP's share post-2004/2005 and the corresponding

[74] Majure V.S. at ¶31.

[75] Deposition of W. Robert Majure, February 7, 2022 at 229, ("It's very hard to make that kind of comparison over a long period like this. And in particular, there are a lot of things that have been changing that would affect this. . . So I would expect changes to happen from investments. I would expect changes to happen from—changes in demand over time. . . So even just the composition of what the traffic is is probably changed somewhat. So those are just some of the reasons why trying to do this over time might lead to a misleading conclusion.").

increase in KCS's share, such as secular improvements in KCS service over this period. These alternatives reduce if not totally eliminate the probative value of the change in the shares. But I note that if Dr. Majure's reasoning regarding the {{ }} in 2019 were to be credited, then so must also be this decline from {{ }} in 2004-2005 down to {{ }}. That is, this large reduction in UP's share over time (and the corresponding increase in KCS's share) equally could be said to be "consistent" with foreclosure by KCS.[76]

92. Dr. Majure's apparent conclusion that his Exhibit 2 rebuts foreclosure concerns also ignores the fact that the foreclosure incentives would be increased after the merger because of the incremental revenue earned on the CP portion of movements diverted to the merged firm from the foreclosure. For example, Figure 6 indicates that there are {{ }} movements to areas not served by KCS today that the merged CPKC could serve and for which UP currently obtains a { }} share at Laredo. These movements are ones that the merged firm could divert from UP, BNSF or others by raising the rate for KCSM's monopoly segment. This is another reason why his Exhibit lacks probative value.

93. In addition, because Dr. Majure does not take into account the likelihood and potential harms from foreclosure, his conclusion that the merger likely will benefit shippers on these routes also lacks probative value.

6.2 Analysis of Southbound Traffic Through the Laredo Gateway Does Not Support Dr. Majure's Conclusion that There Are No Foreclosure Concerns

94. Dr. Majure did not analyze southbound traffic through the Laredo gateway in his report. However, there are similar foreclosure concerns relating to southbound traffic: KCSM could increase the rate for southbound movements interchanged with UP at the Laredo gateway in order to increase the cost to shippers of using UP for the U.S. portion of a movement and thereby increase traffic obtained by KCS instead. Figure 8 presents UP and KCS' 2019 shares of southbound carloads interchanged with KCSM at the Laredo gateway in the same format used by Dr. Majure in his northbound analysis. UP's share of southbound traffic (i.e., share of traffic interchanged at the Laredo gateway from areas KCS serves) is only {{ }}, far less than the {{ }} share Dr. Majure found for northbound traffic.

95. Had Dr. Majure analyzed southbound traffic in his report, and if he had applied his rule on northbound traffic that a "sizable percentage [share of UP] is consistent with KCS having an incentive to provide shippers with their preferred route and carrier … rather than forcing

[76] Dr. Majure refers to {{ }} rate of interchange traffic as "consistent with KCS having no ability to force shippers into using KCS." (Majure V.S. at ¶31.)

shippers to use KCS alone,"[77] he then should have concluded that UP's "small" {{ }} share of traffic from areas that KCS serves (versus {{ }} share for traffic from areas that KCS does not serve) is "consistent" with a significant foreclosure concern.[78] Similarly, KCS's "large" {{ }} share of southbound carloads from areas is much higher than the {{ }} of northbound traffic he flagged. Thus, Dr. Majure should have concluded that this high rate indicated that foreclosure was occurring.

96. Of course, these metrics also are subject to the same criticism of Dr. Majure's analysis that I made earlier: these figures do not compare this percentage to an estimated percentage in the but-for world absent the merger.

Figure 8: Shares of Southbound Traffic Interchanged at Laredo Gateway with KCSM

Area	Total Carloads	UP share at Laredo Gateway	KCS Share at Laredo Gateway		
			Total KCS Share [A = B + C]	BNSF to KCS at Robstown or Corpus Christi [B]	KCS share before Robstown or Corpus Christi [C]
KCS serves…	{{ }}	{{ }}	{{ }}	{{ }}	{{ }}
KCS does not serve…	{{ }}	{{ }}	{{ }}	{{ }}	{{ }}
KCS does not serve and CP serves…	{{ }}	{{ }}	{{ }}	{{ }}	{{ }}
… and UP and BNSF do not serve	{{ }}	{{ }}	{{ }}	{{ }}	{{ }}
… and UP or BNSF serves	{{ }}	{{ }}	{{ }}	{{ }}	{{ }}
All traffic through Laredo to Mexico	{{ }}	{{ }}	{{ }}	{{ }}	{{ }}

Sources:
CP-KCS Traffic Tapes, 2019
Confidential Waybill Sample, 2019
CP Intermodal Containers to Railcar Conversion Factor.xls
KCS R-1 Annual Report, 2019

[77] Majure V.S. at ¶30.

[78] Dr. Majure writes that he did not report these southbound traffic figures because "[w]hile UP's concern could have applied to southbound traffic as well, I test the effect on the northbound traffic as I can readily categorize movements of this traffic in terms of whether an interchange with another railroad happened as early in the movement as feasible." Majure V.S. at note 17. However, the primary statistic needed for the southbound analysis is UP's share in areas KCS serves, which can readily be calculated using a definition for "serves" focused on origin points that is comparable to the termination points used in the northbound analysis.

6.3 Dr. Majure's Data Do Not Provide Evidence of a Preference for Single-Line Service

97. Dr. Majure also suggests that the data reported in Figure 6 above demonstrate a shipper preference for single-line service.[79] Dr. Majure specifically points to the fact that KCS has a higher share at the Laredo gateway when it is able to provide single-line service beyond Laredo/Robstown/Corpus Christi ({{ }}, as shown in line 1) than it does for traffic bound for areas where KCS could not deliver to the ultimate destination ({{ }}, as shown in line 2). However, just as it is not possible to draw a conclusion about foreclosure in the absence of an estimate of the outcome absent the merger, it also is not possible to draw a conclusion about shipper preferences for single-line service from Dr. Majure's Exhibit 2. This higher share could have been the result of foreclosure rather than preference for single-line service or some other product differentiation or cost factor.

98. Other data do not indicate a strong preference for single-line service. For example, Figure 9 reports northbound carload shipments through Laredo to Kansas City for finished automobiles. KCS *single-line* movements accounted for only {{ }} of finished automobiles from Laredo to Kansas City, whereas UP *interline* movements accounted for {{ }} of these shipments. Thus, these percentages do not indicate a strong preference for single-line service provided by KCS.

Figure 9: Northbound Finished Automobile Shipments through Laredo to Kansas City-2019

Routing Railroads North of Mexican Border	Total Carloads	Share
KCS Total	{{ }}	{{ }}
KCS-BNSF	{{ }}	{{ }}
KCS	{{ }}	{{ }}
UP Total	{{ }}	{{ }}
UP	{{ }}	{{ }}
Total	{{ }}	

Source: Brown & Zebrowski V.S., workpaper "4 - Traffic Screening.xlsx"
Note: Movements with railroad routing "KCS-NS" are grouped with movements with railroad routing "KCS".

[79] Majure V.S. at ¶32. ("That difference, {{ }} percent [KCS share] where KCS could offer a single-line service compared to {{ }} [KCS share] where they could not, suggests that shippers have a preference for single-line service.").

6.4 Dr. Majure's Flawed Argument that There Are No "Pre-Existing Constraints" on Foreclosure

99. At his deposition, Dr. Majure suggested that it was important to identify whether there was an "unexploited pre-merger way to influence competition that becomes feasible to implement as a result of the merger."[80] He identified this as "one of the conditions for when a vertical merger might have an anticompetitive effect."[81] He also testified that he reached "the conclusion that they don't have any unexploited power in a way that might be unlocked by a merger."[82] In its Response to CSX Interrogatory 27, Applicants' counsel fulsomely described Dr. Majure's statement as demanding identification of a "pre-existing constraint" that prevents CP and/or KCS from engaging in conduct that would lessen competition absent the merger, and that there is a "credible mechanism" by which the merger would make the constraint "no longer bind," so that "unexploited potential to impair competition could be realized" after the merger.

100. Stated more simply, Dr. Majure and the Applicants suggest that it is necessary for the Board or opponents to identify pre-merger constraints on successful foreclosure conduct and explain how the merger would relax or eliminate these constraints. As noted above, Dr. Majure testified that he was unable to identify any such constraints.

101. But such pre-merger constraints are not difficult to identify here. There are legal and economic reasons why CP and KCS would improve their ability to engage in successful anticompetitive conduct by merging rather than cooperating absent the merger. These reasons are the pre-merger constraints that are relaxed or eliminated by the merger.

102. Consider the scenario of foreclosure of UP by KCSM. Absent the merger, it is conceivable that CP and KCS/KCSM could strike a foreclosure contract by which CP would compensate KCS in consideration of KCS engaging in conduct to raise the costs of UP and BNSF for their interline movements (e.g., by raising KCSM rates or delaying shipments of UP and BNSF) in order to cause some shippers to divert to CP/KCS interline movements. The profitability analysis in Section 5 explains that this foreclosure would increase the combined profits of CP and KCS/KCSM. Thus, one might hypothesize that they could reach a mutually beneficial deal to share the profits absent the merger and thus the merger would not have incremental foreclosure effects. Stated differently, this reasoning might be assumed to imply that there is no pre-merger constraint that the merger would unbind.

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[80] *See, e.g.,* Majure Deposition at 90.

[81] *Id.*

[82] *Id.* at 71.

103. However, this would-be pre-merger contract would face an obvious *legal constraint*. The agreement would violate Section 1 of the Sherman Act. As stated, it amounts to a naked exclusionary agreement that would harm competition and competitors. The parties similarly would be in legal jeopardy—in light of both antitrust and STB constraints —if they re-framed the pre-merger contract to make CP the exclusive interline partner of KCS, since the contract would likely harm shippers. These legal constraints are a clear "pre-existing constraint" that would (in the Applicants' words) "limit the feasibility of arrangements CP and/or KCS could have, as separate entities, to align their respective incentives and abilities in a fashion that would lessen competition."[83]

104. This would-be pre-merger agreement also would face an *economic constraint* from the combination of private information and related strategic bargaining incentives of the two parties. CP and KCS/KCSM would have to agree on how to divide the increased profits from the foreclosure. In that negotiation, each side would have the incentive to understate its benefits and overstate its costs in order to claim a larger share of the anticompetitive pie.[84] As a result, they may well fail to reach an agreement, even ignoring legal constraints on such an agreement such as the Sherman Act and other legal restrictions. (Of course, these legal constraints make agreeing on relative costs and benefits and arranging for the side payments even harder, given the need to avoid detection.) The merger solves this problem of private information and strategic bargaining incentives by permitting open communication and eliminating the need to allocate the gains between the two separate parties. Indeed, the Applicants make the analogous argument about such information/bargaining constraints in explaining why CP and KCS would be unable to achieve the claimed efficiency benefits absent the merger.[85]

105. Similar informational/bargaining incentive constraints also would constrain CP and KCS from achieving the foreclosure benefits the merger allows that I discussed in Section 3.2. That section explains how the vertical merger leads to information exchange between the merging Carriers A and X and how that information sharing permits the merged Carrier A/X profitably to raise the division quoted to Carrier Y, while in turn causing shippers to pay higher rates on average. In principle, Dr. Majure might postulate that Carriers A and X could have cooperated in the pre-merger world by exchanging the requisite information and sharing the higher profits. However, this information sharing would be constrained by the

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[83] KCS and CP's Supplemental Joint Responses and Objections to CSXT's Second Set of Discovery Requests, Response to Int. No. 27.

[84] This is a standard constraint when bargaining parties have private information. It has been used to explain why parties do not always settle litigation in advance of spending enormous sums, why there are wars, and other more mundane examples of two parties failing to reach a mutually beneficial agreement.

[85] Brooks V.S. at ¶¶28-36.

same sort of private information/strategic bargaining incentives constraints as above. Each party would have the incentive to misrepresent in order to get a large share of the profits. This is not simply a theoretical constraint. As UP witnesses Rocker & Turner have explained, UP and other carriers maintain confidentiality over their Rule 11 rates quoted to shippers and do not share them with other carriers.[86] Moreover, rational shippers would have the incentive to prohibit such information sharing that would lead to higher rates.

106. Finally, it is important to add that Dr. Majure makes the assumption that there is no foreclosure today, and that any foreclosure incentives are neutralized by the KCS previous and current commitments. However, as discussed above, his claim of no-foreclosure is unsupported, due to the fact that he made no effort to identify what would have occurred in the but-for world absent KCS's acquisition of the Mexican rail assets, as he conceded in his deposition.[87] An assumption that the KCS current commitments also would prevent significant foreclosure by CPKC is flawed because it ignores the fact that CPKC's post-merger incentives to evade adherence to the commitments in order to foreclose are greater than KCS's standalone incentives. This is because the merged firm will capture the larger combined revenue and profits from the foreclosure, as discussed in Section 5. That is, there will be a greater post-merger incentive to evade whatever pre-merger constraints occur from the commitments (or constraints from any other pre-merger impediments that might not be observable to outsiders). And in light of how difficult it must be is to detect violations of the rate commitments (as discussed in the next section), it also follows that foreclosure risks are increased by the merger.

7. A Specific Commercially Reasonable Rule 11 Rate Methodology for CPKC's Monopoly Segments Can Avoid Foreclosure Concerns

107. In this section, I discuss a commercially reasonable Rule 11 rate formula to address foreclosure concerns raised by the merger.

7.1 Applicants' Commitments are Vague and Insufficient

108. The analysis in this report confirms that there are significant anticompetitive foreclosure concerns raised by the merger. Dr. Majure suggests that CP has made commitments sufficient to prevent any foreclosure. As he explains, "CP's willingness to make the same sort of commitments adopted by KCS at Laredo [in the KCS-KCSM merger]. . . " means

[86] Rocker & Turner V.S. at 9-10. *See* also Deposition of John Brooks, February 4, 2022, at 51-52.

[87] Majure Deposition at 102-107.

that "CP/KCS should be expected to interchange traffic even where it can offer an enhanced service if the shipper, nevertheless, prefers a different routing or wants to use a different carrier."[88]

109. Applicants have stated a commitment, through CP's Executive Vice President and Chief Marketing Officer John Brooks, to maintain Laredo as an open gateway, pursuant to a previous commitment that KCS made in 2003 with its acquisition of what became KCSM.[89] By "open" gateway, Mr. Brooks states first that CPKC will maintain the "operational efficiency" of gateways like Laredo "to maintain efficient operations… wherever traffic levels warrant—in terms of both the through train services to and from the gateways as well as the operational capabilities and infrastructure necessary to carry out efficient interchange."[90]

110. Applicants have also committed generally to maintaining the "commercial viability" of gateways like Laredo, such that "when a customer requests a rate for only the former-CP or former-KCS portion of an origin-to-destination routing, we will provide the shipper with a Rule 11 rate to the gateway."[91] By this commitment, Mr. Brooks states that "we will not make it impossible to construct viable interline options for shippers by refusing to quote commercially reasonable rates."[92]

111. However, this pricing commitment is vague and incomplete. Mr. Brooks' statement does not define either "viable" or "commercially reasonable rates." Nor is it clear whether this commitment applies to KCSM rates to-or-from the Laredo gateway. Without a firm understanding of what this rate entails, the commitment is meaningless.

112. This concern about the vagueness of CP's commitments is buttressed by some of the ambiguities in Mr. Brooks' Verified Statement, which includes many of the promises summarized above but which also raises additional questions. Importantly, Mr. Brooks distinguishes between interlining (a) on routes where the combined CPKC "will not reach" and where they will "obviously" maintain their ability to interchange efficiently (e.g.,

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[88] Majure V.S. at ¶38.

[89] Brooks V.S. at ¶¶35, 42. Brooks further states that "CP also looks forward to stepping into KCS's shoes to continue cooperating with UP on interline traffic over the important Laredo gateway."

[90] Brooks V.S. at ¶45.

[91] Brooks V.S. at ¶46.

[92] *Id*. "Commercial viability" is not the same as "commercial reasonableness." Mr. Brooks' "commercial viability" standard would appear to allow CP to attempt to engage in margin squeezes by raising its Rule 11 rates for its segment of interline movements. That standard would allow substantial single-line rate increases by the integrated carrier, to the detriment of shippers.

interchange with UP at the Kansas City gateway serving Powder River Basin coal)[93] and (b) traffic that either CP or KCS interchange today but that CPKC can potentially "serve better" with their integrated routing post-merger (e.g., service from Mexico through Laredo to the Upper Midwest).[94] Regarding the latter, Applicants offer only a "promise" not to try to foreclose non-integrated competitors that customers may prefer to use because "that would hurt us in the long run by damaging the value of our brand as a promise of customer value."[95] This suggests that Applicants understand the difference between routes on which there might be an incentive to foreclose an interline "competitor," and those with an interline "partner" where this incentive is missing. Yet Applicants make only vague promises not to foreclose competitors, and those are premised only on maintaining CPKC's brand value with customers. This type of commitment is flatly insufficient to protect competition and shippers.

113. Applicants have conceded the fact that its commitments are insufficient. In its letter to the NITL, CP explained this insufficiency as follows:

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}}[96]

114. KCSM states that it sets rates to all users on a non-discriminatory basis.[97] However, a commitment for KCSM to charge the same nominal rate for shipments that interchange with UP at the Laredo gateway as for the same or similar shipments that interchange with KCS

[93] Brooks V.S. at ¶39. Brooks also refers to these as "friendly" connections—i.e., ones where each partner needs the other to serve the customer. Brooks V.S. at ¶28.

[94] Brooks V.S. at ¶40.

[95] *Id*.

[96] Letter from CP to National Industrial Transportation League (June 25, 2021) (CP-HC-00000851-854) at ¶¶2-3.

[97] KCS and CP's Joint Responses and Objections to UP's First Set of Discovery Requests, Response to Request No. 63. ("All Commercial rates are to be offered to shippers in a non-discriminatory manner. As a result of the interplay of these laws, if KCSM provides one shipper with a rate from Mexico to the Laredo gateway, it must in general also provide other shippers with a similar rate.") KCS and CP's Joint Responses and Objections to UP's Third Set of Discovery Requests, Responses to Request Nos. 176, 186.

would not prevent foreclosure.[98] KCS (or CPKC) can achieve an effective price foreclosure goal by setting a high nominal rate for KCSM that raises UP's costs to whatever level is desired and then setting whatever KCSM/KCS (or CPKC) through rate as desired by adjusting the Rule 11 rate on the KCS segment in the US or the single-line rate.[99] KCS has this discretion. It explains that it sets rates on the basis of numerous factors "including but not limited to the market, operating and cost considerations, the type of service, volume, risk premiums (such as hazardous materials or high end commodities), asset availability, network capacity, competitive modes of transportation, and regulatory requirements."[100] At the same time, KCS has discretion because the portion assigned to KCSM vs. KCS would be purely an accounting matter for the combined corporation.[101]

115. Indeed, Applicants have essentially conceded that it would be impossible for UP (or the Board) to determine whether KCSM's current rates are reasonable or not. As Applicants' attorneys explained in response to UP's Motion to Compel,

> The Board did not define "commercially reasonable" in its 2004 Tex Mex decision. See Tex Mex Decision at 19. There are no set metrics; there are no dollar caps. There is no ruler by which UP could even determine, at this later date and with full hindsight, whether a particular rate offered for one customer in 2019 for intermodal traffic between Mexico City and Kansas City is "commercially reasonable" without wild speculation.[102]

116. A commitment that is not easily enforceable because it lacks any metrics or any basis on which to evaluate compliance offers no protection to competition or shippers.[103] Only an administrable and enforceable methodology for setting and determining commercially reasonable rates for interline movements can mitigate the risk of anticompetitive foreclosure.

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[98] This same basic analysis applies to shipments that interchange with BNSF at Corpus Christi or Robstown.

[99] *See, supra* note 97 at No. 168. KCS and CP's Joint Responses and Objections to UP's Second Set of Discovery Requests, Response to Request No. 148.

[100] *Id.*

[101] It is possible that tax consequences could differ. However, this likely would be a second-order effect.

[102] Applicants' Reply To UP's Motion to Compel (Feb. 7, 2022).

[103] *See*, e.g., Antitrust Division, Department of Justice, MERGER REMEDIES MANUAL (September 2020) at 8, 16.

7.2 A Proposed Commercially Reasonable Rate Formula for CPKC Monopoly Segments

117. The Board should consider the following methodology for the determination of commercially reasonable Rule 11 rates for KCSM movements to-and-from the Laredo gateway. I refer to this methodology as the Competitively Reasonable Rate (CRR) formula. Under the CRR formula, when a shipper asks CPKC for a single-line rate for the portion of a movement served by CPKC and a Rule 11 rate solely for the monopoly portion, CPKC would set KCSM's Rule 11 rate as a prorated percentage of the merged firm's single-line rate for the entire movement. In the case of UP movements involving the Laredo gateway, the CPKC monopoly portion would be the portion from the Mexican origin or destination point to the Laredo gateway. In the case of BNSF movements, the CPKC monopoly portion would be the portion from the Mexican point to the BNSF interchange point at Robstown or Corpus Christi. The prorated percentage in the CRR formula would be set equal to the ratio of the KCSM miles (or the KCSM and KCS miles, in the case of BNSF movements) to the KCSM/KCS/CP single-line miles from the origin to the destination (or to an interchange with another carrier).

118. To illustrate, suppose that CPKC quotes a through rate of $6000 for a class of merchandise for movements from its origin station in Mexico to Chicago. Suppose that the KCSM miles from the origin station to the Laredo gateway represents one-third (i.e., 33.3%) of the miles for the merged firm's full movement to Chicago. In that case, the CRR for KCSM's share of the movement to the Laredo gateway would be $2000 (i.e., 33.3% x $6000). These rates would be disclosed to the shipper, not to the competitors of the merged firm.

119. To paraphrase the Applicant's language that "when a customer requests a rate for only the former-CP or former-KCS portion of an origin-to-destination routing, we will provide the shipper with a Rule 11 rate to the gateway,"[104] the CRR might be phrased as follows: when a shipper requests a rate for CPKC service on only the former-CP or former-KCS/KCSM portions of an origin-to-destination route and a rate for CPKC single-line service on a competitive route, the merged firm must provide a Rule 11 rate for the former-CP or former-KCS/KCSM portions that reflects a mileage-based prorate of its single-line rate. The prorate would be equal to the ratio of (a) the miles of the merged firm from the origin point to the interchange point to (b) the miles of the merged firm from the origin to the

[104] Brooks V.S. at ¶46.

interchange *plus* the miles of the merged firm from the interchange point to the destination point.[105]

120. This CRR formula has several advantages over other more complex methodologies.[106] First, the administrative costs are low. The CRR is straightforward for the merged carrier to calculate and implement. Compliance also can be easily monitored by the shipper, which will be given both rates by the merged CPKC. Thus, it can be enforced the shipper itself. It similarly is simple for the Board (or an arbitrator) to resolve disputes under this approach, unlike the great complexity and interminable disputes associated with efforts to actually estimate the relevant marginal costs of the two segments and other factors.[107] Second, the CRR protects competition. It ensures access to commercially reasonable interline rates; it prevents the integrated carrier from engaging in a margin squeeze against the interline carrier; and it does not permit the unintegrated carrier automatically to see the single-line rate. Third, the CRR does not regulate the single-line rate; it simply sets the Rule 11 rate on the monopoly segment in accordance with CPKC's own rate decisions.

7.3 The CRR Formula Will Not Reduce Competition

121. Applicants might attempt to argue that the CRR formula will force rate equalization and deter rate reductions driven by lower costs in the same way as the now-discredited DT&I

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[105] The Applicant's Michael R. Baranowski has not suggested that KCSM's operating costs should be treated as exceeding KCS's cost. As he stated, "I also assumed, based on high-level comparisons of KCS and KCSM costs per unit of output that KCS URCS costs are a reasonable surrogate for KCSM costs for diverted volumes. (APP., *Verified Statement of Michael R. Baranowski* (October 29, 2021) (*hereinafter*, Baranowski V.S.) ¶22 at 415.) Applying the MSP adjustment avoids any argument that CPKC would be disadvantaged by the CRR methodology.

[106] These complex alternatives might include a specified mark-up over some measure of costs; the rates charged before the merger, adjusted for objectively measured cost and other changes; rates charged on other comparable routes unaffected by the merger; etc. These alternatives all involve judgment calls (e.g., the level of the mark-up; the particular routes or historical period used as benchmarks; any other factors used to adjust rate levels). As a result, they involve higher administrative cost and complexity that also could lead to more disputes and an inability to resolve these disputes quickly.

[107] Allowing the CPKC the discretion to base the division on its own estimate of the relative costs of the two movements would effectively permit it to set a very high rate for the interline segment under the guise of it being reasonable under the circumstances. In its responses to discovery, KCS states that it assigns revenue divisions between KCS and KCSM "based on the circumstances particular to the move, including but not limited to mileage divisions, operating cost considerations, overall base costs (such as higher fuel costs in Mexico or additional security needs), WACC differences in the United States and Mexico, and regulatory requirements (such as TUCE (Max) rate considerations in Mexico)" KCS and CP's Joint Responses and Objections to UP's Second Set of Discovery Requests, Response to Request No. 148. This approach would be impossible for the shipper or a third party to evaluate easily in real time, but rather would lead to more disputes that would be difficult to resolve in an accurate or timely way.

conditions. However, this criticism is not well-founded. This is because the CRR is far narrower than the DT&I conditions[108] and is formulated to preserve competition among the carriers. In particular, the CRR does not constrain the single-line rate of the merged firm; it simply bases the Rule 11 rate on the monopoly segment of the carrier's independently-determined rate. Nor does the CRR require a negotiation with the competing interline carrier.

122. Applicants also might argue that the CRR formula will reduce competition by diminishing its incentive to reduce its rates in response to cost savings achieved by the merger. While it is the case that reductions in CPKC's single-line rates will lead to some reductions in the CRR, the CRR will not reduce competition for several reasons.

123. First, this argument overlooks the fact that the goal and impact of the CRR is to prevent price foreclosure that would otherwise occur, and which would lead to *higher* single-line rates and *higher* rates charged on interline routes. As demonstrated by the economic analysis presented in this report, CPKC will have the ability and incentive to foreclose unintegrated competitors by raising its rates for its portion of interline movements that would allow it to raise its single-line rates. By preventing that foreclosure, competition will be maintained, not deterred.

124. Second, any reduction in the Rule 11 rate caused by the CRR will amount to only a fraction of the reduction in the single-line rate. For example, suppose that CPKC were to reduce its costs by $100 and decided to reduce its single-line rate by $50, taking the other $50 as an increase in its margin. If its monopoly segment accounted for one-third of the mileage of the total movement, the CRR would fall by $15. Even if the interline competitor passed on this entire $15 fee reduction, it would not be able to match CPKC's single-line rate reduction. Thus, CPKC could still gain more business and a higher margin.

[108] Rulemaking Concerning Traffic Protective Conditions In Railroad Consolidation Proceedings, 366 I.C.C. 112 (1982).

VERIFICATION

I, Steven C. Salop, 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 February 27, 2022.

/s/ Steven C. Salop

Appendix A. Professor Salop's Curriculum Vitae

ADDRESS Georgetown University Law Center

600 New Jersey Ave., N.W.

Washington, D.C. 20001

(202)253-5431(mobile)

salop@law.georgetown.edu

https://www.law.georgetown.edu/faculty/steven-c-salop/
https://papers.ssrn.com/sol3/cf_dev/AbsByAuth.cfm?per_id=68535

PERSONAL Born, December 23, 1946; Married to Judith R. Gelman, three children; U.S. Citizen.

FIELDS OF SPECIALIZATION

Industrial Organization, Competition and Antitrust Policy, Economics of Information, Economic Analysis of Law.

DEGREES

Ph.D.	Economics, Yale University, 1972
M. Phil.	Economics, Yale University, 1972
B.A.	University of Pennsylvania, 1968

AWARDS

AALS Antitrust Section Lifetime Achievement Award (2019);

AAI Antitrust Achievement Award (2010);

Summa Cum Laude, with Honors in Economics, University of Pennsylvania, 1968;

Schoenbaum Prize in Economics, University of Pennsylvania, 1968;

NSF Graduate Fellowship, 1968-72;

Phi Beta Kappa, 1968.

EMPLOYMENT EXPERIENCE

Professor of Economics and Law, Georgetown University Law Center (at GULC since August 1981).

Guest Scholar, Brookings Institution, 1990-1991.

Visiting Professor, Massachusetts Institute of Technology, Spring 1986.

Visiting Interdisciplinary Professor, Georgetown University Law Center, July 1981-June 1982.

Associate Director for Special Projects, Bureau of Economics, Federal Trade Commission, January 1980-June 1981.

Assistant Director for Industry Analysis, Bureau of Economics, Federal Trade Commission, September 1979-January 1980.

Deputy Assistant Director for Consumer Protection, Bureau of Economics, Federal Trade Commission, December 1978-September 1979.

Economist, Division of Consumer Protection, Bureau of Economics, Federal Trade Commission. July 1978-December 1978.

Visiting Professor, Department of Economics, University of Pennsylvania, September 1977-June 1978.

Economist, Office of Economic Analysis, Civil Aeronautics Board, September 1977-July 1978.

Economist, Federal Reserve Board, July 1972-September 1977.

Adjunct Professor, Department of Economics, George Washington University, September 1975- January 1978.

PUBLICATIONS

Books and Reports

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"Economic Reasoning for Lawyers: Cases and Materials" (2010)

SELECTED PROFESSIONAL ACTIVITIES

Co-Chair, Georgetown Global Antitrust Enforcement Symposium (2013- present)

ABA Antitrust Masters Course (2016, 2014, 2012, 2010)

American Antitrust Institute (AAI) Advisory Board

ABA Antitrust Presidential Transition Taskforce (2012)

Associate Editor, JOURNAL OF INDUSTRIAL ECONOMICS (1997-2000)

Advisory Committee, FTC Hearings on Global and Innovation-Based Competition (1996).

Associate Editor (Industrial Organization), JOURNAL OF ECONOMIC PERSPECTIVES (1987-1993).

ABA Antitrust Task Force on Second Requests (1990).

Advisory Board, Georgetown Project on Treble Damages (1986-1987).

Associate Editor, JOURNAL OF INDUSTRIAL ECONOMICS (1983-1988).

Associate Editor, INTERNATIONAL JOURNAL OF INDUSTRIAL ORGANIZATION (1984-1989).

Secretary, Antitrust Section, American Association of Law Schools (1983-1984).

Memberships: American Economic Association, American Bar Association, Phi Beta Kappa.

Nominating Committee: American Economic Association, 1982.

Economics Editorial Advisor, JOURNAL OF CONSUMER RESEARCH, 1982.

OTHER ACTIVITIES

Senior Consultant, Charles River Associates

President, Salop Economics Inc. (1982-present)

Board of Directors, Charles River Associates (1998-2008)

Board of Trustees, The Lowell School (1989-1995)

Appendix B. Numerical Example of Foreclosure with Imperfect Information

The analysis of pre-merger and post-merger competition can be illustrated with a numerical example where the shipper obtains through rates from the competing carriers. The results do not depend on the specific parameter values of the example.[109] As in the example of the one-lump theory (see paragraphs 36–39 above), suppose that the shipper's reservation price is $400 and that demand is inelastic (say, equal to 1 unit) for any price below $400. However, assume now that instead of the competing carriers each having a cost of $100, their costs for the specific movement for the specific shipper may be different and may fall anywhere (independently and uniformly) within a range of $50 to $150, so that the cost of either competing carrier is equal to $100 *on average*, but may differ for a particular shipper's movements. Assume further that neither competing carrier knows the other's cost and, more importantly, that the monopoly carrier does not know the costs of the competing carriers. To show the effect of imperfect information in the simplest context, one can continue to assume that the monopoly carrier's cost is $150 and that the competing carriers know this cost.[110] Furthermore, when the competing carriers bid for the shipper's movement, one can assume for simplicity that they each observe the division that the monopoly carrier has quoted to the other competing carrier.

Under these conditions, in the pre-merger market, each competing carrier will offer a through rate to the shipper that depends on its own total cost, its expectations about likely rates offered by the other competing carrier, and the bid process used by the shipper.[111] The total cost of a competing carrier includes the division quoted by the monopoly carrier, which I discuss further

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[109] Moresi et al., *supra* note 28, demonstrates that the one-lump theory is rejected under general conditions when the monopoly carrier has imperfect information regarding the competing carriers' costs and the shipper has inelastic demand up to its maximum reservation price. The numerical example presented in this appendix is consistent with that article, and the equilibrium prices reported here were calculated using the formulas provided in the article.

[110] If the monopolist's costs also vary, the analysis is more complicated. But the one-lump theory still does not apply.

[111] In the formal model of Moresi et al., *supra* note 28, the carriers' "offers" are their "best" (i.e., minimum) price offers. The shipper chooses the carrier by running sequential bid rounds where each carrier continues to lower its prices until one of the carriers drops out. A carrier will drop out rather than bid below its costs. Thus, in this situation, the winning bidder will be the carrier with the lower cost realization. But it will be paid a price above its own costs, at a level just below the cost of the other, higher cost carrier. For example, if the two carriers have costs of $80 and $120 respectively for a particular movement, the $80 cost carrier will win the competition and be paid a price of $119.99, that is, approximately $120. In technical economic terms, this is equivalent to what economists denote as a "second price" auction. However, as shown in that article, the main post-merger results are the same in the scenario where the carriers make sealed-bid offers, what economists denote as a "first price" auction, and the pre-merger results have the same expected value.

below. Each competing carrier thus will offer a through rate to the shipper that depends on its costs for the specific movement and will have an incentive to offer a higher through rate in situations where its costs are higher. The shipper will then choose the movement with the lowest through rate.

The monopoly carrier bases its own division quotes on its imperfect information about the competing carriers' likely costs and mark-ups. To illustrate, suppose that the monopoly carrier knows that the competing carriers have costs in the $50-$150 range, but does not know the actual costs or resulting contributions to the through rate each will bid to the shipper in its through rate offer. It would not make economic sense for the monopoly carrier to set a division higher than $350. If it did, the competing carriers would be unable to offer through rates that do not exceed the shipper's reservation price of $400, even at the minimum cost of $50.

Applying the analysis in the Moresi et al. article, the monopoly carrier will quote a division to each competing carrier of $283.33 to maximize its *expected profits*.[112] Each competing carrier would then form its own through rate offer to the shipper using this quote from the monopoly carrier, along with its own cost and its expectations of the cost and resulting rate of the other competing carrier. Note that, if a competing carrier's cost is higher than $116.67 (which is possible since costs are anywhere between $50 and $150), then that carrier will not bother to bid since it cannot offer a through rate below the shipper's reservation price of $400. However, if both competing carriers have costs below $116.67, then the winning bid is less than $400 and thus the shipper will obtain some "surplus" value. For example, if the through rate paid is $390, the shipper will obtain a surplus of $10 (i.e., $400 - $390). But if the costs are sufficiently high – say, each competing carrier has a cost of $120 – then the two competing carriers will not be able to offer rates below the shipper's reservation price of $400, and so the shipper will go elsewhere.

To summarize, competition in the pre-merger market with imperfect information leads to the shipper obtaining a through rate below its reservation price some fraction of the time, in particular, when the competing carriers' cost realizations are relatively low. When their cost realizations are higher, the shipper either pays its $400 reservation price for the rail transport or chooses the alternative. Combining the effects of the various possible cost realizations for particular movements, the average through rate paid by the shipper (conditional on the shipper using rail transport) will be less than its reservation price. The monopoly carrier is unable to extract the full monopoly profit margin, contrary to the one-lump theory. Instead, some of the surplus accrues to the shipper and the competing carriers.

Consider next the effect of a vertical merger between the monopoly carrier and one of the competing carriers on the other segment. After the merger, the vertically-integrated carrier

[112] The pre-merger equilibrium division of $283.33 is obtained using the formula in Moresi et al., *supra* note 28.

offers a division to the independent competing carrier, and then the two carriers bid through rates to the shipper. However, when the now-integrated monopoly carrier quotes the division to the independent competing carrier, it does so based on the perfect information it now has about the cost of its merger partner and – as before – on the imperfect information it has about the cost and through price offer of the unintegrated competing carrier.[113]

One possible strategy is for the integrated carrier to offer a full monopoly single-line rate of $400 to the shipper and a prohibitively high division to the independent carrier that makes it impossible for the independent carrier to offer a through rate that does not exceed the shipper's $400 reservation price. Since the independent carrier's costs are no less than $50, the monopoly carrier can quote a division of $350 or more, in which case the through price offered by the independent carrier to the shipper necessarily will exceed $400. An equally profitable alternative would be to offer a division to the independent carrier such that the merged firm would earn the same profit margin from the division as it would from its single-line rate of $400. For example, if the costs of the merged carrier for the entire movement are $270 (i.e., $150 incurred by the monopoly carrier and $120 incurred by the merging competing carrier), it could earn profit of $130 (i.e., $400 - $270) by winning the movement at its single-line rate of $400. Alternatively, the merged carrier could quote a division of $280 to the independent carrier; the latter would win against the single-line bid of $400 whenever its cost realization is smaller than $120 (i.e., $400 - $280) and the merged carrier would earn a profit of $130 (i.e., $280 - $150) regardless of which carrier wins the bidding competition.

But a more profitable strategy is for the monopoly carrier to offer a single-line price to the shipper of $400 and quote a division to the independent carrier that is somewhat higher (i.e., between $280 and $350 in the above example) and will assure that the monopoly carrier earns a *larger* profit (than $130) if the independent carrier wins the interline movement than the monopolist would earn if it won the single-line bid at $400. To illustrate, suppose the costs of the merged carrier for the entire movement are $270 (as before) and the monopoly carrier quotes a division to the independent carrier of $315.[114] If the independent carrier's costs exceed $85, then it will not be able to bid a through rate of less than $400 and still cover its costs, in which case the merged firm will win the movement at a single-line rate of $400 and earn profits of $130 (i.e., $400 less its costs of $270). But, if the independent carrier's costs are below $85, then the merged firm would earn profits of $165 (i.e., $315 minus its costs of $150) on the interline segment (since the independent carrier has sufficiently low costs to offer a through rate below $400). For example, if the independent carrier has costs of (say) $80, it would have total costs of

[113] The single-line rate offered by the merged carrier to the shipper accounts for "elimination of double marginalization" (EDM) incentives from the merger.

[114] The post-merger equilibrium division of $315 is obtained using the formula in Moresi et al., *supra* note 28.

$395 (i.e., $80 + $315 for the interline segment) and in principle could offer a through rate between $395 and $400. It would have the rational incentive to offer a through rate of just below $400, say a rate of $399 (or even $399.99). This is because it would properly anticipate that the merged firm was offering a single-line rate of $400. Thus, the independent carrier could offer a rate of $399 (or $399.99) to the shipper and still win the movement. As a result, the shipper would pay a total through rate of virtually $400.

To summarize, the vertical merger harms the shipper. The shipper pays a total through rate of $400 if the cost realization of the unintegrated competing carrier is $85 or above, and a rate of virtually $400 if the competing carrier's cost is less than $85. These $400 rates are equal to the shipper's reservation price, so the shipper obtains zero surplus. Thus, after the merger, the shipper always pays $400 for rail transport (in which case it obtains no surplus).[115] By contrast, the shipper sometimes does obtain a positive surplus in the pre-merger world as a result of the imperfect information. This occurs when the costs of the competing carriers are relatively low so that the winning rate is less than the shipper's reservation price.

The merger harms the shipper by improving the information available to the merged carrier and, in this numerical example, gives the merged carrier an incentive to foreclose the independent carrier by raising the interline fee from $283.33 to $315.[116] Post-merger, the rate paid by the shipper will never be less than $400 (or $399.99). The higher rate resulting from the merger also leads the profits of the monopoly carrier and its merger partner to rise, relative to their pre-merger profits.

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[115] In this numerical example, the highest cost realization of a competing carrier is $150 and the cost of the monopoly carrier is $150, and therefore the maximum total cost is $300, which is smaller than the shipper's reservation price of $400. It follows that, post-merger, the shipper always obtains at least one bid at $400 (from the merged carrier). Moresi et al., *supra* note 28, also consider situations where the maximum total cost is higher than the shipper's reservation price, in which case post-merger the shipper sometimes does not obtain any bid and must use an alternative transport mode.

[116] In general, the division quoted to the independent carrier can increase or decrease post-merger. *See* Moresi et al., *supra* note 28, Proposition 3. However, the shipper is nonetheless always harmed.

Appendix C. Equilibrium Simulation Model With Upstream Monopoly and Differentiated Products, Downstream Duopoly: Take-It-or-Leave-It Offers

This technical appendix describes the first equilibrium simulation model.

C.1. Description of the Merger Model

In the model, there are two rail transport segments. The monopoly segment is served by a single monopolist carrier, referred to as Carrier A. The competitive segment is served by two competing carriers, referred to as Carriers X and Y. Shippers use these carriers for their through movements. There are thus two competing rail options for a shipper. One option is to use Carriers A and X, and the other option is to use Carriers A and Y. The model assumes that shippers view these two options as non-homogeneous, differentiated transport services.

In the pre-merger market, Carriers A, X, and Y each sets its rate to maximize its own profit. The model formally assumes through pricing both pre-merger and post-merger.[117] It further assumes that Carrier A quotes divisions for its segment to the two competing Carriers X and Y. Given these divisions offered by Carrier A, the competing Carriers X and Y offer through rates to shippers.

In the post-merger market, Carriers A and X operate as a single vertically-integrated Carrier A/X, that sets a single-line rate to the shipper and a division to Carrier Y, in order to maximize its total profits from the two segments. The model assumes that Carrier A/X quotes a division for its monopoly segment to Carrier Y, and then the two Carriers A/X and Y compete by offering through rates to the shipper.[118]

There are two common technical interpretations of shipper demand in this model. One interpretation is that there are numerous shippers with the same general disutility from price, but with idiosyncratic preferences for carriers, so that not all shippers select the same competing carrier. Under this interpretation, each of the two competing carriers faces a demand function that measures the total demand for its services and that depends on the two through rates set by both competing carriers. A second interpretation is that the carriers have imperfect information about the shipper's preferences. Under this interpretation, each of the two competing carriers faces a "demand function" or a winning probability function that measures the probability that

[117] The model also captures Rule 11 pricing when the shipper obtains the rate on the monopoly segment before the competing carriers set their competitive quotes.

[118] The model follows the basic approach in Das Varma & De Stefano, *supra* note 47. *See* also Domnenko &. Sibley, *supra* note 47.

the carrier will be selected by the shipper and that depends on the two through rates offered to the shipper.[119]

In addition, there also are two technical interpretations of the structure of the shippers' bid requests and the associated bidding competition. One interpretation is that each shipper specifies the total volume it wants to ship, runs a "first-score" auction for all of its volume, and each of the two competing carriers submits a (sealed) bid for the shipper's entire volume.[120] Under this interpretation, each of the two competing carriers faces a winning probability function and rates are total payments for the specified volume. EDM here reflects the fact that a lower bid to the shipper leads to an increased probability of winning the shipper's business. Another interpretation is that each of the two competing Carriers X and Y (or A/X and Y after the merger) posts its unit rate (e.g., per carload) and then, based on the posted unit rates, a shipper with particular preferences for a volume of shipments chooses which carrier to use and how much volume to ship.[121] Under this interpretation, each of the two competing carriers faces a demand function for its transport services that is "downward sloping" (such that a higher price yields lower demand), and rates are per unit of volume shipped.[122]

The simulation model is run for many different values of the demand and cost parameters, so as to generate a range of pre-merger market shares (or winning probabilities) and prices, and a variety of merger effects on prices of rail transport services.[123]

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[119] Quoting a lower rate increases the probability of winning.

[120] A first-score auction generalizes a first-price auction by allowing carriers to offer differentiated products and allowing shippers to choose the product with the highest score (i.e., utility net of price). A first-score auction where non-price product characteristics are fixed is equivalent to a Nash-Bertrand pricing game where shippers select only a single product, as is the case under a standard logit demand structure. *See* Nathan H. Miller, *Modeling the Effects of Mergers in Procurement*, 37 INT'L J. IND. ORG 201 (2014).

[121] Under this interpretation, shippers' behavior is somewhat different than in the standard logit model since they choose both a carrier and a volume. (In the standard logit model, all shippers want to ship one unit and each shipper chooses a single carrier to transport that unit.) Nevertheless, the model assumes that the competing Carriers X and Y face demand functions that have a logit-like shape.

[122] Post-merger, one can think of the monopoly carrier (Carrier A) transferring its service internally to the merger partner (Carrier X) at a nominal price equal to marginal cost, although the merger effects do not depend on the magnitude of this nominal transfer price.

[123] By contrast, Das Varma & De Stefano, *supra* note 47 consider only a single numerical example.

C.2. Description of the Simulation Analysis

The simulation model is formulated as a two-stage game:

> Stage 1. Carrier A sets the divisions that Carriers X and Y must pay to Carrier A for transport services on Carrier A's monopoly segment. Carrier A sets the divisions to maximize its own profit. (Post-merger, Carrier A/X sets the division that Carrier Y pays for transport services on the monopoly segment. Carrier A/X maximizes its total profits, i.e., the total profits of former Carriers A and X.)
>
> Stage 2. Carriers X and Y compete for the shippers' business by simultaneously setting through rates.[124] Each carrier seeks to maximize its own profit. (Post-merger, Carriers A/X and Y simultaneously set through rates. Carrier A/X sets its single-line rate to maximize its total profits, i.e., the total profits of former Carriers A and X.)

The pre-merger model is solved using backward induction. This involves deriving the equilibrium rates set by Carriers X and Y (in stage 2), for any given divisions set by Carrier A (in stage 1), and then deriving the equilibrium divisions, assuming that Carrier A correctly anticipates how changing the divisions would affect the through rates of the two competing carriers and hence their volumes of transport on the monopoly segment. The post-merger model also is solved in a similar way using backward induction.

The model assumes that shippers have heterogeneous preferences over the carriers' services. Following the railroad literature, the model assumes that carriers face demand functions (or winning probability functions) that have a logit structure.[125] The model further assumes that each shipper has three shipping options available: Carrier X and Carrier A; Carrier Y and Carrier A; and an alternative mode of transport for the entire through movement. Under the logit structure, the first two options are called the "inside goods" and the third option is called the "outside good."

The model captures the heterogeneous preferences of shippers by using the standard discrete choice modeling approach and applying it to a large number of different bidding competitions. Each bidding competition is different because there are many different through movements (e.g., different origins and destinations) and many different product categories. As discussed earlier, each bidding competition can be interpreted as involving either a large number of heterogeneous shippers or a single shipper with preferences that are unknown to the competing carriers. Thus, a

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[124] The model assumes that Carriers X and Y engage in standard Bertrand-Nash competition with differentiated products and perfect information about each other's cost and demand functions.

[125] *See* Yanyou Chen, *Network Structure and Efficiency Gains from Mergers: Evidence from U.S. Freight Railroads*, Working paper (2021)

shipper may have a preference for Carrier X over Carrier Y, even if both carriers charge the same through rate, while a different shipper may have a preference for Carrier Y over Carrier X.[126]

For each bidding competition, the utility of a shipper from using Carrier X or Carrier Y depends on (i) a demand "fixed effect" that is specific to the carrier (V_X or V_Y) and is the same for all shippers; (ii) the through rate charged by the carrier (p_X or p_Y); (iii) a "price coefficient" (b) that is the same for all shippers and captures the shippers' marginal utility of income and affects the elasticity of demand faced by the carriers; and (iv) an idiosyncratic preference shock (e_{jX} or e_{jY},) that captures each shipper's personal preferences. The utility from using the outside good is, without loss of generality, normalized to a shock e_{j0} (i.e., the systematic component of the utility for the outside good, which is common across shippers, is normalized to zero).

The underlying demand structure can be summarized as follow:

- The utility of shipper j from using Carrier X is given by: $U_{jX} = V_X - b*p_X + e_{jX}$
- The utility of shipper j from using Carrier Y is given by: $U_{jY} = V_Y - b*p_Y + e_{jY}$
- The utility of shipper j from using the outside good is given by: $U_{j0} = e_{j0}$

The model is solved for the following parameter values in order to generate a very broad range of results:

- Three possible values for each of the two fixed effects V_X and V_Y (i.e., 8, 12, and 16);
- Three possible values for the price coefficient b (i.e., 0.05, 0.075, and 0.1);
- Three possible values for each of the two unit costs of production incurred by the two competing Carriers X and Y (i.e., 20, 25, and 30).
- Three possible values for the unit cost of production incurred by the monopoly Carrier A (i.e., 5, 7.5, and 10).
- The "preference shocks" $\{e_{jX}, e_{jY}, e_{j0}\}$ are distributed over $[-\infty, +\infty]$ with Gumbel (extreme value) distribution and are independent of each other.[127]

[126] *See* Steven T. Berry, *Estimating Discrete-Choice Models of Product Differentiation*, 25 RAND J. ECON. 242 (1994); Jeffrey M. Perloff & Steven C. Salop, *Equilibrium with Product Differentiation*, 52 REV. ECON. STUD. 107 (1985); Simon P. Anderson, André De Palma, & Jacques-François Thisse. *Demand for Differentiated Products, Discrete Choice Models, and the Characteristics Approach, 56* REV. ECON. STUD. 21 (1989).

[127] This is a standard assumption. *See, e.g.,* Gregory J. Werden and Luke M. Froeb, *Unilateral Competitive Effects of Horizontal Mergers*, in Paolo Buccirossi (ed.), ADVANCES IN THE ECONOMICS OF COMPETITION LAW (2006).

It follows that the simulation analysis comprises a total of 729 different combinations of the demand and cost parameters (i.e., $3^6 = 729$). Each combination can be thought of as corresponding to a different bidding or price competition.

C.3. Simulation Model Results

The simulation model generates a sample of pre-merger equilibrium outcomes ("pre-merger bidding or price competitions"). For each pre-merger outcome, the simulation model computes the post-merger equilibrium outcome and calculates the merger effects on prices.

The simulation results can be summarized as follows. These results are then illustrated in the Figures below.

a. Result 1: The merger of Carriers A and X always leads the vertically-integrated Carrier A/X to increase the division (W_Y) charged to the unintegrated Carrier Y.

b. Result 2: The merger of Carriers A and X always leads to an increase in the through rate (P_Y) that carrier Y charges to shippers.

c. Result 3a: The merger of Carriers A and X tends to lead to an increase in the through rate (P_X) that the merged Carrier A/X charges to shippers when the pre-merger volume share (S_X) of merging Carrier X is less than about 25%, and often also when that share is in the 25-40% range.

d. Result 3b: The merger of Carriers A and X tends to lead to a decrease in the through rate (P_X) that the merged Carrier A/X charges to shippers when the pre-merger volume share (S_X) of the merging Carrier X exceeds about 40%, and sometimes also when that share is in the 25-40% range.

The following Figures show these results. Each dot represents a different bidding or pricing competition (with a different set of cost and demand parameters).

Figure C1 shows (on the vertical axis) the post-merger percentage changes in the division (W_Y) charged to the unintegrated Carrier Y for all the various values of the pre-merger equilibrium volume share (or winning probability) of merging Carrier X implied by the model (on the horizontal axis).[128] To make it easier to read, Figure C2 shows the same results but restricts attention to bidding or pricing competitions where Carrier X has a pre-merger equilibrium volume share (or winning probability) smaller than or equal to 50%. Figure C3 and Figure C4

[128] The shares (or winning probabilities) are calculated excluding the outside good.

respectively show the post-merger percentage changes in the through rates (P_Y and P_X) that the unintegrated Carrier Y and the merged Carrier A/X charge to shippers.

Figure C1

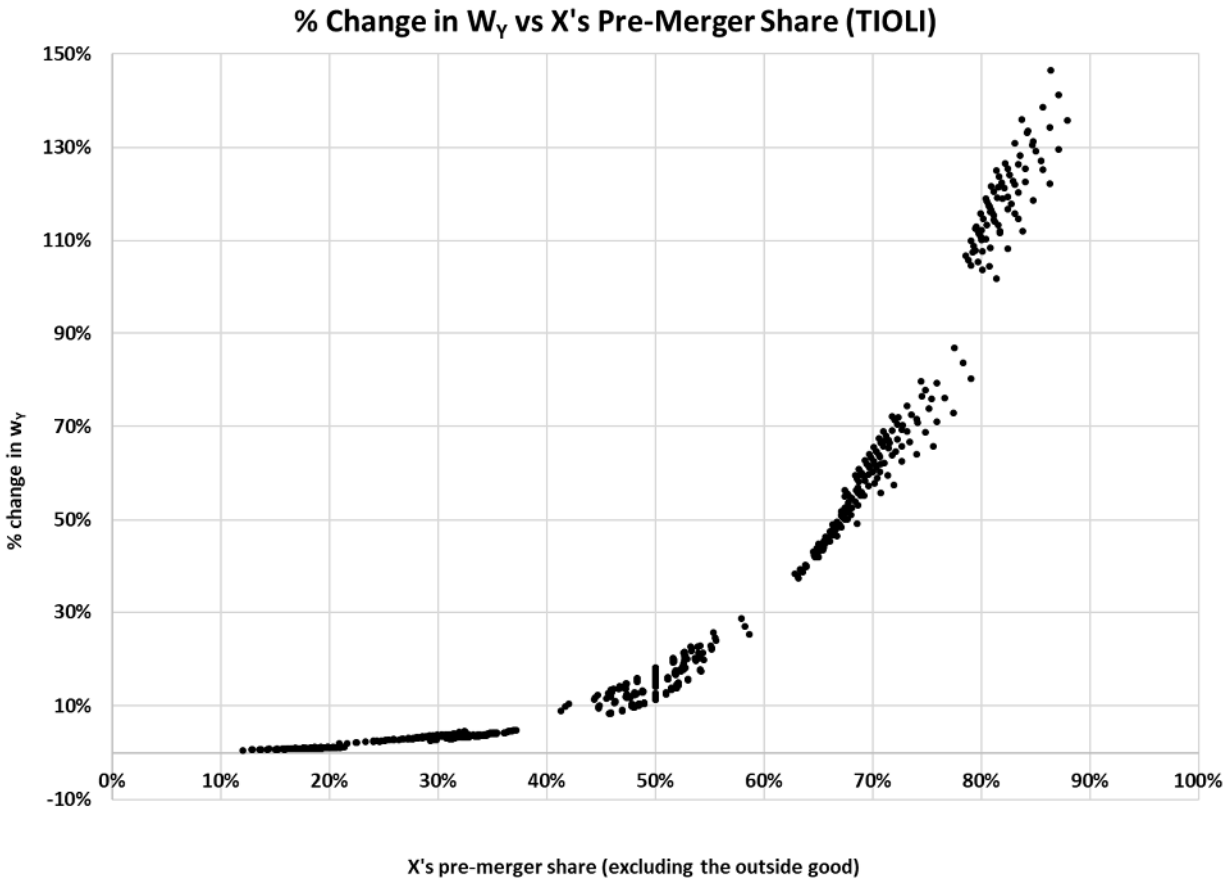

% Change in W_Y vs X's Pre-Merger Share (TIOLI)
150%
130%
110%
90%
70%
50%
30%
10%
-10%
% change in w_Y
0%
10%
20%
30%
40%
50%
60%
70%
80%
90%
100%
X's pre-merger share (excluding the outside good)

Figure C2

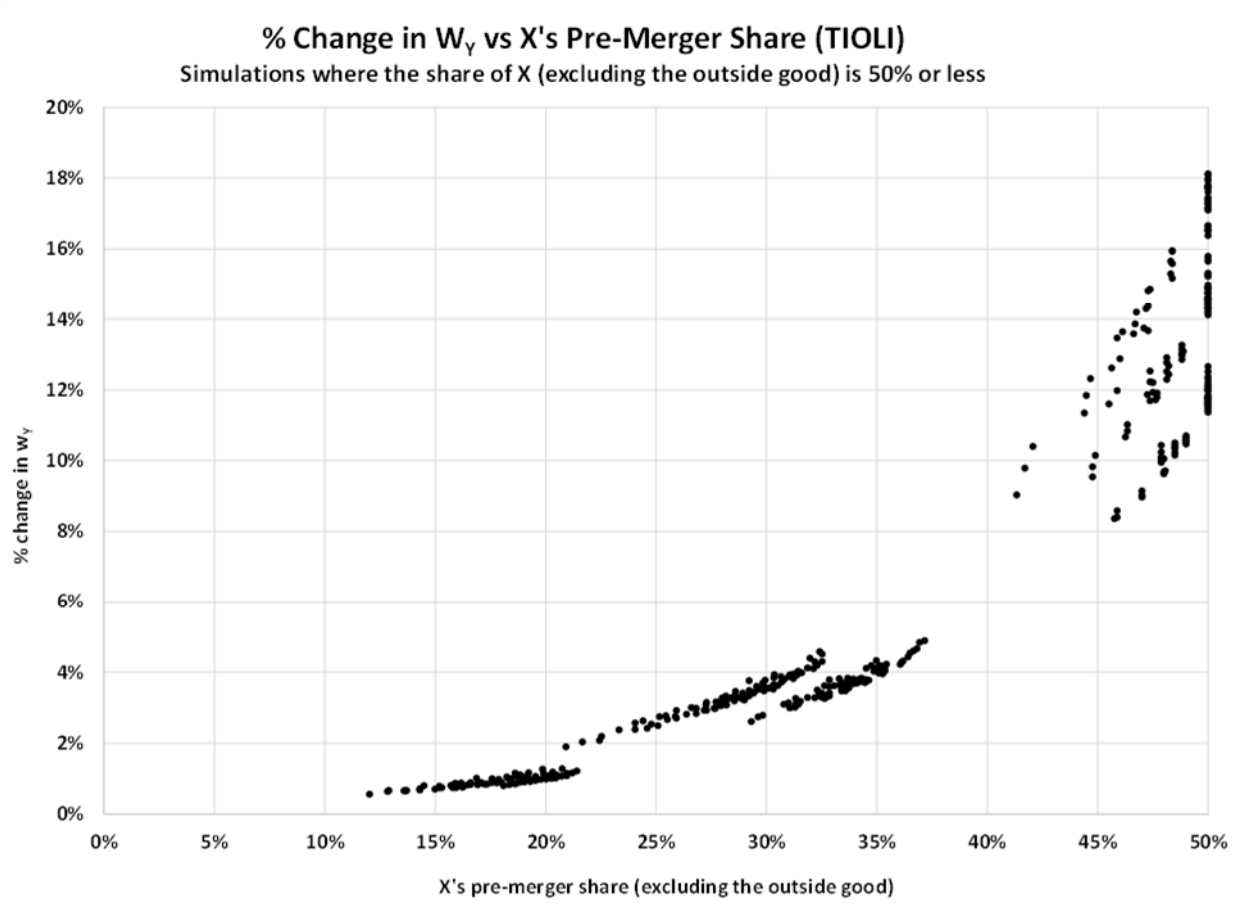

% Change in W_Y vs X's Pre-Merger Share (TIOLI)
Simulations where the share of X (excluding the outside good) is 50% or less
% change in w_Y
20%
18%
16%
14%
12%
10%
8%
6%
4%
2%
0%
0%
5%
10%
15%
20%
25%
30%
35%
40%
45%
50%
X's pre-merger share (excluding the outside good)

Figure C3

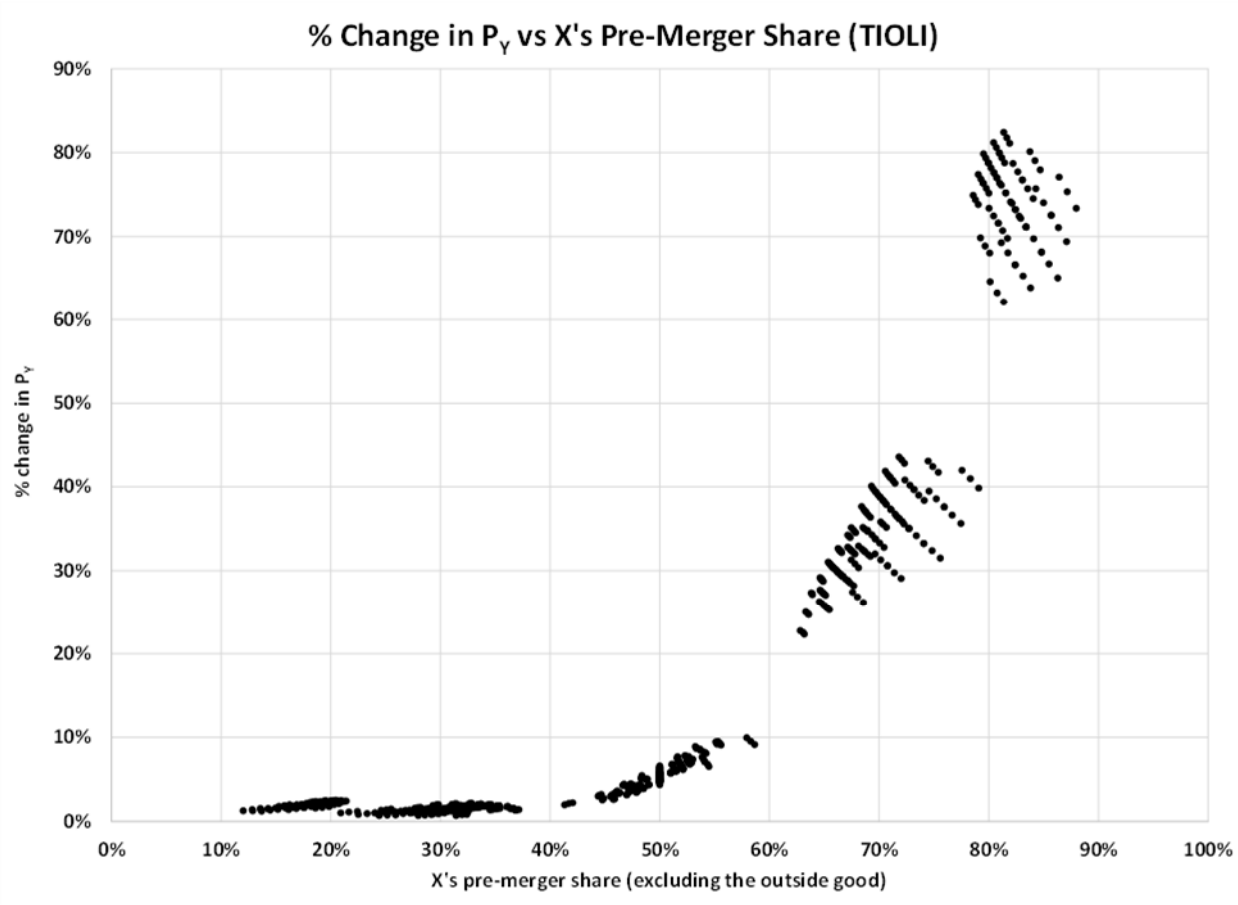
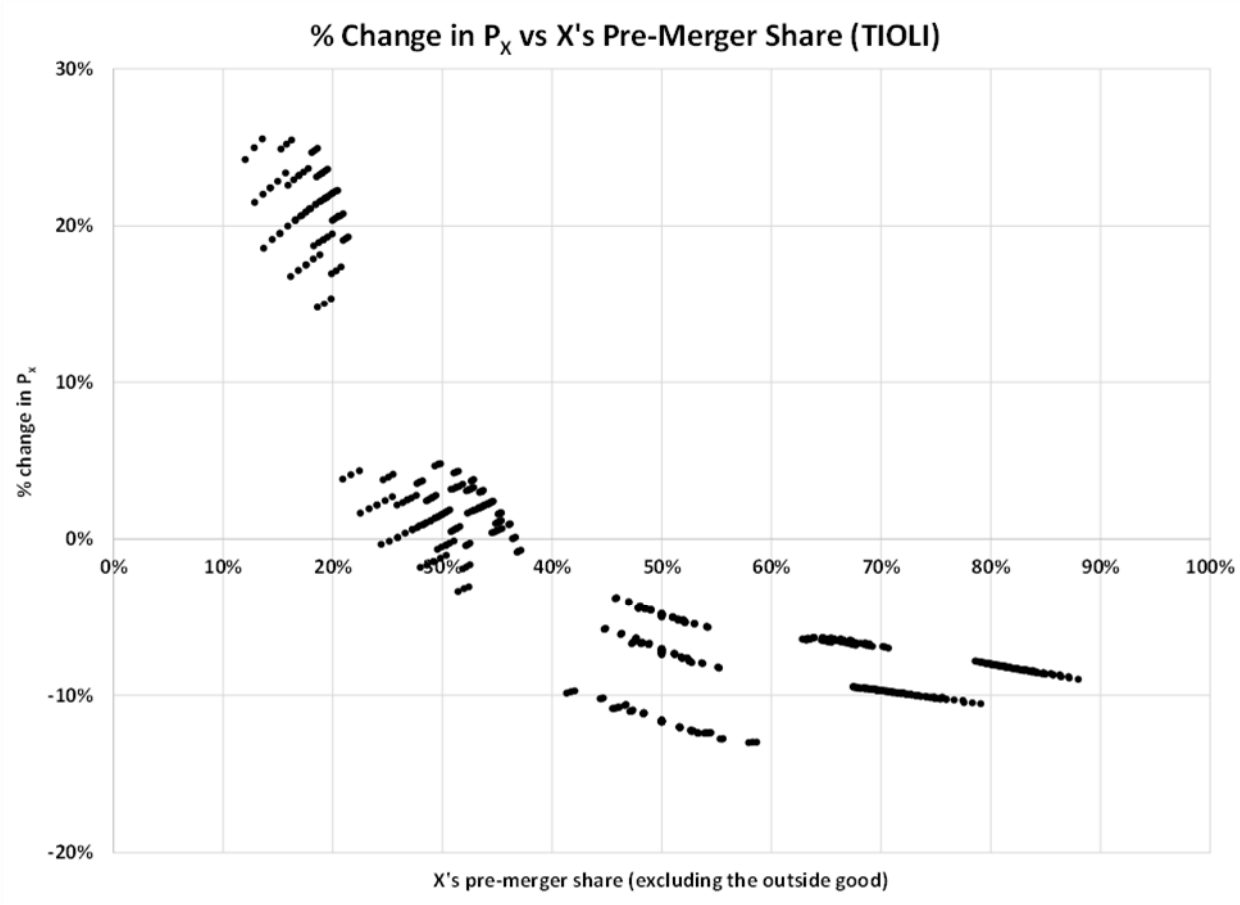

% Change in P_Y vs X's Pre-Merger Share (TIOLI)
% change in P_Y
90%
80%
70%
60%
50%
40%
30%
20%
10%
0%
0%
10%
20%
30%
40%
50%
60%
70%
80%
90%
100%
X's pre-merger share (excluding the outside good)

Figure C4


% Change in P_X vs X's Pre-Merger Share (TIOLI)
30%
20%
10%
0%
-10%
-20%
% change in P_x
0%
10%
20%
30%
40%
50%
60%
70%
80%
90%
100%
X's pre-merger share (excluding the outside good)

Appendix D. Equilibrium Simulation Model With Upstream Monopoly and Differentiated Products, Downstream Duopoly: Inter-Carrier Negotiations

This appendix describes the variant of the equilibrium simulation model described in Appendix C with inter-carrier negotiations. Since many assumptions are the same in the two models, I will focus mainly on the differences between the models.

D.1. Description of the Merger Model

In the pre-merger market, Carriers A and X negotiate the division for Carrier X's through movements, and at the same time Carriers A and Y negotiate the division for Carrier Y's through movements. Given these negotiated divisions, the competing Carriers X and Y offer through prices to shippers.

In the post-merger market, Carriers A/X and Y negotiate the division for Carrier Y's through movements, and then the two Carriers A/X and Y compete by offering through rates to the shipper.

D.2. Description of the Simulation Analysis

The simulation model is formulated as a two-stage game:

Stage 1. Carrier A simultaneously negotiates bilaterally with each of Carriers X and Y over the division for each carrier's through movements. (Post-merger, Carriers A/X and Y negotiate the division for Carrier Y's through movements.) The model assumes that negotiating carriers have equal bargaining power.[129]

Stage 2. Same as in Appendix C.

The pre-merger model is solved using backward induction. This involves deriving the equilibrium rates set by Carriers X and Y (in stage 2), for any given divisions negotiated between Carrier A and Carriers X and Y (in stage 1), and then deriving the equilibrium divisions negotiated among the three carriers, assuming that all three carriers correctly anticipate how changing the divisions would affect the through rates of the two competing carriers and hence

[129] I use the standard Nash-in-Nash bargaining assumption. *See*, for example, Allan Collard-Wexler, Gautam Gowrisankaran, and Robin S. Lee, "*Nash-in-Nash*" *Bargaining: A Microfoundation for Applied Work*, 127 J. POL. ECON. 163(2019).

their volumes of transport on the monopoly segment and the competitive segment. The post-merger model also is solved in a similar way using backward induction.

The model is solved for the same sets of parameter values as in Appendix C.

D.3. Simulation Model Results

The simulation model generates a sample of pre-merger equilibrium outcomes ("pre-merger bidding or price competitions"). For each pre-merger outcome, the simulation model computes the post-merger equilibrium outcome and calculates the merger effects on prices.

The simulation results can be summarized as follows. These results are then illustrated in the Figures below.

- Result 1: The merger of Carriers A and X always leads to the vertically-integrated Carrier A/X negotiating a higher division (W_Y) with the unintegrated Carrier Y.

- Result 2: The merger of Carriers A and X always leads to an increase in the through rate (P_Y) that carrier Y charges to shippers.

- Result 3: The merger of Carriers A and X almost always leads to an increase in the through rate (P_X) that the merged Carrier A/X charges to shippers.

The following Figures show these results.

Figure D1 shows (on the vertical axis) the post-merger percentage changes in the division (W_Y) negotiated with the unintegrated Carrier Y for all the various values of the pre-merger equilibrium volume share (or winning probability) of merging Carrier X implied by the model (on the horizontal axis). Figure D2 shows the same results but restricts attention to bidding or pricing competitions where Carrier X has a pre-merger equilibrium volume share (or winning probability) smaller than or equal to 50%. Figure D3 and Figure D4 respectively show the post-merger percentage changes in the through rates (P_Y and P_Y) that the unintegrated Carrier Y and the merged Carrier A/X charge to shippers.

Figure D1

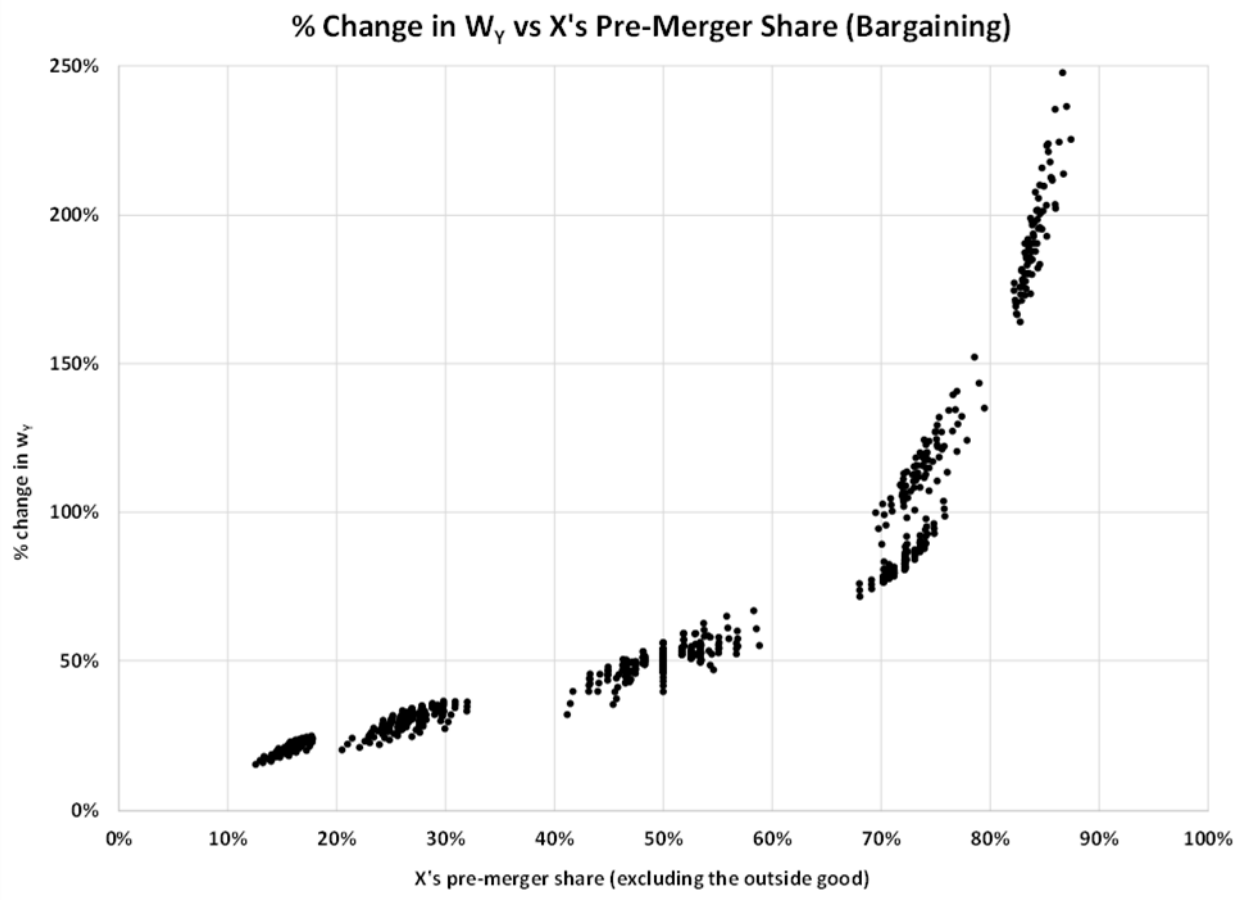

% Change in W_Y vs X's Pre-Merger Share (Bargaining)
250%
200%
150%
100%
50%
0%
% change in w_Y
0%
10%
20%
30%
40%
50%
60%
70%
80%
90%
100%
X's pre-merger share (excluding the outside good)

Figure D2

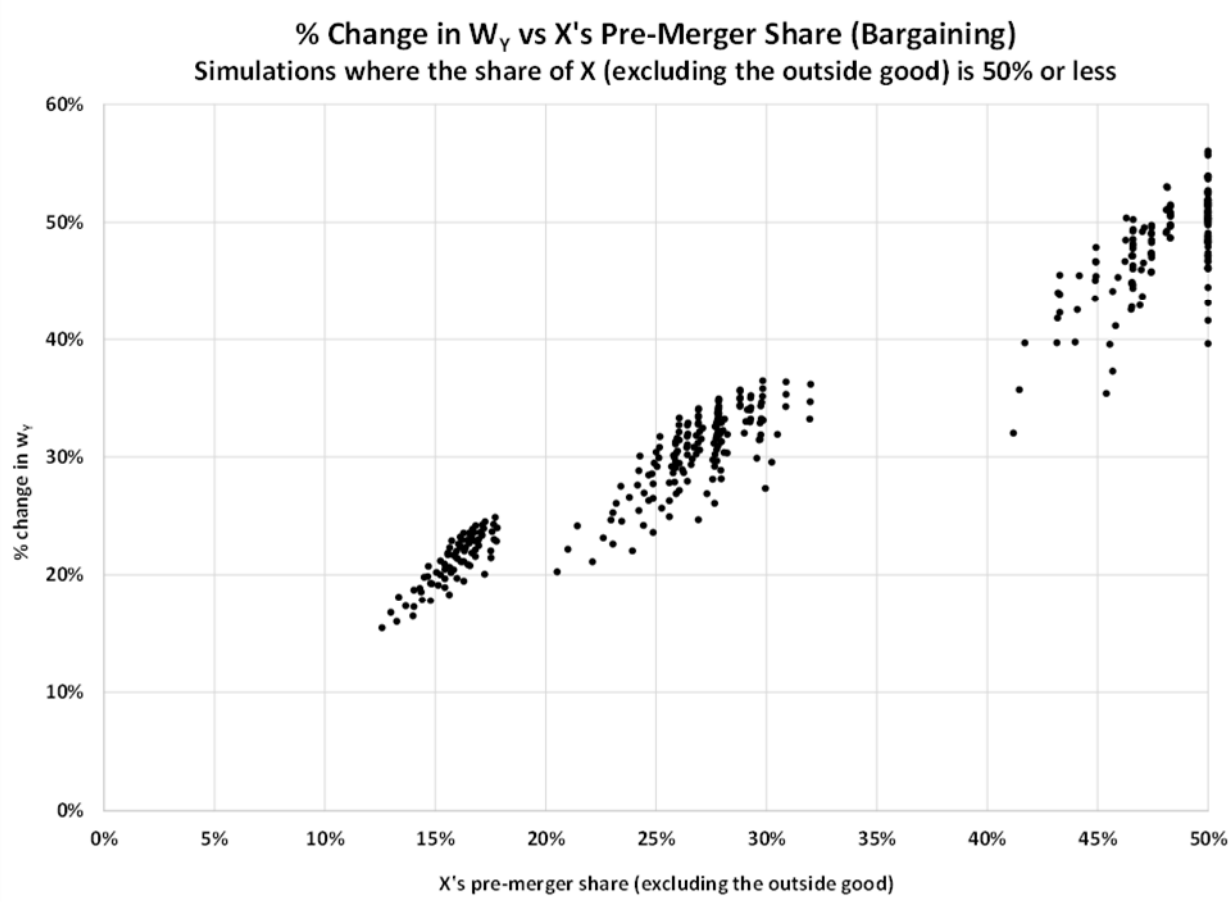

% Change in W_Y vs X's Pre-Merger Share (Bargaining)
Simulations where the share of X (excluding the outside good) is 50% or less
% change in w_Y
60%
50%
40%
30%
20%
10%
0%
0%
5%
10%
15%
20%
25%
30%
35%
40%
45%
50%
X's pre-merger share (excluding the outside good)

Figure D3

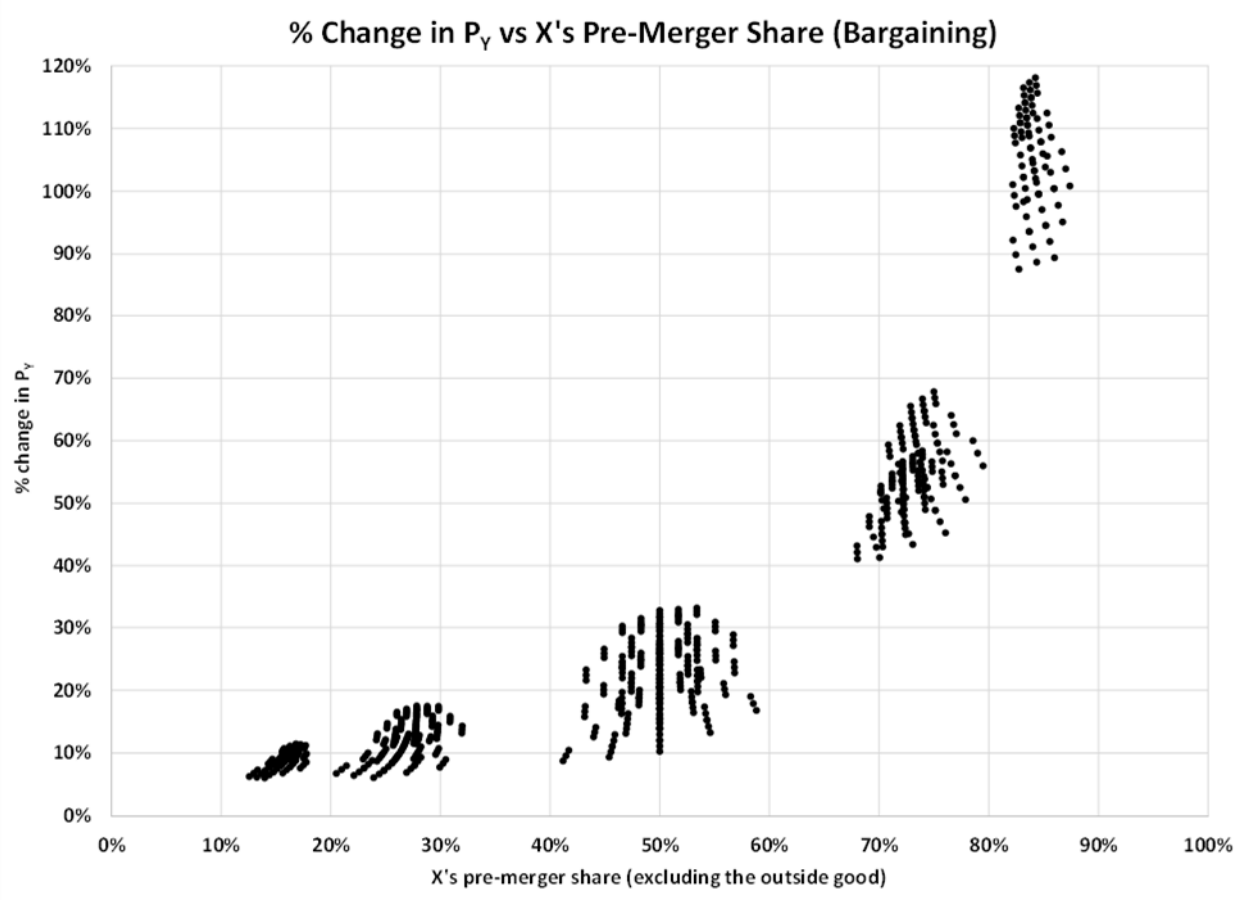
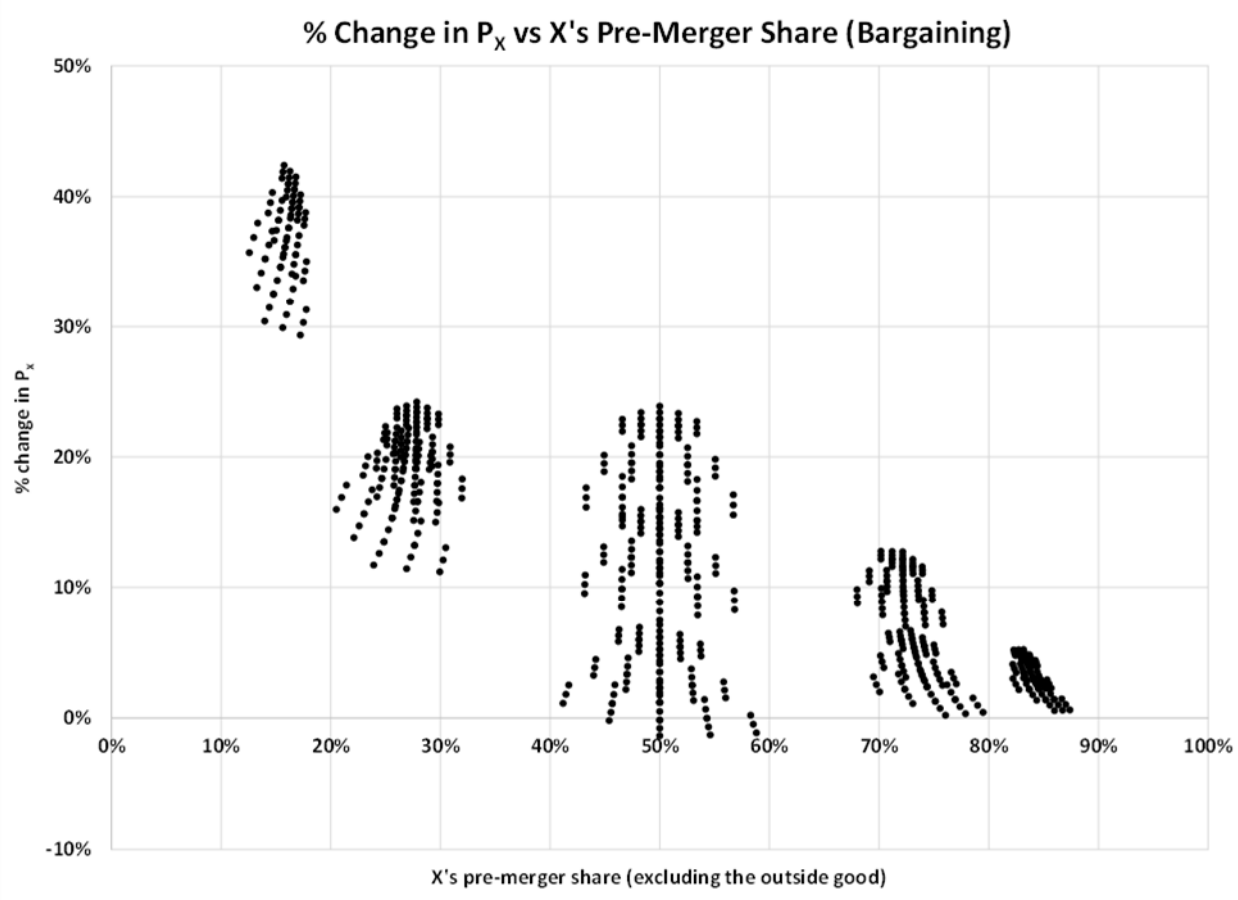

% Change in P_Y vs X's Pre-Merger Share (Bargaining)
% change in P_Y
120%
110%
100%
90%
80%
70%
60%
50%
40%
30%
20%
10%
0%
0%
10%
20%
30%
40%
50%
60%
70%
80%
90%
100%
X's pre-merger share (excluding the outside good)

Figure D4


% Change in P_X vs X's Pre-Merger Share (Bargaining)
50%
40%
30%
20%
10%
0%
-10%
% change in P_x
0%
10%
20%
30%
40%
50%
60%
70%
80%
90%
100%
X's pre-merger share (excluding the outside good)

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BEFORE THE
SURFACE TRANSPORTATION BOARD

Finance Docket No. 36500

CANADIAN PACIFIC RAILWAY LIMITED; CANADIAN PACIFIC RAILWAY COMPANY; SOO LINE RAILROAD COMPANY; CENTRAL MAINE & QUEBEC RAILWAY US INC.; DAKOTA, MINNESOTA & EASTERN RAILROAD CORPORATION; AND DELAWARE & HUDSON RAILWAY COMPANY, INC.
—CONTROL—
KANSAS CITY SOUTHERN; THE KANSAS CITY SOUTHERN RAILWAY COMPANY; GATEWAY EASTERN RAILWAY COMPANY; AND THE TEXAS MEXICAN RAILWAY COMPANY

VERIFIED STATEMENT

OF

THOMAS C. HALEY

VERIFIED STATEMENT

OF

THOMAS C. HALEY

1. My name is Thomas C. Haley. I retired in 2019 as Vice President – Network Planning & Operation for Union Pacific Railroad Company (UP). I worked in the railroad industry for 36 years, from 1983 until 2019. More than 30 of those years were with UP.

2. I have extensive experience with railroad operations and finance. I began my railroad career as a college intern with CSX. After graduation, I became a full-time management employee and was assigned to field operations and locomotive management roles. I joined UP's Finance department while earning my Master's in Business Administration in finance and transportation from Indiana University in 1989. In 1993, I moved to UP's Operating department and advanced through several positions until being appointed Assistant Vice President – Network Planning in 2001, followed by my promotion to Vice President – Network Planning & Operation in 2014.

3. As Vice President – Network Planning & Operation, I led the team responsible for UP's service design function, which is charged with taking a holistic view of UP's network and creating transportation plans to deliver high-quality service for UP's customers efficiently and productively across its network. I also oversaw UP's resource planning function, which is charged with assuring UP has the resources in place—the tracks and yards, equipment, and workforce—to execute its service plans. In addition, I led UP's Joint Facilities team, which makes and manages agreements for tracks and other facilities shared with other railroads. My Network Planning team and I were also involved in arranging interline service with other railroads.

4. On behalf of UP, I served on the boards of the Terminal Railroad Association of St. Louis and the Port Terminal Railroad in Houston and oversaw the activities of others on my team who served on the boards of several other jointly owned railroads. I also led UP's Network Development team, which helped develop and coordinate public-private partnerships, including the CREATE project in Chicago, and also helped coordinate projects with commuter rail agencies, including the Capital Corridor and ACE services in northern California, Metra in Chicago, and Metrolink in Los Angeles.

5. Over my many years at UP, I have been involved in many strategic railroad industry issues involving mergers and interline service. I have first-hand knowledge of UP's entire network and substantial portions of the nationwide railroad network. I have traveled with Canadian Pacific Railway (CP) leaders over CP's route between Kansas City and Minnesota, and with Kansas City Southern Railway (KCS) executives on most of the KCS/ KCSM route between the Mexico City area and Laredo, Houston, and Shreveport. I am familiar with rail facilities in the Kansas City area, including the 42-mile joint facility between Polo and Airline Junction that CP uses to access Kansas City (which is shared with UP), the connection between CP and KCS, and CP's and KCS's shared Joint Agency yard.

6. As Vice President – Network Planning & Operation, I helped develop plans and negotiate the terms for KCS's investments in capacity on the UP-owned lines between Robstown and Victoria, Texas, and between Rosenberg and Beaumont, Texas, that are used by KCS to connect with its KCSM concession in Mexico via the Texas Mexican Railway (Tex Mex). My team and I were also involved in designing and improving the UP-KCSM interline service plan and reciprocal blocking arrangements for moving traffic over the Laredo gateway.

7. I have previously testified and filed written statements about rail operations and service before the Surface Transportation Board. I testified at the Board's March 2014 hearing in *Petition for Rulemaking to Adopt Competitive Switching Rules*, Ex Parte No. 711, and the Board's April 2014, hearing in *United States Rail Service Issues*, Ex. Parte No. 724. I also submitted written comments for UP in *Reciprocal Switching*, Ex Parte No. 711 (Sub-No. 1), *Simplified Standards for Rail Rate Cases*, Ex Parte No. 646, and *Major Issues in Rail Rate Cases*, Ex Parte No. 657.

I. Introduction And Summary

8. I am providing this statement at the request of UP in connection with the Surface Transportation Board's review of the proposed combination of CP and KCS (the Applicants).

9. I was asked to address whether Applicants' projected merger-related benefits from the proposed transaction are consistent with Applicants' Operating Plan and real-world network conditions and outcomes Applicants would face when operating a merged CPKC system.

10. Applicants have set themselves an extraordinarily high bar, projecting merger-related benefits of over $1 billion annually (in 2025 dollars) through a combination of revenue growth from traffic gains and operating cost savings.[1]

11. My review of the Operating Plan and related materials in the Application and accompanying workpapers led me to three main conclusions:

- ***First,*** Applicants' projected operating costs savings are small, amounting to just 3.1% of CP's and KCS's current combined operating costs, and most of the savings are not merger-related. Applicants project savings by "optimizing" the

[1] *See* APP Vol. 1 at 351, Vargas VS ¶ 41, Table 2.

two railroads' "base" operations at current traffic levels. Most of Applicants' projected savings reflect CP plans to improve current KCS and KCSM operations. These changes could be accomplished without merger.

- ***Second,*** Applicants' projected revenues from traffic growth are unrealistic, at least within the 3-year timeframe described in their Application, and especially considering the exceptionally low operating costs that they project. Applicants expect to achieve an operating ratio of 30% on the growth traffic, which is unrealistic on such large volumes of additional traffic.
- ***Third,*** Applicants' projected revenues from traffic diversions also appear unrealistic. Applicants' routes between Mexico/Texas markets and Chicago/Twin Cities/Upper Midwest markets are significantly longer and less efficient than UP and BNSF alternatives. I do not believe that Applicants could meet their traffic diversion goals by solely competing for business on the merits.

12. I discuss each of these points in more detail below.

II. Applicants' Projected Operating Cost Savings Are Very Small, And Almost All Could Be Achieved Without A Merger.

A. Applicants Do Not Project Substantial Operating Costs Savings.

13. Applicants say that "[c]ombining the CP and KCS rail networks into a single network unlocks tremendous opportunities for efficiency gains."[2] This is an overstatement. In their exercise of optimizing current operations, Applicants identify opportunities for efficiency gains and cost savings. Relative to the total operations of the two railroads, these opportunities

[2] APP Vol. 2 at 283, OP Plan ¶ 76.

are not large, and most of them involve KCS/KCSM operational improvements, which could be accomplished without merging with CP.

14. CP's and KCS's total operating expenses in 2019 were a combined $5.57 billion.[3] Applicants project merger-related operating savings of just $172.8 million annually.[4] In other words, even taking all Applicants' projected operating savings into account, their total projected savings amount to only 3.1% of their current combined operating expenses. Railroads regularly achieve similar levels of productivity improvement as part of their normal course of business without merging with other railroads.

15. Applicants' actual opportunities for merger-related efficiency gains and cost are very limited. The CP system and KCS system connect at just one location: Kansas City. Every post-merger CPKC route will be basically the same as every pre-merger CP-KCS route. This means that a CP/KCS merger does not create the same opportunities for efficiency gains and costs savings from new and improved train services for existing traffic as many earlier rail mergers. By contrast, UP's merger with Southern Pacific produced a dozen or more significantly shorter, more efficient routes by combining the two rail systems.

16. In Kansas City, CP and KCS already share a yard, referred to as the Joint Agency yard. Their only duplicative facilities are headquarters facilities. This means a CP/KCS combination does not create the same opportunities for efficiency gains and cost savings from improving terminal operations as many earlier rail mergers. By comparison, UP's merger with Southern Pacific allowed the merged railroad to create significant efficiency gains and cost

[3] *See* APP Vol. 1 at 132 (CP Historical 2019 Operating Expenses of $3.59 billion); *id.* at 134 (KCS Historical 2019 Operating Expenses of $1.98 billion).

[4] *See* APP Vol. 1 at 74, App. B (Summary of Benefits Exhibit).

savings by combining and coordinating their operations at the many locations where both railroads had terminal facilities before they merged.

17. Applicants' main opportunity to achieve merger-related operating savings comes from changes to operations that would improve their handling of cars that CP and KCS currently interchange in Kansas City. That opportunity is very limited, as I explain below.

B. Most of Applicants' Projected Operating Cost Savings Could Be Achieved Without A Merger.

18. A sound analysis of merger-related operating cost savings must count only those reductions in costs that could not be accomplished but for the merger. Operating cost savings attributable to a merger of CP and KCS are those involving changes in handling traffic that the two roads interchange with one another, plus operational consolidations at common points. In this case, the amount of traffic interchanged between the two railroads is relatively small, and there is a single common point: Kansas City.[5] In their optimized operating plan, CP and KCS identify changes to the handling of 75 cars per day of traffic interchanged between them at the common point, Kansas City. Applicants identify no operational consolidations at Kansas City because the Joint Agency yard is already a shared facility. The 75 cars per day are evidently handled today on a single pair of scheduled CP trains that operate north of Kansas City, trains 474 and 475, which also handle CP's interchange with the other railroads in Kansas City.[6]

[5] *See* APP Vol. 2 at 295, OP Plan ¶ 109 ("CP and KCS intersect only in Kansas City, where they already share yard facilities, and the two railroads have no overlapping or parallel routes. As a result, there will be no change in the principle routes operated by either railroad. There will be no abandonments or discontinued operations anywhere on the combined system as a result of the Transaction.").

[6] *See* APP Vol. 2 at 311–12, OP Plan ¶¶ 148–49. Applicants mention interchanging "bulk trains" with flexibility to change crews at Kansas City, or at KCS's IFG facility or on CP at Polo, which are 23.4 miles south or 42.1 miles north of Airline Jct. in Kansas City, respectively. *See* APP Vol. 2 at 311, OP Plan ¶ 147. There does not appear to be a post-merger change in bulk unit train operations. Applicants' discussion of changes in blocking in the optimized plan

Applicants identify operational changes that will eliminate the need to switch or handle the 75 cars per day of interchange traffic. Therefore, cost savings from changes in handling the 75 cars per day of traffic interchanged between the two railroads are merger-related. Cost savings from operational changes internal to KCS and KCSM to implement Precision Scheduled Railroading ("PSR") are not attributable to the proposed merger. CP and other railroads did not require mergers to implement PSR in their operations.

19. In their Application, Applicants address the changes to their operations in Kansas City that would result from their transaction. Applicants say traffic that CP and KCS interchange in Kansas City will no longer need to be processed in Kansas City.[7] This results in a decrease of 75 switch handlings per day in Kansas City.[8]

consistently identifies manifest, auto, and intermodal traffic as being affected, not bulk traffic. *See* APP Vol. 2 at 296–99, OP Plan ¶¶ 112–16; *see also* APP Vol. 2 at 423–24, OP Plan App. F (New Blocks Optimized Plan).

[7] *See* APP Vol. 2 at 300, OP Plan ¶ 120 ("Under the Optimized Plan: the separate KCS Shreveport to Kansas City and CP Kansas City to St. Paul blocks and trains would be combined, with new blocking at Shreveport that will eliminate the reprocessing of traffic that currently takes place in Kansas City. *The result is an average reduction in transit time of 26 hours*. Comparable changes would be made for southbound flows in this corridor, with St. Paul building blocks for Shreveport and beyond.") (Emphasis in original.); *see also* APP Vol. 2 at 298, OP Plan ¶ 114 ("The decrease in cars per day at Kanas City is a reflection of no longer terminating CP and KCS train symbols at Kansas City, and the impact of longer distance blocks supporting a through train service.").

[8] *See* APP Vol. 2 at 297, OP Plan ¶ 112, Table 3. Applicants also identify changes that would reduce switching at KCS's International Freight Gateway. The changes do not involve traffic KCS interchanges with CP, {
} *See* Haley workpaper "HC - Operating Plan Deposition Excerpts."

Material within single braces ("{ }") has been designated "Confidential" under the Protective Order in this proceeding. Material within double braces ("{{ }}") has been designated "Highly Confidential." Confidential and Highly Confidential materials have been redacted from the public version of this statement.

20. To put that number into perspective, 75 saved switch handlings is about 1/10th of 1% of the 56,545 car handlings currently conducted on the combined railroads each day.[9]

21. Applicants calculated the 75 switch handlings reduction by comparing operating statistics generated under two different operating plans: a "base" plan and an "optimized" plan. The "base" plan reflects the separate CP and the KCS blocking and train plans that were in effect in the first quarter of 2021.[10] The optimized plan reflects Applicants' view of how a combined CPKC would operate to optimize efficiency,[11] based on CP's application of precision scheduled railroading (PSR).[12] Applicants modeled how "base year" traffic would be handled under both plans to identify changes in various operating statistics, including car handlings, that would result from implementation of the optimized plan.[13]

22. If I were calculating merger-related cost savings, I would look at the car costs and switch costs saved in connection with the 75 cars per day that would no longer be switched in Kansas City, net of the costs of any additional handling upstream and downstream to enable the cars to "overhead" Kansas City. If all of the handling in Kansas City is counted as savings, with no additional upstream or downstream costs, the total savings comes to $457,710 per year. The math is simple. Applicants say that they will save 26 hours per car on transit time in Kansas

[9] In their Operating Plan, Applicants' identify the number of "intermediate handlings" under their base plan as 22.01 million annually. *See* APP Vol. 2 at 287, OP Plan ¶ 86, Table 2. Applicants' workpapers contain the daily amount. *See* Baranowski workpaper "HC - Base to Optimized Operating Plan Savings.xlsx," tab "Base to Optimized Metrics."

[10] *See* APP Vol. 2 at 283, OP Plan ¶ 75.

[11] *See* APP Vol. 2 at 283, OP Plan ¶ 76.

[12] APP. Vol. 2 at 285, OP Plan ¶ 77 ("In developing the Optimized Plan, CP drew on its unparalleled experience with PSR . . . .").

[13] *See* APP Vol. 2 at 284–85, OP Plan ¶ 80, Table 1. Applicants appear to use a mix of CP's 2019 traffic data and KCS's 2020 traffic data to generate their operating statistics. *See* APP Vol. 2 at 283, OP Plan ¶ 75 n.4.

City,[14] and that an average railcar costs $4,800 per year, or $0.55 per hour, to lease and maintain.[15] Applicants also say the cost of a car handling is $2.42 per car.[16] I believe the $2.42 per car switch cost is significantly understated, but Applicants furnished it.

23. It could well be argued that the $457,710 annual savings estimate associated with eliminating the switching on 75 cars per day at Kansas City actually *overstates* merger-related operating savings for CP/KCS because this could be accomplished by the two railroads today through an interline service agreement. This is common practice in the industry. Railroads build blocks for each other to eliminate switching at interchange gateways. Nothing prevents KCS from agreeing today to build a "St. Paul" block for CP in Shreveport, if CP agrees to build a "Shreveport" block for KCS in St. Paul. Applicants further imply that there will be locomotive dwell savings associated with eliminating the 75 car switches per day in Kansas City. If locomotives are sitting idle in Kansas City because of CP-KCS interchange traffic, then this time could similarly be eliminated by executing a run-through locomotive agreement. Railroads do it all the time. CP and KCS do it elsewhere on their railroads.[17]

24. When Applicants calculate merger-related operating cost savings, they point to $52.59 million in annual savings based on comparing certain "operating metrics" produced by

[14] *See* APP Vol. 2 at 300, OP Plan ¶ 120.

[15] *See* APP Vol. 2 at 329, OP Plan ¶ 204 ($4,800 ÷365 ÷ 8=$1.64).

[16] *See* APP Vol. 1 at 407, Baranowski VS ¶ 8, Table 2 (1.4921 SEMs x $1.6207 per SEM = $2.42).

[17] Even counting savings from improved locomotive utilization would add annual merger-related savings in the $345,000 to $515,000 range. In my experience, a locomotive in mixed freight road service operates 12,000 to 18,000 miles a month, or 400 to 600 miles per day. Applicants say the cost of a locomotive unit mile is $1.1702. *See* APP Vol. 1 at 410, Baranowski VS ¶ 11, Table 5. Achieving an extra day's utilization of two locomotives for one year would save approximately $345,000 to $515,000 (2 x (400 to 600) x $1.1702 x 365).

their optimized plan with "operating metrics" produced by their base plan.[18] What explains the massive difference between my calculation and Applicants' calculation? The simple answer is that Applicants' calculation reflects optimizations of KCS's (and KCSM's) base operating plan that are not related to the proposed transaction.

25. As Applicants themselves acknowledge, their optimized operating plan is really just an application of PSR to the KCS system.[19] Applying PSR might produce significant operational savings for KCS, but KCS could achieving those savings without merging with CP. PSR and its elements are now commonly applied in the railroad industry.

26. Applicants' focus on changing KCS operations is easy to see in their Operating Plan. It is especially clear in Table 3, which shows the locations of changes in anticipated yard workloads between the base and optimized plans.[20] Nearly all the locations with changes are on KCS, and the overwhelming majority of changes in workload involve KCSM yards in Mexico. In Table 3, the only exclusively CP location is Nahant at a scant 16.5 cars per day. This is less than 2% of the Table 3 changes (>10 cars per day), indicating that over 98% of the operational change is on the KCS/KCSM. If you remove Kansas City because it is a joint location, 92% of the changes are on the KCS and KCSM.[21]

[18] *See* APP Vol. 1 at 412, Baranowski VS ¶ 15, Table 9.

[19] *See* APP Vol. 2 at 283, OP Plan ¶ 77.

[20] *See* APP Vol. 2 at 297, OP Plan ¶ 112, Table 3.

[21] If you look the Applicants' more detailed workpapers, the percentage changes are essentially the same. *See* OP Plan workpaper "HC - Cars Per Day by Yard.docx."

27. Another way to see the same point is to look at Applicants' proposed changes to train plans by comparing the base to the optimized plans. All of the train plan changes involve KCS and KCSM trains, with the exception of one train that would run through Kansas City.[22]

28. Applicants calculate their $52.59 million in "operating metric" savings based mainly on their changes in train plans. They say they could save 4,558 train miles per day by implementing their optimized plan, and they calculate cost savings that would follow from the reduction in train miles.[23]

29. As I said above, the best way to look at merger-related savings is to focus on changes in how cars are handled, not how trains are named. Train plans are designed to move cars. There are many different ways you can design a train plan to get cars from their origins to their destinations. What really matters is changes in how the cars are handled. In a CP/KCS transaction, the only merger-related changes involve cars that no longer require switching in Kansas City because that is the only traffic whose handling changes directly because of the merger. Changes in the train plan can be enacted now, independent of merger.

30. However, Applicants calculate cost savings using costs relating to train miles, so I want to briefly address how those costs might be used more appropriately in this case. I would focus on the trains carrying the 75 cars per day that would no longer require handling at Kansas City. In the optimized plan, those cars would be on the KCS 260/261 train pair, which would

[22] *See* APP Vol. 2 at 406–21, OP Plan App. C–E.

[23] *See* Baranowski workpaper "HC - Base to Optimized Operating Plan Savings.xlsx," tab "Base to Optimized Metrics." Applicants also use reductions in locomotive unit miles (LUMs), but their calculation of the reduction in LUMs flows from their calculation of the reduction in train miles. *See* Baranowski workpaper "HC - CP Operating Plan Output Cost Metrics Model.xlsx," tab "Model." Applicants also calculate savings from reductions in locomotive gross ton miles, again, they calculate reductions in gross ton miles based on reductions in train miles. *See id.*

travel a total of 2,363 miles per day, according to Applicants.[24] Since the new train pair replaces the existing 474/475, which today handles CP's interchange traffic for all railroads in Kansas City,[25] the train pair clearly handles more than a total of 75 cars in both directions. The 75 cars would be approximately one-third of the total capacity of both trains 260 and 261.[26] The costs associated with one-third of 2,363 train miles, or 788 train miles,[27] calculated using the same methodology as Applicants, plus the costs savings associated with a reduction in 75 car handlings per day, the result is $9.05 million, not $52.59 million.[28]

31. Again, I am not saying that KCS could not reduce train miles and generate cost savings. CP's optimized plan seems to reflect solid ideas for improving KCS and KCSM train plans. However, KCS could implement an optimization plan and generate savings without a merger. Most large railroads have implemented some version of PSR without merging with other railroads.

32. Applicants also calculate certain merger-related operating savings in addition to savings based on "operating metrics." However, those calculations generally suffer from the same flaw—they reflect savings that could be achieved without a merger.

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[24] *See* APP Vol. 2 at 419, OP Plan App. E.

[25] *See* APP Vol. 2 at 311–12, OP Plan ¶¶ 148–49.

[26] Applicants say their optimal train size north of Kansas City will be 10,000 feet. *See* APP Vol. 2 at 338, OP Plan ¶ 234. A pair of daily trains (260 and 261) at 10,000 feet have a theoretical capacity of 275 to 300 cars at a typical 65 to 70 average feet per car. The 75 cars per day in question would therefore amount to 25 to 27% of train capacity. Since the real world falls short of optimal, regarding the 75 cars as roughly one-third of train capacity seems more realistic. The 75 cars would be approximately one-third of train capacity if actual train sizes were in the range of 7,500 to 8,000 feet, at 65 to 70 feet per car. Note that my conservatism here *increases* the merger-related savings estimate.

[27] It does not matter whether the cars get on or off the train between Shreveport and St. Paul. I conservatively assume they stay on the train the whole way.

[28] *See* Haley workpaper "Train Mile Savings Calculations.xlsx," tab "Summary Tables."

33. For example, Applicants calculate fuel savings of $26.57 million in the first year post merger. They say those savings reflect their assumption "that the fuel consumption for the combined CP/KCS system will mirror the improvement projected internally at CP based on a regression of horsepower per ton and gross ton-miles."[29] Changes to improve fuel efficiency of the KCS/KCSM are not merger dependent. Fuel conservation practices are widely known and practiced across the railroad industry. If better fuel consumption practices exist, KCS does not need to merge with CP to adopt them.

34. Applicants also identify savings in locomotive depreciation and lease costs. But as Applicants acknowledge, their calculations are driven entirely by the reduction in LUMs from their optimization of KCS's train plans,[30] so only a small fraction could possibly be counted as merger-related.

35. Applicants also describe projected operating savings from freight cars and procurement, but those do not change the overall picture. Applicants do not project any freight car savings from applying the optimized plan.[31] Finally, they say they might achieve $4.18 million in procurement savings from increased bargaining leverage.[32] These savings hardly amount to "tremendous opportunities for efficiency gains."

36. In sum, Applicants' claimed merger-related savings are very low to begin with, and to the extent they reflect viable strategies for improving KCS's operations, most could be achieved without a merger.

[29] APP Vol. 1 at 408, Baranowski VS ¶ 9.

[30] APP Vol. 1 at 409, Baranowski VS ¶ 11

[31] APP Vol. 1 at 411, Baranowski VS ¶ 13, Table 7.

[32] APP Vol. 1 at 412, Baranowski VS ¶ 14, Table 8.

III. Applicants' Projected Revenues From Traffic Growth Appear Unrealistic.

37. Applicants' projected cost savings from operational synergies plainly are not large enough to provide their projected $1 billion plus annually in merger benefits. To get there, Applicants also rely on projections of massive traffic growth and a huge leveraging of productivity. From my operating perspective, their growth plan is unrealistic.

38. To be clear, I am not second-guessing Applicants' business evaluation of the various targets of traffic growth that are addressed in their "growth" operating plan. Rather, I am providing my perspective on whether Applicants could realistically achieve the projected traffic growth, within the projected timeframe, at the projected operating costs levels.

39. Applicants' projection of merger benefits relies on capturing traffic that is currently moving on highways, through other ports, or on other railroads. Applicants project total growth in traffic by {{ }} cars and intermodal containers by 2025.[33] Of that total, {{ }} has some existing connection to CP or KCS—that is, CP or KCS handles part of an existing movement and expects to extend its haul.[34] The remainder is traffic that Applicants say they will attract to the Port of Lazaro Cardenas, divert from truck to rail, attract by creating new routes and new services, or attract from other railroads.[35]

40. Applicants' growth operating plan shows the massive increase in the amount of traffic to be accommodated on their North-South corridor between Mexico and the Midwest in

[33] OP Plan workpaper "1.Proposed Final FTI Rail to Rail Diversion Results for Merger Application_matching Finance with Truck to Rail.xlsx," tab "All Volumes;" *see also* APP Vol. 1 at 427, Baranowski VS ¶ 55, Table 16 (509,490 "Diverted Carloads/Units" by 2025).

[34] *See* OP Plan workpaper "HC - 1.Proposed Final FTI Rail to Rail Diversion Results for Merger Application_matching Finance with Truck to Rail.xlsx," tab "All Volumes" {{ }}

[35] *See generally* APP Vol. 1 at 243–302, Wahba/Naatz VS.

just 3 years. Applicants' growth operating plan shows massive growth south of Kansas City on top of an already solid base. Trains per day increase from 11 to 25 between Kansas City and Shreveport, and from 9 to 20 between Shreveport and Houston.[36] Those are 127% and 122% increases, respectively—more than *doubling* the train traffic on these already busy routes.

41. I do not believe there is any precedent for so much growth across such a long corridor in such a short period of time for an end-to-end merger.

42. I noticed in Applicants' capacity investment plans that capacity is provided only for the trackage owned by CP and KCS/M.[37] Applicants are silent on the capacity needs on the significant trackage rights territory on Union Pacific from Beaumont, Texas, through Houston to just south of Rosenberg, Texas, and from Victoria, Texas, to Robstown, Texas, near Corpus Christi. Applicants' growth plan seeks to approximately double KCS volumes on these segments in three years, to 19-20 trains per day on a base of 9-11 trains per day.[38] Of the {{ }} carloads and containers of existing and new rail business they plan to capture, approximately {{ }} or roughly {{ }} would move over these segments.[39] The most significant capacity challenges in the entire CP/KCS merger are likely to be faced in this territory, including a major bridge at Beaumont and the Houston terminal area, one of the most complex and sensitive rail facilities in North America. Even if the capacity needs of the trackage rights territory are tackled immediately, difficult projects, such as the Neches River bridge and facilities to accommodate the growth in the constrained urban Houston area, are unlikely to be

[36] *Compare* APP Vol. 2 at 452, OP Plan App. N, *with id* at 454, OP Plan App. O.

[37] *See* APP Vol. 2 at 337–44; Op. Plan ¶¶ 231–44.

[38] *Compare* APP Vol. 2 at 452, OP Plan App. N, *with id* at 454, OP Plan App. O.

[39] *See* Operating Plan workpaper "HC - 1.Proposed Final FTI Rail to Rail Diversions for Merger Application matching Finance with Truck to Rail.xlsx." {{
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designed, permitted, and completed in three years. This is a major hole in Applicants' Operating Plan, one completely ignored.

43. Moreover, to be successful, Applicants must not only attract all of their projected growth traffic and accommodate it, they must also handle the traffic at an exceptionally low incremental cost. Their calculations imply a 30% operating ratio on all the growth.[40]

44. Applicants plainly recognize the issue and propose a very aggressive plan for handling the traffic. Their growth plan says CPKC will grow carloads by {{ }} in Year 3, resulting in an increase of 21.3% in total car-miles and an increase of approximately 20% in gross ton-miles on the *entire* CP/KCS combined network, compared to both the optimized plan and to today's levels.[41] Yet total train miles will increase by only 11.6% compared to their *optimized* plan, and by only 7.4% compared to today's operation.[42] Also, by assuming significant improvements in train size and velocity, Applicants say they will increase train hours by only 1.1% compared to their *optimized* plan, and actually *reduce* train-hours by 3.7% compared to today's operation.[43] This would represent an astounding increase in productivity.

45. Applicants' exceptionally aggressive operating plans extend to their plans for car handlings. Applicants' growth plan reflects an increase in intermediate handlings of only 3.5% compared to their *optimized* plan.[44] That is, Applicants plan to handle approximately 20% more traffic with only 3.5% more car handlings as compared with their *optimized* operation at today's traffic levels.

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[40] *See* APP Vol. 1 at 427, Baranowski VS ¶ 55, Table 16 ($306.3 M in total incremental costs, and $1.02 B in incremental revenues).

[41] APP Vol. 2 at 287, OP Plan ¶ 86, Table 2.

[42] *Id.*

[43] *Id.*

[44] *Id.*

46. Applicants' growth operating plan appears even more aggressive when one considers the reduction in car handlings already reflected in their optimized plan. Applicants reduced total car handlings by 1.8% from their base plan to their optimized plan—mostly by assuming KCS and KCSM implement PSR. Then, in their growth plan, they show the traffic moving over their North-South corridor will double or triple, driving up gross ton-miles and car miles on the CPKC network by 20% and 21.3%, respectively. Yet, they say car handlings on the combined network will increase over the base plan level by just 1.6%. Stated differently, Applicants project accommodating network-wide growth of approximately 20% with 1.6% more car handlings than CP and KCS perform network-wide today. This would be an extraordinary result. Applicants have very lofty aims.

47. I recognize that large volume growth, if actually achieved, can create significant leverage in railroad operations. But I have never seen growth occur to the degree, or leverage obtained to the extent, that Applicants are projecting.

48. Applicants' aggressive assumptions are further illustrated in their calculations of the incremental costs of handling their projected traffic growth. Applicants project they will generate incremental revenues of $1.02 billion at an incremental cost of $306.3 million in 2025.[45] These numbers imply that the operating ratio for the massive body of traffic that Applicants plan to attract to CPKC would be in the ballpark of 30%.[46]

49. Rail traffic with a 30% operating ratio exists in some circumstances. However, where a railroad is growing traffic to this extent on top of a sizeable existing base, operating ratios would be much closer to average. Best in class operating ratios are in the 55-60% range.

[45] APP Vol. 1 at 427, Baranowski VS ¶ 55, Table 16.

[46] Operating ratio is simply operating expenses divided by revenue.

Even CP, which touts its expertise in PSR, had an operating ratio of 60.2 in the third quarter of 2021.[47] Applicants are simply not being realistic when they assume they can divert large amounts of traffic from other railroads and modes at an operating ratio that is roughly half CP's average.

IV. Applicants' Projected Revenues From Traffic Diversions Appear Unrealistic.

50. If the Board approves the proposed transaction, CPKC will face intense pressure to deliver on their aggressive revenue and growth projections. I know this from my own experiences with railroad mergers.

51. Applicants' revenue projections rely to a large extent on speculation that they will be successful in attracting new traffic to CPKC, as noted above. Their most readily available source of additional revenue to meet promises to investors is what they call "extended hauls"—for example, taking traffic that KCSM currently interchanges with UP at Laredo for movement to Chicago, and diverting the business to a single-line haul on KCS to Kansas City, then CP to Chicago.

52. Applicants' project they will divert substantial quantities of traffic by offering "single-line service," but they offer no concrete reason why customers would willingly choose CPKC routes over existing interline routes.

53. CP-KCS have a fundamental routing disadvantage—that is, their routes are longer, slower, and otherwise less efficient than available alternatives. Applicants implicitly recognize their fundamental routing disadvantage when they show that, for traffic they

[47] *See* Haley workpaper "P - CP Third Quarter Earnings Release.pdf."

considered to be divertible, CPKC routes would be, *on average*, 217 miles longer than the existing movement, or approximately 12% longer.[48]

54. Moreover, Applicants do not propose to offer rate reductions to attract all this traffic.[49] They cannot afford to make such promises: their ambitious revenue projections assume they successfully divert traffic to create extended hauls *at existing rates*.[50]

55. CPKC's routing disadvantage is even greater for vast amounts of traffic they say they will actually divert. A prime example is the one I mentioned above: UP traffic currently moving between Chicago and Laredo, which is interchanged with KCSM.

56. The Chicago-Laredo lane is of particular significance in this case. Of Applicants' projected diversions of 137,416 intermodal containers, about 60% involve movements between Mexico and Chicago, or Mexico and Detroit (which would move via Chicago).[51] Of Applicants' projected diversions of 33,218 automotive carloads, about 60% involve movements between Mexico and Chicago (including traffic to Chicago interchanges with CSX and NS).[52]

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[48] *See* APP Vol. 2 at 132, Brown/Zebrowski VS ¶ 30, Table 6.

[49] Applicants assume that "CP/KCS would be required to offer rate reductions averaging five percent in order to attract traffic away from existing single-line service." *See* APP Vol. 2 at 133, Brown/Zebrowski VS ¶ 32. Traffic that UP interchanges with KCSM is not "existing single-line service." *See id.* at 149, Brown/Zebrowski VS ¶ 64 (asserting that "CP/KCS would offer the only single-line service in the market" for automotive carloads moving from Mexico into the United States).

[50] *See* APP Vol. 2 at 163–66, Brown/Zebrowski VS ¶¶ 90–96 & Table 28. The $513.1 million in incremental revenue from diversions reflected in Brown/Zebrowski Table 28 was incorporated into the calculation of $1.02 billion in incremental revenues that appears in Table 16 of Mr. Baranowski's Verified Statement. *See* APP Vol. 1 at 415, Baranowski VS ¶ 23; *see also id.* at 427, Baranowski VS ¶ 55, Table 16. The $1.02 billion figure is the same one that appears in Applicants' Summary of Benefits exhibit. *See* APP Vol. 1 at 74, App. B.

[51] *See* APP Vol. 2 at 144, Brown/Zebrowksi VS ¶ 55, Table 15.

[52] *See* APP Vol. 2 at 149, Brown/Zebrowski VS ¶ 63, Table 18.

57. According to Applicants' own calculations, CPKC's route between Laredo and Chicago would be {{ }} while the average of existing movements handled by other carriers is {{ }}.[53] The {{ }}

58. When I was at UP, we used a variety of metrics to compare alternative routes. Those metrics include not only mileage, but also more detailed calculations to assess the relative efficiency and potential performance of routes, including rise and fall (total grade change) curvature, fuel consumption, and simulated transit time.[54] I asked UP to provide me those metrics to permit a more detailed comparison of alternative routes between Laredo and Chicago.

59. The more detailed data confirm what a simple mileage comparison indicates: a CPKC route from Chicago to Laredo would be substantially less efficient and slower than UP's existing route, and slower than BNSF's route using an interchange with KCS at Robstown. I summarize the results in the table below:

Chicago-Laredo Route Comparison[55]

Railroad	Miles	Rise and Fall (ft)	Curvature (degrees)	Fuel (gal)	Simulated Transit Time (hr)
UP	**{{**				
BNSF					
CPKC					**}}**

60. Comparisons of routes to Texas markets, including Dallas and Houston, also favor UP and BNSF routings as compared to CPKC routings.

[53] *See* Brown/Zebrowski workpaper "HC - Rail to Rail Diversions Summary.xls," tab "Table 6," row 34.

[54] Simulated transit time is also known as unimpeded run time—it measures a run time based on the maximum speed limits of the route with no traffic interference. It is a useful measure to compare the relative performance potential of alternative routes.

[55] *See* Haley workpapers "HC – BNSF TPS Chicago-Laredo.xlsx"; "HC – CPKC TPS Chicago-Laredo.xlsx"; "HC – UP TPS Chicago-Laredo.xlsx."

61. A CP/KCS transaction cannot change the underlying route structure. The two railroads connect only in Kansas City. The post-merger CPKC route from Laredo to Chicago will be the same as pre-merger CP-KCS route.

62. This means every car that Applicants manage to divert to their route will move over a longer, slower, less efficient route, with increased fuel consumption. Stated differently, if CPKC succeed in diverting traffic from other railroads, they will reduce overall rail network efficiency and consume more fuel on the traffic diverted from other railroads, generating *negative* environmental impacts on that traffic.

63. CPKC will face a similar situation when moving traffic to Texas and Gulf Coast markets. Applicants' own data show significant circuity in Chicago-Dallas lanes and for traffic moving from a variety of Canadian origins to Texas destinations, to pick just a few examples.[56]

64. How will Applicants respond to the pressure to divert traffic to meet their revenue projections? They have boxed themselves in regarding rate reductions. Their Application does not suggest they can somehow overcome their routing disadvantage and beat the transit times of their competitors to and from the Laredo Gateway. CPKC, UP, and BNSF must rely on KCSM service within Mexico. I believe it is unlikely that Applicants could meet their traffic diversion goals by competing for business on the merits.

V. Conclusion

65. Based on my review of the Application, including the accompanying verified statements and work papers, I do not believe that Applicants can achieve the projections they have set out. I am not saying that the Board should not allow them to try, but the Board should

[56] *See* Brown/Zebrowski workpaper "HC -Rail to Rail Diversions Summary.xls," tab "Table 6."

ensure that when Applicants seek to divert traffic or compete for new business, they compete on the merits.

66. I believe it is especially critical to protect against outcomes of a CP/KCS merger that might impair current competitive options for rail traffic. The Board should not direct how rail traffic moves, but it should ensure that customers can select options that provide them with their desired combination of service and price. The best way to ensure efficiency and excellent service is to ensure that traffic is free to flow to the carriers and routes that provide the best service and value to rail customers.

VERIFICATION

I, Thomas C. Haley, 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 February 25, 2022.

/s/ Thomas C. Haley

BEFORE THE
SURFACE TRANSPORTATION BOARD

Finance Docket No. 36500

CANADIAN PACIFIC RAILWAY LIMITED; CANADIAN PACIFIC RAILWAY COMPANY; SOO LINE RAILROAD COMPANY; CENTRAL MAINE & QUEBEC RAILWAY US INC.; DAKOTA, MINNESOTA & EASTERN RAILROAD CORPORATION; AND DELAWARE & HUDSON RAILWAY COMPANY, INC.
—CONTROL—
KANSAS CITY SOUTHERN; THE KANSAS CITY SOUTHERN RAILWAY COMPANY; GATEWAY EASTERN RAILWAY COMPANY; AND THE TEXAS MEXICAN RAILWAY COMPANY

VERIFIED STATEMENT

OF

LUIS F. DE LA CALLE

VERIFIED STATEMENT

OF

LUIS F. DE LA CALLE

My name is Luis F. de la Calle. I am the founding partner at De la Calle, Madrazo, Mancera, S.C. (CMM), and have served as its managing director since its creation in 2004. CMM specializes in economics, regulatory processes, and international trade. I am trained as an economist and hold a doctorate in Economics from the University of Virginia. Prior to joining the private sector, I served as Undersecretary for International Trade Negotiations in Mexico's Ministry of the Economy. Before that, I served as Trade and NAFTA Minister at the Mexican Embassy in Washington, D.C., participating in the crafting and implementation of the North American Free Trade Agreement ("NAFTA").

At CMM, I have regularly advised clients on competition issues in Mexico and participated as an expert witness in economics before the Federal Economic Competition Commission (Comisión Federal de Competencia Económica) ("COFECE"), the Mexican antitrust body. In 2011, in preparation for the drafting of a new antitrust law, which broadened COFECE's authority, I was retained by the Economy Commission of the Lower House of the Mexican Congress to prepare and present a comparative analysis of competition laws, including those of Mexico, Chile, South Korea, the US, Australia, Canada and the EU. In 2014, I testified before the House on reforms in connection with establishment of COFECE and on the special procedures on barriers, essential facilities, and effective competition included in the new antitrust law.

My positions and experience in both the public and private sectors have given me broad knowledge of U.S.-Mexico cross-border traffic and the Mexican laws and regulations

governing rail competition, as well as familiarity with the agencies and procedures involved in implementing these laws and regulations.

In this statement, requested by Union Pacific Corporation ("UP"), I discuss how Mexican laws and regulations governing railroads and competition and implementation of these laws and regulations by Mexican agencies ought to be considered in evaluating competitive aspects of the merger between Canadian Pacific Railway Limited ("CP") and Kansas City Southern ("KCS") (the "CP-KCS Merger"). In Section I, I explain why Mexican laws and regulations and any enforcement activity by Mexican authorities cannot be relied on to prevent potential anticompetitive effects of the CP-KCS Merger on cross-border rail traffic. I explain that Mexican laws and regulations do not clearly prevent a merged CP/KCS from setting rates in a manner that would reduce competition for cross-border rail traffic. I also explain that the Mexican antitrust and railroad agencies will be unable to timely and effectively design and enforce remedial measures to reverse potential anticompetitive practices resulting from the CP-KCS Merger. In Section II, I explain that COFECE has approved the CP-KCS Merger with no conditions, but with no indication that the agency considered potential effects of the merger on competition for US-Mexico cross-border traffic. Finally in Section III, I stress that measures UP will ask the Surface Transportation Board ("STB") to impose requiring that CP/KCS not discriminate against competitive connections and that it offer competitive rates for connecting cross-border traffic would be consistent with Mexican law and would not be regarded as interfering with the prerogatives of Mexican agencies.

I. MEXICAN LAWS AND REGULATIONS CANNOT BE RELIED ON TO PREVENT ANTICOMPETITIVE EFFECTS OF THE CP-KCS MERGER ON CROSS-BORDER TRAFFIC.

U.S.-Mexico cross-border rail traffic has increased significantly in recent years, and this is a key reason for CP's interest in acquiring KCS. Indeed, the high valuation of the CP-KCS Merger is testimony to the potentially significant value of a North-South rail backbone linking Canada, the Central U.S. and Mexico. The Laredo crossing is a particularly valuable part of this backbone. The cross-border exchange at Laredo is by far the fastest route connecting Mexico to the U.S. and Canada, with a wide range of connecting options in the U.S. Kansas City Southern Mexico, S.A. de C.V. ("KCSM"), a KCS subsidiary, owns the only route that extends south from Laredo. To date, KCSM has had incentives to work not just with KCS, but also with UP and BNSF Railway to move traffic North-South from the Mexico-U.S. border, including at the key Laredo crossing. Shippers have benefited from having strong competitive alternatives involving both single-line service and service by competitive interconnections.

The CP-KCS Merger could give the merged company substantial market power in the Canada-U.S.-Mexico corridor. UP is understandably concerned that the combined CP/KCS will have strong incentives to discriminate against connections with (and within) the United States. Among other things, UP argues that the combined railroad could raise KCSM rate factors for Laredo traffic while reducing CP/KCS rates north of the border, effectively raising rates for shippers using UP service north of Laredo, making those routes less competitive than CP/KCS/KCSM routes, or otherwise engage in anticompetitive strategies.

Mexican law and regulations would not clearly prevent the potential anticompetitive conduct that UP has identified, creating uncertainty about how Mexican agencies and courts

would treat any disputes about such discriminatory conduct. Moreover, it is clear that, in light of this uncertainty, the numerous procedural hurdles a complainant would face, and experience to date with the relevant Mexican agencies, it would take many years before a final decision is issued on a complaint by shippers or other carriers about CP/KCS/KCSM rate discrimination against connecting carriers handling cross-border traffic.

A. Mexican Law and Regulations Would Not Clearly Prevent CP/KCS from Setting Rates in a Manner That Would Discriminate Against Cross-Border Connections.

Mexican law and practice do not clearly prevent the type of discriminatory rate practices that UP expects CP/KCS could adopt after they consummate their merger. Following the privatization of the Mexican railway sector in the late 1990s, Mexican rail service has been subject to the Railway Service Law (Ley Reglamentaria del Servicio Ferroviario) (the "RSL") and the Regulations of the Railway Service (Reglamento del Servicio Ferroviario) (the "Regulations").[1] Jurisdiction over rail rates is split between two agencies, COFECE, the Mexican antitrust agency, and the Railway Transport Regulatory Agency (Agencia Reguladora del Transporte Ferroviario) (the "ARTF"), with overlapping responsibilities. COFECE's authorities, including those for merger control and conduct of investigations, are defined by the Federal Economic Competition Law (Ley Federal de Competencia Económica) (the "FECL"). ARTF, created in 2015 as part of an amendment to the RSL, is a unit within SICT. ARTF took over responsibility for rail tariff regulation (as well as interconnection of railways and enforcement of the RSL).

[1] The Regulations were issued by the Secretary of Infrastructure, Communications and Transport ("SICT") (previously named Secretary of Communications and Transport) in 1996 pursuant to the RSL.

Under the RSL and the Regulations, carriers may freely set their rates as per Articles 46 of the RSL and 170 of the Regulations. Carriers must file their maximum rates with the ARTF for each of their routes; once a maximum rate is registered, the carrier cannot charge more than that rate for the traffic on that route. However, a carrier may return to the agency and file a higher rate whenever it wishes.

Although concession holders (like KCSM) are free to set their rates, the RSL and Regulations contain a procedure through which certain parties may challenge a carrier's registered rates. However, to make such a challenge a party must first obtain a ruling from COFECE that effective competition does not exist in the relevant market.[2] See Article 47 of the RSL. To my knowledge, this procedure for challenging a rate has seldom been used. So far as I am aware, neither the ARTF nor COFECE has ever investigated a case involving allegations of discrimination in freight rail rates.

Mexican authorities likely would not take any action against an overall CP/KCS/KCSM rate for traffic moving between Mexico and the U.S. if the KCSM portion of the rate was offered in a non-discriminatory manner to all shippers under equal conditions. Mexican railroad law does contain a requirement that carriers set rates in a non-discriminatory manner. Under Article 170 of the Regulations, a carrier's maximum rates "shall be applied in a non-discriminatory manner and shall be the same for users in equal conditions." Carriers may charge less than their maximum rates if they grant these discounts

[2] And for such ruling, the procedure set forth in Article 96 of the FECL governing investigation and determination of market conductions (including matters concerning effective competition) needs to be followed, and such ruling can be challenged through an *amparo* claim. An *amparo* proceeding is one in which the plaintiff alleges that a governmental act is unconstitutional, in which the act can be challenged on the grounds that the act was contrary to the applicable law, equivalent to a cassation appeal.

to "users in a non-discriminatory manner and in equal circumstances", and "shall consider the specific characteristics of each service, according to the classifications established pursuant to the Regulations." But there is no reason to believe that this requirement of non-discrimination would apply to more than the KCSM portion of an overall rate.

The KCSM's Concession includes several provisions requiring non-discriminatory conduct. Section 2.1 of the Concession states that KCSM must provide rail services "under equitable and non-discriminatory conditions with respect to opportunity, quality and price." Section 2.2 of the Concession requires that KCSM provide interconnection services "with connecting railroads of other countries under fair and non-discriminatory conditions in regard to timeliness, quality and price" and that "[a]ny difference … in the rates applied must be based on specific circumstances that justify such distinctions being made." But these provisions do not appear to address an increase in KCSM rates that was the same for both connections at Laredo (UP and CP/KCS), as part of a strategy by CP/KCS to divert cross-border traffic from KCSM-UP routes to CP/KCS/KCSM routes.

In the period since the rail industry was privatized, there have been no developments suggesting that Mexican regulators would apply Mexican laws and regulations to a carrier's discriminatory use of rates to disadvantage connecting carriers at the U.S.-Mexico border. Since 2014, when COFECE gained broader authority, it has opened only two investigations into the railway sector, neither of which involved cross-border traffic or allegations of discriminatory rates. COFECE closed a 2016 investigation, which involved trackage rights markets[3], due to methodological errors by its Investigative Authority, resulting in

[3] Five relevant markets were defined, each one defined as the interconnection services in trackage rights modality (relevant service), in each of the railway network of five different concessionaries and/or economic interest groups (each a geographic market).

insufficient evidence to establish the lack of effective competition in the markets at issue. To my knowledge, the closing of the procedure was not challenged by any economic agent. In a 2020 COFECE declaration (issued in the procedure opened in 2018), which involved the rail freight transportation of four chemical products, each in routes with origin/destination in the south of the State of Veracruz[4], COFECE issued, in 2020, a declaration of lack of effective competition in certain Mexican markets[5]. The decision regarding the 2018 case has been challenged through multiple appeals (*amparo* claims filed in Federal District Courts), which have been pending for two years and could result in annulment of the COFECE decision. Since the COFECE decision did not relate to cross-border traffic or rate discrimination, the decisions on the appeals will not shed any light on UP's concern about potential discriminatory rate setting by CP/KCS/KCSM.

In 2021, COFECE published a report on competition in freight rail service. While the report raised concerns about several aspects of competition in the freight rail sector, to my knowledge it has not yet led to the opening of any investigations to identify potential solutions to the alleged lack of competition. In any event, the report did not address conduct relating to cross-border traffic or rate practices for interconnections more generally. Thus, the report does not suggest that the Mexican laws and regulations would be read to address the concerns UP has raised about the potential for CP/KCS's use of discriminatory rates in connection with cross-border moves. As before, there is no assurance that Mexican

[4] Defining as a separate relevant market the rail freight transportation of a single product in a separate route. Thirty one markets were initially defined by the Investigative Authority.

[5] In twenty five out of the thirty one initially defined by the Investigative Authority.

regulators would apply Mexican laws and regulations, or the KCSM's Concession terms, to address any discriminatory rate practices CP/KCS may adopt following the merger.

Since its creation in 2015, ARTF's regulatory activity has been very limited. The agency has opened only three tariff regulation procedures[6] (each opened and decided in 2020), all based on COFECE's 2020 declaration (issued in the procedure opened in 2018), imposing tariff regulations in each of the twenty five relevant markets where COFECE determined the lack of effective competition (i.e., only for certain specific routes for the transportation of a particular chemical) and, to my knowledge, each of these decisions has been challenged through administrative annulment procedures and *amparo* claims. At this point, it does not appear that ARTF is becoming an effective regulator of the rail industry.

So far as I am aware, neither COFECE nor ARTF has ever investigated a case involving rate discrimination. Thus, it is unclear how either agency would respond to a complaint about the sort of discriminatory rate conduct UP anticipates as a result of the CP-KCS Merger.

B. There Is No Assurance That Shippers or Competing Carriers Could Obtain Enforcement of Mexican Law, Regulations or the KCSM Concession Terms to Remedy Anticompetitive Rate Practices by CP/KCS.

Even if it were clear that provisions of Mexican law, regulations, or the KCSM Concession could be applied to remedy the anticompetitive rate practices that CP/KCS might adopt following the merger, there is no question in my mind that efforts to enforce such provisions would be ineffective. Because COFECE did not impose conditions on the CP-KCS Merger to prevent use of rate practices that discriminate against cross-border

[6] One for each concessionary that operates certain routes that were defined as the geographic dimension of the relevant markets involved.

connecting traffic (see below), a victim of such practices would have to pursue burdensome procedures in an effort to obtain remedial measures. For example, in order to obtain a rate decision from ARTF, a victim of anticompetitive rates would first have to seek from COFECE a declaration of lack of effective competition under Article 96 of the FECL. For such an investigation, an applicant must present extensive information to define the relevant market and establish substantial market power under the terms of the antitrust law.

Article 96 investigations are lengthy and complex. To date, COFECE has conducted four investigations under Article 96 (two being the ones opened in 2016 and 2018 in the railway sector). The three investigations that went forward to conclusion had an average time of 16 months from start of the procedure to its closing. Other COFECE investigations (focused on barriers to competition or essential facilities under Article 94 of the FECL) have taken an average of 21 months from start to closing. In one case involving airport slots, it took four years to complete the proceeding, including an *amparo* procedure.

A declaration of barriers to competition or declaration of an essential facility under Article 94 of the FECL could lead COFECE to order measures to eliminate the barrier or regulate the access to the essential facility. However, the first time COFECE tried to use this new authority, it was challenged in an *amparo* procedure in the case involving airport slots referenced previously. The tribunal concluded that the investigation had infringed the regulatory purview of the SICT. In 2021, COFECE unsuccessfully challenged SICT jurisdiction over allocation of slots in saturated airports before the Mexico Supreme Court, which confirmed SICT jurisdiction over slots.

Turf battles between Mexican regulatory agencies add to the standard delay and dysfunction that accompany any effort by the agencies to enforce provisions addressed to

anticompetitive conduct. Another recent complication is COFECE's inability to vote on certain matters, including the special procedures related to barriers to competition or essential facilities (prescribed by Article 94 of the FECL), due to lack of a quorum in its plenum of commissioners. To date, COFECE has had to suspend one investigation due to lack of a quorum, the result of a decision by Mexico's President to put a hold on nominations.

ARTF tariff regulation has been limited in part as a result of the split of responsibilities between that agency and COFECE. As explained above, in order for ARTF to proceed with tariff regulation, COFECE must first issue a declaration of lack of effective competition in the market at issue. Since its inception ARTF has opened only three tariff regulation procedures, all based on the 2020 declaration (issued in the procedure opened in 2018). Each ARTF decision has been challenged through federal annulment procedures and *amparo* claims, none of which has yet been ruled on. In any case involving claims of anticompetitive rates, there is a potential for overlapping agency authority and turf battles, since provision of rail services in an anticompetitive manner could be seen as a breach of both the FECL and the RSL. ARTF decisions may be appealed to federal administrative and judiciary tribunals and in some cases could be challenged directly by *amparo* proceedings in federal courts. Moreover, challenges to ARTF's actions can include litigation seeking the issuance of preliminary injunctions against the agency issued by administrative or judiciary courts, adding a new layer of complexity as well as potential delays.

Thus, even if it were clear that a shipper or competing carrier could invoke Mexican laws and regulations in an effort to remedy any discriminatory rate practices by CP/KCS, seeking relief through the ARTF and/or COFECE would entail lengthy administrative and

judicial procedures. The situation is complicated by the split of authority between COFECE and ARTF, creating more opportunities to challenge their acts – before multiple administrative agencies and/or administrative and judicial federal courts in Mexico.

Given the uncertainty about whether anticompetitive rate practices can be addressed under Mexican laws and regulations, the absence of effective enforcement by the antitrust and rail regulation agencies, and the complexities resulting from the split of jurisdiction between the two agencies, the STB cannot assume that Mexican agencies will provide effective remedies for potential anticompetitive rate practices of the type that UP believes a combined CP/KCS is likely to pursue following the merger to take cross-border traffic from competitors. I have seen no indication that this situation is likely to change in the foreseeable future.

II. COFECE HAS APPROVED THE MERGER OF CP-KCSM WITH NO CONDITIONS.

On October 4 and 5, 2021 KCS and CP filed a merger control notice with each of COFECE and the Federal Institute of Telecommunications (Instituto Federal de Telecomunicaciones) (the "FTI").[7] On November 25, 2021, COFECE issued a decision unconditionally clearing the CP-KCS Merger. The four-page decision states only that "from the assessment undertaken by this Commission, it is considered that, if the notified transaction is carried out, it would have low probabilities of affecting competition." Based on this very brief statement I cannot tell whether COFECE had any concern about, or

[7] Because KCSM and Ferrovalle (in which KCSM has a 25% interest) have certain telecommunication concession titles, the FTI, which serves as the antitrust authority in the broadcasting and telecommunications sectors, handled the assessment of concentration in the telecom sector. In its decision, issued on November 3, 2021, the FTI cleared the transaction unconditionally. It considered that CP has no activities in the telecommunications and broadcasting sector and determined that the CP-KCS Merger would not have any anticompetitive effects in telecommunications and broadcasting services.

conducted any assessment of, whether the transaction could affect competition in cross-border rail traffic. It is likely that COFECE concerned itself only with competition within Mexico and that it did not consider any potential competitive impact of the merger within the United States.

III. THE STB'S IMPOSITION OF CONDITIONS REQUIRING CP-KCS-KCSM TO OFFER COMPETITIVE RATES AND NOT DISCRIMINATE AGAINST COMPETITIVE CONNECTIONS IS CONSISTENT WITH MEXICAN LAW AND WOULD NOT INTERFERE WITH THE PREROGATIVES OF MEXICAN AGENCIES.

I understand that UP plans to ask the STB to impose conditions on the CP-KCS Merger that would require CP/KCS to comply with commitments they are offering regarding the Laredo Bridge and use of their control over KCSM to ensure that KCSM continues to work with UP on cross-border traffic via the Laredo Gateway and continues to provide commercially reasonable rate factors that allow UP-KCSM services to remain competitive. UP will urge the STB to include conditions that would more specifically define when KCSM rate factors will be considered commercially reasonable.

Imposition of such conditions by the STB would not interfere with the role of any relevant Mexican governmental agency or conflict with Mexican legal principles. As discussed above, Mexican railroad law requires that KCSM cooperate with its connections on a non-discriminatory basis, including on the rates it sets and the services it provides. Commitments CP and KCS have made appear designed to ensure that their control of KCSM does not adversely affect the way KCSM behaves with respect to its other connections, including UP, on international traffic flows. This is entirely consistent with Mexican law and regulations.

Mexican authorities would not question the STB's role in taking steps to protect competition for international traffic flows that benefit U.S. customers. No agency of the

Mexican government has taken on the protection of rail competition in the United States that depends on cooperation from KCSM for the portion of the movement from Laredo south. In general, the Mexican agencies (COFECE and ARTF) are not concerned with competition on the U.S. segment of traffic originating in or destined for Mexico; they focus entirely on competition in Mexican territory. Requiring CP/KCS to use its control of KCSM to ensure that KCSM works with UP on traffic moving across the border and quotes commercially reasonable rates for UP-KCSM cross-border interline movements would not interfere inappropriately in internal Mexican affairs nor require KCSM to do anything inconsistent with Mexican legal requirements. Such a requirement would be consistent with the principles of non-discrimination reflected in the RSL and the KCSM's Concession.

Although the RSL and KCSM's Concession title contain certain provisions addressing discriminatory pricing practices by KCSM, and such practices could be assessed under the Mexican antitrust regime, this is not a practical concern. There is no precedent that I am aware of that establishes whether these anti-discrimination provisions could be applied to KCSM and U.S. connecting carriers other than CP/KCS and to the sorts of discriminatory rate practices that are the focus of UP's concern. As noted above, to my knowledge, neither the ARTF nor COFECE have ever investigated a case involving allegations of rate discrimination. And as explained above, seeking remedies from the ARTF and/or COFECE would entail lengthy administrative and judicial procedures – a situation complicated by the split of authority between COFECE and ARTF, raising multiple opportunities to challenge their acts. In these circumstances, it is clear that action by the STB to address concerns about rate discrimination affecting cross-border traffic would not be regarded as interference with the prerogatives of Mexican antitrust and rail agencies.

Imposition of conditions by the STB would also be consistent with the terms of the United States-Mexico-Canada Agreement ("USMCA," the successor to NAFTA). Under Article 21.1.2 of the USMCA a Party is not prevented from "applying its national competition laws to commercial activities outside its borders that have an appropriate nexus to its jurisdiction." I believe the STB's imposition of the non-discrimination conditions requested by UP would fall within this provision.

VERIFICATION

I, Luis F. de la Calle, declare under penalty of perjury under the laws of the United States that the foregoing is true and correct. Further, I certify that I am qualified and authorized to file this Verified Statement.

Executed on February 23, 2022

/s/ Luis F. de la Calle

EXHIBIT 1

[REDACTED]

EXHIBIT 2

[REDACTED]

EXHIBIT 3

BEFORE THE
SURFACE TRANSPORTATION BOARD

Finance Docket No. 36500

CANADIAN PACIFIC RAILWAY LIMITED, *ET AL.*
– CONTROL –
KANSAS CITY SOUTHERN, *ET AL.*

KANSAS CITY SOUTHERN AND CANADIAN PACIFIC'S JOINT RESPONSES AND OBJECTIONS TO UNION PACIFIC RAILROAD COMPANY'S FIRST SET OF DISCOVERY REQUESTS

Pursuant to 49 C.F.R. Part 1114, Subpart B, Canadian Pacific Railway Limited, Canadian Pacific Railway Company, Soo Line Railroad Company, Central Maine & Quebec Railway US Inc., Dakota, Minnesota & Eastern Railroad Corporation, and Delaware and Hudson Railway Company, Inc. (collectively, "Canadian Pacific" or "CP") and Kansas City Southern, The Kansas City Southern Railway Company, Gateway Eastern Railway Company, and The Texas Mexican Railway Company (collectively, "KCS"; together with CP, the "Applicants") hereby respond and object as follows to Union Pacific Railroad Company's First Set of Discovery Requests to Applicants (the "UP Requests") served on November 8, 2021 in connection with the above-captioned proceeding.

GENERAL OBJECTIONS

The following General Objections apply to each of the UP Requests and shall have the same force and effect as if set forth in full in response to each individually numbered UP Request.

1. Applicants object to the UP Requests and to each Definition, Instruction and Request contained therein to the extent they purport to impose upon the Applicants burdens

Request No. 39:

Produce documents sufficient to show the post-acquisition growth of traffic to/from Central Maine & Quebec Railway US Inc.

Response to Request No. 39:

Subject to and without waiving the General Objections and the specific objections set forth above, Applicants will provide non-privileged and non-duplicative documents responsive to this Request that they are able to locate after a reasonable search.

Request No. 40:

Describe in detail the meaning of the phrase "commercially reasonable terms," as the phrase is used on page 14 of the Creel VS.

Response to Request No. 40:

In addition to the General Objections set forth above, Applicants object to this Request on the grounds that it is unduly burdensome and not proportional to the needs of this proceeding. Applicants further object to this Request on the grounds that the Application speaks for itself. Applicants further object to this Request to the extent that it improperly calls for legal analysis, arguments or conclusions.

Subject to and without waiving the General Objections and the specific objections set forth above, Applicants respond that the phrase "commercially reasonable terms" as used in this context (Application Vol. 1 at 1-169) refers to Applicants' commitment that they will keep affected gateways open on commercially reasonable terms. Applicants will continue to support efficient interchange from an operational standpoint, and they will also offer shippers commercial terms that support interline transportation options that shippers have chosen, if shippers desire such options in the future. Thus, the referenced "terms" are those that CPKC

would be prepared to offer to potential rail transportation customers (or, if desired by a customer, to other railroads for purposes of constructing a through rate) in connection with post-Transaction interline rail services for shipments handled on an interline basis prior to the Transaction and for which the Transaction made possible new CPKC single-line alternatives. Such terms would be "commercially reasonable" in the sense that they would be established by CPKC in good faith to provide customers with the option of continued movement of rail traffic via an affected pre-Transaction interline route if that route was preferred by a shipper.

Request No. 41:

Describe in detail the Applicants' "detailed integration planning," as described on page 16 of the Creel VS, in relation to operations via the Laredo gateway.

Response to Request No. 41:

In addition to the General Objections set forth above, Applicants object to this Request on the grounds that it is unduly burdensome and not proportional to the needs of this proceeding. Applicants further object to this Request on the grounds that the Application speaks for itself. Applicants further object to this Request to the extent that it improperly calls for legal analysis, arguments or conclusions.

Subject to and without waiving the General Objections and the specific objections set forth above, Applicants respond that Applicants' detailed integration planning includes the work undertaken to prepare the Operating Plan, described in detail in Exhibit 13 to the Application, as well as the planning relating to service assurance and IT systems described in detail in the Verified Statement of James Clements and the planning relating to labor force needs described in detail in the Verified Statements of Chad Rolstad and Myron Becker, and also reflected in the Labor Impact Exhibit. *See also* Verified Statement of John Brooks at 23-25

Request No. 99:

Produce all documents discussing whether KCS or KCSM is collecting "the full measure of returns associated with its existing market power." *See* Majure VS at 15.

Response to Request No. 99:

In addition to the General Objections set forth above, Applicants object to this Request on the grounds that it is overly broad, unduly burdensome, and not proportional to the needs of this proceeding. Applicants further object to this Request as unduly burdensome and overly broad as it seeks "all" documents underlying an economic concept. KCS does not discuss whether it or KCSM collects "the full measure of returns associated with its existing market power" in its ordinary course of business.

Subject to and without waiving the General Objections and the specific objections set forth above, Applicants respond that KCS does not have any responsive documents.

Request No. 100:

Produce all documents discussing whether KCS rates or KCSM rates are subject to "a regulatory constraint." *See* Majure VS at 16.

Response to Request No. 100:

In addition to the General Objections set forth above, Applicants object to this Request on the grounds that it is overly broad, unduly burdensome, and not proportional to the needs of this proceeding. Applicants further object to this Request as unduly burdensome and overly broad as it seeks "all" documents regarding regulation of KCS or KCSM rates. Applicants further object to this Request to the extent that it seeks documents protected from discovery by the attorney-client privilege, attorney work product doctrine or any other applicable

privilege, protection, immunity, law, or rule. Applicants further object to the extent that the information is publicly available or in UP's possession.

Subject to and without waiving the General Objections and the specific objections set forth above, Applicants refer UP, and incorporate by reference, Applicants' Objections and Responses to Request Nos. 63 and 64.

Request No. 101:

Produce all documents discussing whether KCSM rates are constrained by "competitive pressure from other rail . . . options." *See* Majure VS at 16.

Response to Request No. 101:

In addition to the General Objections set forth above, Applicants object to this Request on the grounds that it is overly broad, unduly burdensome, and not proportional to the needs of this proceeding. Applicants further object to this Request as unduly burdensome and overly broad as it seeks "all" documents discussing whether KCSM rates are constrained by "competitive pressure from other rail options." Applicants further object to this Request as unduly burdensome and overly broad as it seeks "all" documents underlying an economic concept. Applicants further object to this Request to the extent that it could be interpreted to refer to any document in which KCSM competes with a competitor and this would entail a substantial part of KCS business and encompass nearly all business documents. Applicants further object to this Request to the extent that it seeks documents protected from discovery by the attorney-client privilege, attorney work product doctrine or any other applicable privilege, protection, immunity, law, or rule. Applicants further object to the extent that the information is publicly available or in UP's possession.

Subject to and without waiving the General Objections and specific objections, Applicants respond that KCS does not maintain documents in the ordinary course of business that discuss the extent to which KCSM rates are "constrained by 'competitive pressure from other rail…options'" and thus has no responsive documents.

Request No. 102:

Describe what the term "level of access" means, as the phrase is used on page 17 of the Brown/Zebrowski VS, and how various "levels of access" factored into the diversion analysis performed by Messrs. Brown and Zebrowski, and produce all workpapers addressing how "level of access" factored into the diversion analysis performed by Messrs. Brown and Zebrowski.

Response to Request No. 102:

In addition to the General Objections set forth above, Applicants object to this Request on the grounds that it is overly broad, unduly burdensome, and not proportional to the needs of this proceeding.

Subject to and without waiving the General Objections and the specific objections set forth above, Applicants respond that the term "level of access" as used on page 17 of the Brown/Zebrowski VS (Application Vol. 2 at 2-129) refers to the extent to which CP or KCS would likely be able to provide service for the traffic at issue at origin and/or destination. For example, Messrs. Brown and Zebrowski considered whether CP or KCS or a connecting shortline served the stations where the traffic was originated and terminated, whether CP or KCS had served the pertinent shipper facilities in the past or in connection with shipments of the same or different commodities to or from alternative destinations or origins, whether a CPKC route between the origin and destination would be unduly circuitous, whether alternative origin or

EXHIBIT 4

PUBLIC VERSION - REDACTED

CPR-5

BEFORE THE
SURFACE TRANSPORTATION BOARD

STB Finance Docket No. 34342

KANSAS CITY SOUTHERN
— CONTROL —
THE KANSAS CITY SOUTHERN RAILWAY COMPANY
GATEWAY EASTERN RAILWAY COMPANY,
AND THE TEXAS MEXICAN RAILWAY COMPANY

ADDITIONAL COMMENTS OF CANADIAN PACIFIC RAILWAY COMPANY

Paul Guthrie
Canadian Pacific Railway Company
401 9th Avenue, S.W.
Gulf Canada Square, Suite 500
Calgary, Alberta T2P 4Z4 Canada
(403) 319-6184
(403) 319-6770 (Fax)

Terence M. Hynes
Gabriel S. Meyer
Sidley Austin Brown & Wood LLP
1501 K Street, N.W.
Washington, D.C. 20005
(202) 736-8000
(202) 736-8711 (Fax)

Counsel for Canadian Pacific Railway Company

DATED: September 30, 2004

PUBLIC VERSION - REDACTED

BEFORE THE
SURFACE TRANSPORTATION BOARD

STB Finance Docket No. 34342

KANSAS CITY SOUTHERN
— CONTROL —
THE KANSAS CITY SOUTHERN RAILWAY COMPANY
GATEWAY EASTERN RAILWAY COMPANY,
AND THE TEXAS MEXICAN RAILWAY COMPANY

ADDITIONAL COMMENTS OF CANADIAN PACIFIC RAILWAY COMPANY

Pursuant to the Board's *Decision No. 11* served in the above-captioned proceeding on August 31, 2004, Canadian Pacific Railway Company and its wholly-owned subsidiaries, Soo Line Railroad Company ("Soo") and Delaware and Hudson Railway Company, Inc. ("D&H") (collectively, "CPR") submit these additional comments concerning the application of Kansas City Southern ("KCS") to acquire control of The Texas Mexican Railway Company ("TexMex").

As indicated in its prior submissions, CPR takes no position as to whether the proposed KCS/TexMex control transaction ought to be approved. *See* CPR-3, Comments filed August 4, 2003 at 1. However, if the Board decides to approve KCS' application to control TexMex, CPR urges the Board to impose a condition requiring Applicants to enter into one or more written agreements that would assure non-Applicant carriers serving the "NAFTA Corridor" future access to the Laredo gateway on commercially reasonable terms. Such a condition is necessary to preserve effective rail competition for traffic moving between points in Canada and the United States, on the one hand, and points in Mexico, on the other hand, in the event that KCS' plan to acquire both TexMex and TFM, S.A. de C.V. ("TFM") is successful.

Applicants acknowledge that the continued growth of NAFTA trade depends upon the availability of competitive transportation alternatives for traffic moving to/from Mexico. *See* KCS-10/TM-10, Supplement to Application at 13. Yet, while Applicants vaguely assert that they would "keep the Laredo gateway open on commercially reasonable terms" (*see, e.g., id.* at 4, 24), they have not committed on the record to any specific measures to assure that result. Instead, Applicants have suggested that carriers interested in access to the Laredo gateway seek to negotiate "a private agreement to ensure that KCS abides by this commitment." *See* CPR-3, Comments, Attachment 1 (Letter dated July 21, 2003 from Mr. Mullins to Mr. Meyer at 2). The condition proposed by CPR would simply require Applicants to follow through with their own suggestion by entering into a written agreement (or agreements) defining the "commercially reasonable" terms upon which non-Applicant railroads (and the shippers that they serve) will be able to access the Laredo gateway in the event that KCS creates its proposed "NAFTA Rail" system by acquiring both TexMex and TFM.

The reasons why such a condition is both necessary and appropriate are discussed in detail in CPR's prior submissions. As CPR demonstrated, the Laredo gateway plays an indispensable role in the movement of rail freight to and from Mexico – indeed, nearly 90 percent of all traffic handled by CPR to and from Mexico currently moves via Laredo. *See* CPR-3, Comments at 4; CPR-4, Reply Comments filed September 2, 2003 at 3. The Board has frequently acknowledged that Laredo "occupie[s] a position of separate and surpassing economic significance" among the rail gateways serving the U.S. – Mexico border. *Union Pacific Corporation, et. al. – Control and Merger – Southern Pacific Rail Corporation, et al.("UP/SP")*, 1 S.T.B. 233, 422 (1996) (emphasis added).[1]

[1] *See also id. at 565* (Laredo "the premier Eastern Mexico gateway"); *Santa Fe Southern Pacific Corp. – Control – SPT Co.*, 2 I.C.C. 2d 709, 797 (1986) (Laredo "by far the most important" Mexican rail gateway); *id.* at 894-895 ("Laredo historically has been the foremost international rail gateway to Mexico").

KCS' proposal to acquire both TexMex and TFM would give it control of one of the two U.S. carriers serving the Laredo gateway as well as the only carrier (TFM) providing connecting service to/from points in Mexico. If the "NAFTA Rail" system were to exercise that control in a manner that closed the Laredo gateway commercially to competing railroads (*e.g.*, by refusing to participate in interline routes on reasonable terms), the competing services by CPR and others (in conjunction with UP) in the NAFTA Corridor would be severely impaired. The condition requested by CPR is designed to assure the continued viability of those competing rail routes following the creation of a NAFTA Rail system.

Nothing that has occurred since the Board suspended these proceedings in October 2003 obviates the need for such a condition. As Applicants acknowledge, "the differences between the previous transaction and the revised transaction [now before the Board] are minor in nature and do not involve any changes in the substantive areas of concern" that the Board must consider in this proceeding. KCS Status Report filed August 16, 2004 at 3 (emphasis added). *See also Decision No. 11* at 5. While the revised KCS/TMM Stock Purchase Agreement commits KCS to comply with existing protocols regarding "use and operation" of the International Bridge at Laredo (*see* Revised Stock Purchase Agrt., § 5.1), it contains no provision that would require Applicants to preserve the commercial access of competing carriers to the Laredo gateway. Even KCS' limited commitment to observe protocols for operation of the International Bridge would be rendered moot if KCS acquires TFM, which controls the southern half of the bridge. Thus, KCS' revised proposal – like its prior submissions – fails to give substance to its representation that the Laredo gateway will remain open to KCS' competitors on commercially reasonable terms.

Moreover, recent events have made a KCS acquisition of TFM more likely than it was at the time the Board suspended this proceeding in *Decision No. 10*. The Board's action was

triggered by the decision of the shareholders of Grupo TMM, S.A. ("TMM"), on August 18, 2003, to reject the KCS/TFM Acquisition Agreement, and TFM's subsequent exercise of its right to repurchase from KCS the 51 percent interest in Mexrail upon which KCS' control application was predicated. However, on March 22, 2004, an arbitration panel ruled that shareholder rejection of the KCS/TFM Acquisition Agreement did not authorize TMM to terminate the Agreement.[2] In the wake of that decision, KCS and TMM renewed their negotiations regarding the sale of TFM, and TMM agreed to support KCS' application to the Mexican Foreign Investment Commission ("MFIC") for authority to acquire a controlling interest in TFM.[3]

On September 16, 2004, MFIC gave notice that it was denying KCS' application to acquire TFM. However, in a joint press release, KCS and TMM stated:

> "KCS and TMM are actively involved in discussions with the FIC and believe that they are close to an agreement to resolve these matters. KCS and TMM will seek reconsideration of this decision and remain confident that they should ultimately obtain approval of the transaction.[4]

KCS and TMM have also agreed to extend the deadline for closing under the KCS/TFM Acquisition Agreement until June 15, 2005 "to provide additional time to complete the transaction." *Id.*

Thus, it now appears that TMM is actively supporting KCS' efforts to acquire TFM, and that the prospects for completion of the KCS/TFM transaction are considerably better than they were prior to the suspension of these proceedings in *Decision No. 10*. The danger that future rail competition via Laredo might be compromised by a NAFTA Rail system wielding exclusive

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[2] *See* Attachment 1, "Interim Award in Arbitration Between TMM and KCS" (press release issued by TMM on March 22, 2004).

[3] *See* Attachment 2, "KCS Clarifies Obligations Under Stipulation Agreement" (press release issued by KCS on April 12, 2004).

[4] *See* KCS Sixth Status Report, filed September 16, 2004, Attachment, "Kansas City Southern and Grupo TMM To Seek Reconsideration of Mexican Foreign Investment Commission Decision" (joint press release) at 1 (emphasis added).

control over that vital gateway is likewise heightened. So long as KCS continues to pursue an acquisition of TFM, the public interest requires that the Board, in ruling on the KCS/TexMex control application, take into account "the broader transaction, incorporating the related KCS/TFM component," as contemplated by *Decision No. 2*.

KCS continues to take the position that the Board "has no legal authority" to consider the competitive effects of KCS' strategy to create a combined KCS/TexMex/TFM system. *See, e.g.*, KCS-10/TM-10 at 3, n.2. Most recently, in refusing to respond to discovery requests inquiring about the status of the KCS/TFM transaction, KCS asserted: "Whether or not KCS acquires control of TFM is irrelevant inasmuch as acquisition of TFM, which operates entirely in Mexico, is a proposed transaction that is beyond the jurisdiction of the STB and is, instead, subject to the jurisdiction of Mexican authorities." *See* KCS' Responses and Objections To Union Pacific Railroad Company's Fourth Set of Discovery Requests to Applicants, filed September 8, 2004 at 4-5. *See also id.* at 6 (objecting to production of documents analyzing possible acquisition of TFM on the grounds that "[t]he requested documents, insofar as they relate to KCS's interest in acquiring control of TFM, are irrelevant because that matter is outside of the Board's jurisdiction").

KCS is wrong. As the Board has correctly observed, KCS' proposal to acquire TFM, while subject to regulation by Mexican authorities, has "broader potential implications in the U.S." *Decision No. 2* at 11. Accordingly, "the role played by TFM in the U.S.-Mexico NAFTA corridor cannot be ignored" in considering the merits of the KCS/TexMex proposal. *Id.* at 10. For that reason, the Board instructed Applicants to supplement their application with evidence addressing the potential effects of a KCS/TFM consolidation on rail competition in the United States. *Id.* at 10-11 (emphasis added). More recently, the Board's order restarting this proceeding expressly extended the requirement (imposed in *Decision No. 10*) that KCS file

periodic status reports "detailing new developments (if any) in its efforts to acquire control of TFM." *Decision No. 11* at 6.

These rulings leave no doubt that the Board can – and should – consider the potential effects of KCS acquiring control of TFM in deciding whether to approve the KCS/TexMex transaction. The Board should likewise exercise its conditioning authority in this case to assure that a prospective "NAFTA Rail" system could not undermine future rail competition at the Laredo gateway. Indeed, this proceeding presents the only opportunity for the Board to do so, because KCS will not be required to return to the Board for authority to acquire TFM. (A condition imposed by the Board now, but made contingent upon KCS succeeding in acquiring TFM, would not impose any burden on Applicants if KCS abandoned its pursuit of TFM.)

As CPR has previously shown (CPR-4, Reply Comments at 2-3), Applicants' settlement arrangement with the National Industrial Transportation League ("NITL") – which Applicants have asked the Board to impose as a condition – does not mitigate the potential for competitive harm in the event that a combined "NAFTA Rail" system gains control of the Laredo gateway. Both Applicants and NITL frankly acknowledge that "[t]he NITL-KCS Agreement will not require NAFTA Rail to establish and maintain commercially reasonable contract or common carrier rates and charges with respect to traffic interchanged between UP and TFM at the Laredo Gateway." *See* NITL-4/KCS-17, Letter to Mr. Meyer dated August 18, 2003 at 1. The KCS-NITL settlement applies only to U.S-Mexico cross-border movements in which KCS and/or TexMex are the participating carriers, and preserves interline competition only at interchange points other than Laredo. The KCS-NITL Agreement does not address the ability of non-Applicant railroads to access the Laredo gateway on commercially reasonable terms following the creation of a "NAFTA Rail" system, and therefore does not respond to the competitive concerns identified in CPR's comments.

The Board's prior decisions demonstrate a strong commitment to ensuring that railroad mergers do not undermine the goals of NAFTA. *See, e.g., UP/SP*, 1 S.T.B. at 421-426 (imposing trackage rights condition to preserve TexMex's ability to compete for U.S.-Mexico rail traffic via Laredo); *Canadian National Ry. Co., et al. – Control – Illinois Central Corporation, et al.* (served May 21, 1999) ("*CN/IC*") at 35-36 (condition imposed to prevent interference with rail tunnel serving US/Canada gateway at Detroit). The Board also routinely requires applicant carriers to abide by any representations they make on the record. *See, e.g., Canadian National Ry. Co. et al. – Control – Wisconsin Central Transportation Corp., et al.,* (decision served September 5, 2001) ("*CN/WC*") at 12-14 (condition holding applicants to representations regarding preservation of rail gateways); *CN/IC* at 7, n. 21 (1999) (condition holding applicants to all representations made in writing and at oral argument); *CSX Corporation, et al. and Norfolk Southern Corporation, et al. – Control and Operating Leases – Conrail, Inc. et al.*, 3 S.T.B. 196, 387 (1998) (applicants required to adhere to all representations made during proceeding).

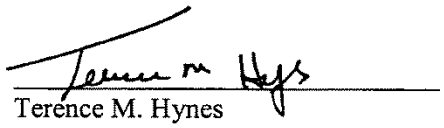
It is equally appropriate for the Board to exercise its conditioning authority in this case to compel Applicants to adhere to their promise to keep the Laredo gateway open on "commercially reasonable terms" by requiring them to enter into binding written agreement(s) setting forth the terms upon which competing carriers will be able to access Laredo in the event that KCS acquires control of both TexMex and TFM. Such agreement(s) should apply to <u>all</u> rail routings via Laredo, including the TFM-UP routes excluded from the scope of the KCS-NITL Agreement. The specific terms of such an arrangement can be left, in the first instance, to negotiation between Applicants and other carriers serving the NAFTA Corridor. If the parties fail to reach agreement, the Board could then act as needed to define such terms.

CPR's proposed condition is necessary to preserve effective competition for rail traffic to/from Mexico in the event that TexMex and TFM come under the common control of KCS. Given the unique importance of the Laredo gateway to NAFTA trade, the Board should act in this proceeding to assure that a KCS-TFM consolidation does not compromise the competitive rail system serving the NAFTA Corridor.

CONCLUSION

For all of the foregoing reasons, and those set forth in CPR's Comments (CPR-3) and Reply Comments (CPR-4), CPR respectfully requests that the Board condition its approval of the proposed transaction by requiring Applicants to enter into binding written agreement(s) specifying commercially reasonable terms upon which competing railroads (including CPR) can route traffic to or from Mexico via the Laredo gateway in the event that KCS acquires control of both TexMex and TFM.

Respectfully submitted,



Paul Guthrie
Canadian Pacific Railway Company
401 9th Avenue, SW
Gulf Canada Square, Suite 500
Calgary, Alberta T2P 4Z4 CANADA
(403) 218-7474

Terence M. Hynes
Gabriel S. Meyer
Sidley Austin Brown & Wood
1501 K Street, N.W.
Washington, D.C. 20005
(202) 736-8000

Counsel for Canadian Pacific Railway Company

DATED: September 30, 2004

CPR-5

CERTIFICATE OF SERVICE

I hereby certify on this 30th day of September 2004, that I caused copies of the foregoing Additional Comments of Canadian Pacific Railway Company to be served, by hand-delivery on Applicants' counsel, and by first-class mail, postage prepaid, on all other Parties of Record.

Terence M. Hynes

EXHIBIT 5

[REDACTED]

EXHIBIT 6

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

SCHEDULE 14A

Proxy Statement Pursuant to Section 14(a) of the Securities Exchange Act of 1934 (Amendment No.)

Filed by the Registrant ☒ Filed by a Party other than the Registrant ☐

Check the appropriate box:

☐ Preliminary Proxy Statement

☐ **Confidential, for Use of the Commission Only (as permitted by Rule 14a-6(e)(2))**

☒ Definitive Proxy Statement

☐ Definitive Additional Materials

☐ Soliciting Material under §240.14a-12

KANSAS CITY SOUTHERN
(Name of Registrant as Specified In Its Charter)

(Name of Person(s) Filing Proxy Statement, if other than the Registrant)

Payment of Filing Fee (Check the appropriate box):

☒ No fee required.

☐ Fee computed on table below per Exchange Act Rules 14a-6(i)(1) and 0-11.

(1) Title of each class of securities to which transaction applies:

(2) Aggregate number of securities to which transaction applies:

(3) Per unit price or other underlying value of transaction computed pursuant to Exchange Act Rule 0-11 (set forth the amount on which the filing fee is calculated and state how it was determined):

(4) Proposed maximum aggregate value of transaction:

(5) Total fee paid:

☐ Fee paid previously with preliminary materials.

☐ Check box if any part of the fee is offset as provided by Exchange Act Rule 0-11(a)(2) and identify the filing for which the offsetting fee was paid previously. Identify the previous filing by registration statement number, or the Form or Schedule and the date of its filing.

Table of Contents

"*The KCS Merger Proposal—Opinion of Morgan Stanley*" and "*The KCS Merger Proposal—Opinion of BofA Securities*" on pages 72 and 85, respectively. After further discussion and deliberation, the KCS board unanimously determined that the final CPRL proposal continued to constitute a company superior proposal and approved the proposed waiver letter agreement with CN, termination of the CN merger agreement, KCS's payment of the $700.0 million CN agreement termination payment and the $700.0 million CN refund owed to CN (or its affiliates) under the terms of the CN agreement, and KCS's entry into the merger agreement with CPRL. The KCS board also approved the updated retention and severance arrangements set forth in the final CPRL proposal.

Following the completion of the KCS board meeting, KCS management notified CN of the KCS board's determination, after which KCS and CN entered into the waiver letter agreement and KCS terminated the CN agreement and paid the $700.0 million CN agreement termination payment. Shortly thereafter, KCS delivered an executed signature page to the merger agreement with CPRL, which had already been executed by CPRL, and KCS and CPRL issued a joint press release announcing the transaction. Following execution of the merger agreement, CPRL remitted to KCS $700.0 million in connection with the payment of the CN agreement termination payment made by KCS to CN, KCS paid the $700.0 million CN refund to an affiliate of CN, and CPRL remitted to KCS $700.0 million in connection with the payment of the CN refund made by KCS to an affiliate of CN.

Recommendation of the KCS Board; KCS's Reasons for the Transaction

At a special meeting held on September 15, 2021, the KCS board unanimously: (1) determined that it was in the best interests of KCS and its stockholders, and declared it advisable, to enter into the merger agreement with CPRL; (2) approved the execution, delivery and performance of the merger agreement and the transactions contemplated by the merger agreement (including the merger); (3) recommended that the stockholders of KCS adopt the merger agreement; and (4) directed that the merger agreement be submitted to a vote at a meeting of KCS's stockholders. **The KCS board unanimously recommends that KCS stockholders vote "FOR" the merger proposal.**

In evaluating the transaction and in reaching its determinations and making its recommendations with respect to the merger agreement, the KCS board consulted with KCS senior management and outside legal and financial advisors over the course of several meetings, and considered a number of factors, including the following material factors that weighed in favor of the transaction.

Strategic Considerations and Synergies:

- The KCS board believes the transaction will create the first rail network connecting the U.S., Mexico and Canada, with the ability to deliver dramatically expanded market reach for KCS and CPRL customers, provide new competitive transportation options, provide infrastructure, public safety and environmental benefits through truck to rail conversion opportunities, and support North American economic growth;
- The KCS board believes CPRL and KCS are the fastest growing Class 1 railroads, with significant success in the transformation to Precision Scheduled Railroading;
- The KCS board considered a synergy analysis (based on CPRL's synergies analysis) showing annualized EBITDA synergies for the combined company of approximately $990 million (plus $20 million of capital expenditure and depreciation and amortization synergies) expected to be realized within the first three years after the transaction, primarily by executing the combined growth strategies of KCS and CPRL with new efficiencies for customers and improved on-time performance under their respective PSR programs; the KCS board also considered a more conservative synergy analysis
  prepared by KCS management showing EBITDA synergies of approximately $377 million (plus

Table of Contents

$23 million of capital expenditure and depreciation and amortization synergies) over three years, and assessed both synergy analyses in making its decision, as further described in the section entitled "*KCS Unaudited Prospective Financial Information*";

- The KCS board believes that the combined company will have the scale, balance sheet strength, financial flexibility, and free cash flow to fund future growth, and improved ability to access the capital markets on more favorable terms than available to KCS as an independent company, which would allow the combined company to be more competitive in capturing strategic opportunities;
- The KCS board received information from and had discussions with KCS's management, in consultation with outside financial advisors, regarding CPRL's business, results of operations, financial and market position, KCS management's expectations concerning the combined company's business and financial prospects, and historical and current trading prices of CPRL common shares;

Attractive Value and Mix of Consideration

- The KCS board considered the aggregate value and nature of the consideration to be received in the transaction by KCS stockholders, including:
  - that the merger consideration had an implied value per share of KCS common stock of $300, based on the closing price of CPRL common shares on the NYSE as of August 9, 2021 (the last full trading day prior to the date on which CPRL submitted the revised CPRL proposal), which represented a premium of approximately 34% to KCS stockholders based on the unaffected closing price of KCS common stock on March 19, 2021 (the last trading day before the KCS board's approval of and the announcement of the prior CP merger agreement);
  - that based on CPRL's market price on September 13, 2021, approximately 69% of the merger consideration consists of CPRL common shares, with the CPRL common shares to be issued to KCS common stockholders constituting approximately 28% of the outstanding shares of CPRL common shares following the transaction, offering KCS common stockholders the opportunity for meaningful ownership participation in the future earnings, dividends, synergies and growth of the combined company, a company which the KCS board considers to be an attractive investment for the reasons discussed above in the section entitled "*Strategic Considerations and Synergies*";
  - that based on CPRL's market price on September 13, 2021, approximately 31% of the merger consideration consists of cash, which provides KCS stockholders with immediate liquidity for a portion of their shares; and
  - that the first merger and the second merger, taken together, are intended to qualify as a "reorganization" within the meaning of Section 368(a) of the Code and that Section 367(a)(1) of the Code will not apply to cause the mergers to result in gain recognition by holders of KCS common stock that exchange their shares of KCS common stock for the merger consideration (other than any Excepted Shareholder), as more fully described in the section entitled "*Material U.S. Federal Income Tax Consequences*";

Attractive Strategic Alternative:

- The KCS board believes that the transaction with CPRL is attractive in comparison to the alternative of remaining independent and continuing to execute on KCS's long-range business strategy and is also attractive in comparison to other alternatives, including the CN agreement. In this regard, the KCS board considered:
  - the course and history of KCS's discussions and competitive negotiations with Party A and CN, including: (i) the fact that, after six rounds of bidding, Party A's last proposal to acquire KCS for

EXHIBIT 7

[REDACTED]

EXHIBIT 8

[REDACTED]

EXHIBIT 9

[REDACTED]

EXHIBIT 10

UP-8

REDACTED – TO BE PLACED ON PUBLIC FILE

BEFORE THE
SURFACE TRANSPORTATION BOARD

Finance Docket No. 36500

CANADIAN PACIFIC RAILWAY LIMITED; CANADIAN PACIFIC RAILWAY COMPANY; SOO LINE RAILROAD COMPANY; CENTRAL MAINE & QUEBEC RAILWAY US INC.; DAKOTA, MINNESOTA & EASTERN RAILROAD CORPORATION; AND DELAWARE & HUDSON RAILWAY COMPANY, INC.
—CONTROL—
KANSAS CITY SOUTHERN; THE KANSAS CITY SOUTHERN RAILWAY COMPANY; GATEWAY EASTERN RAILWAY COMPANY; AND THE TEXAS MEXICAN RAILWAY COMPANY

UNION PACIFIC RAILROAD COMPANY'S MOTION TO COMPEL

EXPEDITED HANDLING REQUESTED

CRAIG V. RICHARDSON
JAMES B. BOLES
TONYA W. CONLEY
Union Pacific Railroad Company
1400 Douglas Street
Omaha, Nebraska 68179
(402) 544-5543

MICHAEL L. ROSENTHAL
PRATIK AGARWAL
Covington & Burling LLP
One CityCenter
850 Tenth Street, NW
Washington, D.C. 20001
(202) 662-6000

Attorneys for Union Pacific Railroad Company

January 27, 2022

may be somewhat over-inclusive, it may be somewhat under-inclusive. That's why you run searches and see what happens.

I've done this before. I've been on live phone calls with opposing counsel where we have adjusted the search terms to generate reasonable numbers of potentially responsive documents. I'm not sure why you've run a bunch of commodities other than plastics, and I don't think I ever asked for Intermodal, but 13,000 hits for "benzene" for one year seems like a reasonable start (especially because this is apparently for multiple people, since you say you got 11,000 hits for benzene, grain, and intermodal for one senior person). Now add terms designed to identify documents in which KCS addresses UP-KCSM moves and also addresses both single-line and interline pricing, and I suspect the number will shrink further. If you've pulled the data, it should be easy to run the tests. And if it turns out most of the hits come from spreadsheets, we can talk about excluding those documents, or making other changes to produce a reasonable number of hits.

Regards,

Mike

From: WMullins@bakerandmiller.com <WMullins@bakerandmiller.com>
Sent: Tuesday, January 18, 2022 5:25 PM
To: Rosenthal, Michael <mrosenthal@cov.com>
Cc: Cyrm@sullcrom.com; Agarwal, Pratik <PAgarwal@cov.com>; Sarnoff, Zachary A. <sarnoffz@sullcrom.com>; Vandergrift, Sophia A. <vandergrifts@sullcrom.com>; David Meyer <david@meyerlawdc.com>; eglavich@bakerandmiller.com; AMcDonald@bakerandmiller.com
Subject: RE: FD 36500 - Follow up regarding meet and confer

[EXTERNAL]

Mike, below we respond to your January 10 email. Responses in Red. The production we intended to go out last week will be out later today or tomorrow morning.

William ("Bill") A. Mullins
Partner
Baker & Miller PLLC
Suite 300
2401 Pennsylvania Ave, N.W.
Washington, D.C. 20037

(202) 663-7823 (Direct)
(202) 663-7849 (Fax)
The above message may be privileged, confidential and protected from disclosure by attorney/client. work product or other privileges. If you believe that it has been sent to you in error, do not read it. Please reply to the sender that you have received the message in error. Then delete it. Thank you.

-----"Rosenthal, Michael" <mrosenthal@cov.com> wrote: -----

To: Cyr
From: "Rosenthal, Michael" <mrosenthal@cov.com>
Date: 01/10/2022 10:03AM
Cc: "Agarwal, Pratik" <PAgarwal@cov.com>, "Sarnoff, Zachary A." <sarnoffz@sullcrom.com>, "Vandergrift, Sophia A." <vandergrifts@sullcrom.com>, David Meyer <david@meyerlawdc.com>, Bill Mullins <wmullins@bakerandmiller.com>
Subject: RE: FD 36500 - Follow up regarding meet and confer

Thanks very much for your responses. I have a few follow-up questions.

1. I realize you might have prepared this response before reviewing the email I sent yesterday, but with regard to UP Request No. 4, I have not seen any material reflecting communications with customers (and others) asking them to contact the STB or others to support the proposed transaction. While I do not expect applicants to produce copies of every document actually sent to every potential supporter, I suspect there were some standard communications and a list of recipients. If I've overlooked that information in the production, please tell me where to find it. If applicants did not solicit support statements through written communications, please let me know.

RESPONSE: In today's (or tomorrow morning's) production, KCS is producing a number of letters to third parties, template support letters sent to customers/shippers, and letters sent to US government officials. We will also provide the lists of third parties/officials who received the letters (if not obvious from documents).

2. With regard to UP Request No. 5, as indicated in the email I sent yesterday, our review of the depository points to the existence of additional submissions to COFECE and or IFT. Such documents are referenced in the documents that were produced (or so my Spanish speaking colleagues tell me).

RESPONSE: KCS is searching for and will produce additional substantive documents provided to COFECE and IFT relating to the Proposed Transaction.

3. With regard to the requests you say are complete, could you tell me where I can find documents produced in response to UP Request Nos. 70, 74, 90, 93, 113, and 122 (or confirm that your searches did not identify responsive documents).

RESPONSE:

Below are the Bates numbers for documents that are responsive primarily to the Requests you identified. As you are aware, UP's requests are extremely broad and documents may be responsive to multiple requests, including the ones you identified. This list is not intended to be comprehensive of every document that may be responsive.

Request No. 90 was mistakenly included as completed last week. Documents responsive to this request are in today's production at Bates numbers: KCSR-HC-00015675 to KCSR-HC-00015784.

UP 70 & 113: KCSR-HC-00012593

UP 74: These documents may be found under the Venue folder "HIGHLY CONFIDENTIAL - Ice Pick Documents"

UP 93: KCS does not have non-privileged documents responsive to this Request.

UP 122: KCSR-HC-00011604

KCSR-HC-00011609

KCSR-HC-00011611

KCSR-HC-00012594

KCSR-HC-00012599

KCSR-HC-00012615

KCSR-HC-00012664

KCSR-HC-00012678

KCSR-HC-00012706

KCSR-HC-00012717

KCSR-HC-00013031

4. With regard to UP Request Nos. 94 through 94, I appreciate the additional information. To be clear, are you saying that when a customer with a U.S. facility that is accessible to both KCS and UP wants to send its product to a Mexican destination served by KCSM, the same KCS personnel would set both the KCS-KCSM single line rate and the KCSM Rule 11 rate that the customer can use in conjunction with a UP Rule 11 rate (or would provide KCSM's revenue requirement to UP if the railroads offer a joint through rate)? Also, are you saying the Pricing Review Board generally addresses both single-line rates to be offered by KCS-KCSM and rates KCSM offers for shippers that want to interchange traffic with UP at Laredo?

In any event, I would not characterize the major limiting factor in the searches I'm proposing as "UP" and "rate." I'm not looking for all documents setting rates when UP interchanges traffic with KCSM or KCS. I'm looking for documents where the U.S. side of the movement is served by both KCS and UP. I expect the documents would include the terms: (1) UP (or Union Pacific), KCS, and KCSM; and (2) "single-line" or "KCS-KCSM" or "KCSM-KCS" (or whatever terminology KCS personnel use when quoting single-line KCS-KCSM rates); and (3) "Rule 11" or "UP-KCSM" or "KCSM-UP" (or whatever terminology KCS personnel use when quoting KCSM rates for traffic interchanged at Laredo with UP). I'd also suggest

focusing the initial search on Plastics, so I'd propose including (4) Plastics, polypropylene, polyethylene, polyvinyl, polystyrene, or 28211!.

RESPONSE:

We are trying to provide some background on KCS's pricing practice in light of your requests and the searches you are asking for, and not attempting to put all of KCS's pricing into an email. To that extent, when we explained the pricing groups day-to-day work, we were doing so with a focus on what your search terms ask us to do: search and produce five years-worth of day-to-day routine business.

To back up a bit, the problem here is that your requests are based on a misconception of how KCS pricing works. Your requests assume that KCS and KCSM price separately (or have independent pricing groups) and that by seeking communications between the two, you would get a picture of how rates are set. This assumption is incorrect.

KCS has a core pricing team for all rates, US and Mexico. KCS and KCSM do not have separate pricing groups - and therefore communications between the two is not dispositive.

[redacted] We already explained the basic considerations underlying pricing in our Response to UP's Request No. 148, served December 7. The Pricing Review Board reports provide insight into higher level pricing strategy.

Search terms do not resolve the undue burden problem. We ran test terms for the year 2019. For just one year: the term "benzene" brings back over 13,000 hits; "Grain" brings back almost 100,000 hit. BNSF has a similar request but asked for different commodities, including "intermodal" which brings back over a million hits for one year. Running benzene, grain, and intermodal against one senior level person brought back over 11,000 hits for one year for one person.

As such, there are some basic conceptual problems for running your proposed search. First, your (1) will pick up any instance of KCSM-KCS/KCSM-UP, which means, for example, the search will pick up every document that has in it "KCSM-KCS" and "KCSM-UP" and "plastic." Second, using "AND" as a connector means that those terms may have nothing to do with each other. This is a problem for complex spreadsheet that include disparate information. Add on top of that, as you recognize, people do not always use the official terms like "Rule 11" or "single-line" and may use shorthand, customer names, origination or destination, or other identifying language, which can greatly expand the number of terms to run. On top of that, you asked for five commodities that themselves have multiple terms. You suggested six different terms under the single commodity "plastics." You also asked for "field crops" which KCS does not recognize. We assume you mean "grain" which is a huge category and could consist of grain, soy, corn, wheat, rice, and so on, as well as STCC numbers, as well as grain by-products, such as DDG. Multiply the number of commodity terms, with the number of people, with possibly five years of

day-to-day communications, and you are asking KCS to run over a hundred search combinations and pull, search, and review millions of documents. Tweaks and alternative searches suffer from the same issues.

As we tried to explain, because there are no separate teams between KCS and KCSM and the core pricing team develops pricing on an individual basis, your Requests essentially demand KCS produce its day-to-day routine business documents for a period of five years. Specific commodities may narrow down what KCS has to produce, but the burden of searching and determining responsive documents still requires an effort that far exceeds the probative value. (We again question the value of these documents. In order to be useful in any regard, UP would have to reverse engineer individual rate discussions over time between multiple people, assuming that all relevant documents can even be identified let alone produced. Otherwise, any attempt to use a rate discussion would devolve into a debate about whether the rate discussion is complete, accurate, and representative.)

We produced the Pricing Review Board reports for your requested commodities in today's production and they may be found at Bates numbers KCSR-HC-00015675 to KCSR-HC-00015784. We invite you to review these and, if you are still missing something you need, please explain what you need so that we can get you helpful documents.

Cc: Agarwal, Pratik <PAgarwal@cov.com>; Sarnoff, Zachary A. <sarnoffz@sullcrom.com>; Vandergrift, Sophia A. <vandergrifts@sullcrom.com>; David Meyer <david@meyerlawdc.com>; Bill Mullins <wmullins@bakerandmiller.com>
Subject: RE: FD 36500 - Follow up regarding meet and confer

[EXTERNAL]

Mike,

Please see responses from CP and KCS below, in black.

Thanks,

Marc-André Cyr

Sullivan & Cromwell LLP

T: (857) 209- 1986 | cyrm@sullcrom.com

EXHIBIT 11

BEFORE THE
SURFACE TRANSPORTATION BOARD

Finance Docket No. 36500

CANADIAN PACIFIC RAILWAY LIMITED, *ET AL.*
– CONTROL –
KANSAS CITY SOUTHERN, *ET AL.*

KANSAS CITY SOUTHERN AND CANADIAN PACIFIC'S JOINT RESPONSES AND OBJECTIONS TO UNION PACIFIC RAILROAD COMPANY'S SECOND SET OF DISCOVERY REQUESTS

Pursuant to 49 C.F.R. Part 1114, Subpart B, Canadian Pacific Railway Limited, Canadian Pacific Railway Company, Soo Line Railroad Company, Central Maine & Quebec Railway US Inc., Dakota, Minnesota & Eastern Railroad Corporation, and Delaware and Hudson Railway Company, Inc. (collectively, "Canadian Pacific" or "CP") and Kansas City Southern, The Kansas City Southern Railway Company, Gateway Eastern Railway Company, and The Texas Mexican Railway Company (collectively, "KCS"; together with CP, the "Applicants") hereby respond and object as follows to Union Pacific Railroad Company ("UP")'s Second Set of Discovery Requests to Applicants ("Second UP Requests") served on November 22, 2021 in connection with the above-captioned proceeding.

GENERAL OBJECTIONS

The following General Objections apply to each of the Second UP Requests and shall have the same force and effect as if set forth in full in response to each individually numbered Second UP Request.

1. Applicants object to the Second UP Requests and to each Definition, Instruction and Request contained therein to the extent they purport to impose upon the

Response to Request No. 147:

In addition to the General Objections set forth above, Applicants object to this Request on the grounds that it is cumulative, overly broad, and unduly burdensome. The Applicants further object to this Request as duplicative of UP's Request No. 89.

Subject to and without waiving the General Objections and the specific objections set forth above, Applicants incorporate by reference the Applicants' Joint Response to UP Request No. 89.

Request No. 148:

Describe in detail how KCS sets rates for KCSR and KCSM, or allocates revenue between KCSR and KCSM, for traffic interchanged between KCSR and KCSM.

Response to Request No. 148:

In addition to the General Objections set forth above, Applicants object to this Request on the grounds that it is cumulative, overly broad, and unduly burdensome. The Request refers to the substance of much of KCS business, including its day-to-day operations, and lacks a reasonable limitation. As such it is vague and ambiguous, rendering the Request unduly burdensome and not proportional to the needs of the proceeding. The Applicants further object to this Request to the extent that it is duplicative of UP's Requests Nos. 93-97.

Subject to and without waiving the General Objections and the specific objections set forth above, Applicants respond that, generally, revenue and pricing are determined on a variety of factors and considerations, including but not limited to the market, operating and cost considerations, the type of service, volume, risk premiums (such as hazardous materials or high-end commodities), asset availability, network capacity, competitive modes of transportation, and regulatory requirements. The same considerations apply to cross-border rates. Once the overall

rate is determined, revenue divisions are assigned between KCSR and KCSM based on the circumstances particular to the move, including but not limited to mileage divisions, operating cost considerations, overall base costs (such as higher fuel costs in Mexico or additional security needs), WACC differences in the United States and Mexico, and regulatory requirements (such as TUCE (Max) rate considerations in Mexico).

Request No. 149:

Produce an electronic copy of the "KCS Runtimes/Capacity Calculations" and "KCS Capacity Calculations/Project list" spreadsheets embedded in workpaper "FD 36500 - Work Paper - HC - Capacity - Methodology.pdf."

Response to Request No. 149:

In addition to the General Objections set forth above, Applicants object to Requests Nos. 149 and 151-162 on the grounds that they are cumulative, unduly burdensome and not proportional to the needs of this proceeding.

Subject to and without waiving the General Objections and the specific objections set forth above, Applicants respond that the documents UP requests are embedded in the Workpapers that Applicants made available to UP already. Nevertheless, if UP has difficulty reading or using a particular embedded document, Applicants will respond to reasonable requests for assistance.

Request No. 150:

Produce an electronic copy of CP-related spreadsheets containing the same type of information as the spreadsheets addressed in Request No. 149.

EXHIBIT 12

REDACTED PUBLIC RECORD VERSION

BEFORE THE
SURFACE TRANSPORTATION BOARD

Finance Docket No. 36500

CANADIAN PACIFIC RAILWAY LIMITED, *ET AL.*
– CONTROL –
KANSAS CITY SOUTHERN, *ET AL.*

KANSAS CITY SOUTHERN AND CANADIAN PACIFIC'S SUPPLEMENTAL JOINT RESPONSES AND OBJECTIONS TO CSX TRANSPORTATION'S SECOND SET OF DISCOVERY REQUESTS

Pursuant to 49 C.F.R. Part 1114, Subpart B, Canadian Pacific Railway Limited, Canadian Pacific Railway Company, Soo Line Railroad Company, Central Maine & Quebec Railway US Inc., Dakota, Minnesota & Eastern Railroad Corporation, and Delaware and Hudson Railway Company, Inc. (collectively, "Canadian Pacific" or "CP") and Kansas City Southern, The Kansas City Southern Railway Company, Gateway Eastern Railway Company, and The Texas Mexican Railway Company (collectively, "KCS"; together with CP, the "Applicants"), and pursuant to several meet and confer discussions with CSXT Transportation ("CSXT") regarding its motion to compel ("Motion"), filed on January 20, 2022 in response to Applicants' initial response and objections ("Initial Response"), served on January 10, 2022, hereby supplement their Initial Response as follows to CSX Transportation's Second Set of Discovery Requests to Applicants ("Second CSXT Requests"), served on December 24, 2021 in connection with the above-captioned proceeding.[1]

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[1] By making these Supplemental Responses, Applicants do not concede the merit of any assertion made by CSXT in its Motion, and reserves all of its positions in connection therewith.

Movements, origin stations, and destination stations) for the transportation of goods to, from, or through the United States.

Response to Interrogatory No. 11:

In addition to the General Objections set forth above, Applicants object to this Request on the grounds that it is vague and ambiguous. Applicants further object to this Request on the grounds that it is overly broad, unduly burdensome and not proportional to the needs of this proceeding, including because it requests identification of "all" documents without a reasonable scope limitation. Applicants further object to this Request to the extent it seeks the identification of documents that are accessible to CSXT. Applicants further object to this Request to the extent CSXT construes this Request as a "contention interrogatory."

Subject to and without waiving the General Objections and the specific objections set forth above, Applicants respond that documents responsive to this Request are contained in the Application and accompanying Workpapers.

In further response to additional inquiries and pursuant to the parties' meet and confer discussions regarding this Request, Applicants respond by referring CSXT without limitation to the 100% traffic tapes and Carload Waybill Sample ("CWS") data that is available to CSXT.

Interrogatory No. 12:

Regarding customers served by KCSM or KCS, Identify all Analyses or other Documents You contend support the claim that "A combined CP/KCS would not be expected to have any incentive to affect the competitive terms available to a Solely-served shipper because KCS would already be collecting the full measure of returns associated with its existing market power," as stated in the Majure V.S. ¶ 24.

Response to Interrogatory No. 12:

In addition to the General Objections set forth above, Applicants object to this Request on the grounds that it is vague and ambiguous. Applicants further object to this Request on the grounds that it is overly broad, unduly burdensome and not proportional to the needs of this proceeding, including because it requests identification of "all" documents without a reasonable scope limitation. Applicants further object to this Request to the extent it seeks the identification of documents that are accessible to CSXT. Applicants further object to the extent this Request asks Applicants to perform a special study.

Subject to and without waiving the General Objections and the specific objections set forth above, Applicants respond that documents responsive to this Request are contained in the Application and accompanying Workpapers. In particular, the referenced statement of Dr. Majure was not based on any specific documentary evidence in the possession of Applicants.

In further response to additional inquiries and pursuant to the parties' meet and confer discussions regarding this Request, Applicants respond by confirming the quoted language is based on Dr. Majure's economic analysis and does not reflect an analysis that was specific to any particular customers or rates.

Interrogatory No. 13:

Identify each origin station, each destination station, and each shipper that KCSM serves in Mexico for which You contend that FXE is a "ready alternative" to KCSM as stated in the Majure Verified Statement ¶ 25.

Response to Interrogatory No. 13:

In addition to the General Objections set forth above, Applicants object to this Request on the grounds that it is vague and ambiguous. Applicants further object to this Request

on the grounds that it is overly broad, unduly burdensome and not proportional to the needs of this proceeding. Applicants further object to this Request to the extent it seeks the identification of documents or information that are accessible to CSXT. Applicants further object to the extent this Request asks Applicants to perform a special study. Applicants further object to this Request on the grounds that it misconstrues the Majure Verified Statement.

Subject to and without waiving the General Objections and the specific objections set forth above, Applicants respond that Paragraph 25 of the Majure Verified Statement reflects the application of economic theory to a range of potentially applicable facts, and does not make contentions of fact regarding specific individual stations and shippers.

In further response to additional inquiries and pursuant to the parties' meet and confer discussions regarding this Request, Applicants provide this further narrative response: Paragraph 25 of the Majure Verified Statement refers to the group of shippers that have "ready alternatives," where FXE could be one of those alternatives for such shippers. This statement was not based on a contention regarding any particular shipper's actual competitive options, though Applicants likely will assert that many KCSM shippers have effective transportation alternatives. As referenced in Dr. Majure's statement, the illustrative shipper with "ready alternatives" was presented to illuminate the range of possibilities envisioned by economic theory and analysis.

Interrogatory No. 14:

Identify all Analyses or other Documents You contend support the claim that FXE is a "ready alternative" to KCSM for each origin station, each destination station, and each shipper Identified in response to Interrogatory 13.

likely to significant opportunities for CP/KCS for reasons of circuity, shipper access, or other factors.

Interrogatory No. 27:

Identify all Analyses or other Documents You contend support the claim that competitors "would not likely be foreclosed," see Majure V.S. ¶ 34, on routes originating or terminating in Mexico, Including all Analyses or other Documents Concerning, as regards Movements to, from, or through Mexico via Laredo or other U.S./Mexico border locations:

a. KCSM market shares of those compared to those of other carriers competing for those Movements.

b. CPKC market shares compared to those of other carriers competing for those Movements

c. The competitively significant elements of KCSM service quality compared to those of other carriers competing for those Movements, Including route miles and cycle times.

d. The competitively significant elements of CPKC service quality compared to those of other carriers competing for those Movements, Including route miles and cycle times.

e. The shipper's total costs for using KCSM compared to the shipper's total costs for using other carriers competing for those Movements, Including KCSM rates and any costs shippers would to pay for services provided KCSM by other carriers, Including any haulage, trackage rights, terminal service, or switching fees.

f. The shipper's total costs for using CPKC compared to the shipper's total costs for using other carriers competing for those Movements, Including CPKC rates and any costs shippers would to pay for services provided CPKC by other carriers, Including any haulage, trackage rights, terminal service, or switching fees.

g. CPKC's ability to raise KCSM's rates or reduce KCSM's service quality Concerning Movements to or from stations in Mexico via Laredo to stations in the US. or Canada that can be served by CPKC or another carrier.

h. The economic impact on CPKC from raising KCSM's rates or reducing KCSM's service quality Concerning Movements to or from stations in

Mexico via Laredo to stations in the US or Canada that can be served by CPKC or another carrier.

i. Analyses of any conditions CPKC anticipates using to keep Laredo and other gateways open to interchange.

j. Any foreclosure Analyses Concerning KCSM.

k. Any Analysis of railroad rate regulation in Mexico.

Response to Interrogatory No. 27:

In addition to the General Objections set forth above, Applicants object to this Request on the grounds that it is vague and ambiguous. Applicants further object to this Request on the grounds that it is overly broad, unduly burdensome and not proportional to the needs of this proceeding, including because it requests identification of "all" documents without a reasonable scope limitation. Applicants further object to this Request to the extent it seeks the identification of documents that are accessible to CSXT. Applicants further object to the extent this Request asks Applicants to perform a special study.

Subject to and without waiving the General Objections and the specific objections set forth above, Applicants respond that documents responsive to this Request are contained in the Application and accompanying Workpapers.

In further response to additional inquiries pursuant to the parties' meet and confer discussions regarding this Request, Applicants provide this narrative response. CSXT requested in meet and confer discussions that Applicants provide a narrative response regarding the competitively significant elements Dr. Majure considered in making the assertions CSXT states he made in this Request.

As Dr. Majure explained at his deposition on February 7, 2022, the conditions that would raise concern about possible foreclosure are not evident in a combination of CP with KCS.

Without foreclosing Applicants' ability to provide any further explanation if needed, those conditions may be summarized as follows:

1) a pre-existing constraint that can be shown to limit the feasibility of arrangements CP and/or KCS could have, as separate entities, to align their respective incentives and abilities in a fashion that would lessen competition;

2) a credible mechanism by which the combination of CP and KCS makes the constraint no longer bind (i.e., a demonstration that some theretofore unexploited potential to impair competition could be realized); and

3) an assessment of the overall costs and benefits of engaging in such a strategy relative to other possibilities available to the combined firm which may be mutually inconsistent with such a strategy.

In contrast, Dr. Majure identified constraints on greater efficiency and competitiveness of CP/KCS options that would be relieved by the CP/KCS combination, which would allow the combined firm to pursue procompetitive strategies—specifically, the difficulties discussed in Mr. Brooks' Verified Statement that have kept CP and KCS, as separate companies, from achieving services via interchange that are equivalent to single-line service. By shifting the set of achievable outcomes, this pro-competitive opportunity for the combined firm, and the lack of any anti-competitive potential, makes their choice of profit-maximizing strategy after their combination likely to be one that is procompetitive as Dr. Majure concludes.

Interrogatory No. 28:

Identify all Analyses or other Documents You contend support the claim that "a combined CP/KCS will have incentives and ability to compete more effectively, rather than an incentive to impair competitors" on routes originating or terminating in Mexico. *See* Majure V.S. ¶ 35.

EXHIBIT 13

[REDACTED]

EXHIBIT 14

[REDACTED]

EXHIBIT 15

[REDACTED]

EXHIBIT 16

[REDACTED]

EXHIBIT 17

[REDACTED]

EXHIBIT 18

[REDACTED]

EXHIBIT 19

BEFORE THE
SURFACE TRANSPORTATION BOARD

FINANCE DOCKET No. 36500

CANADIAN PACIFIC RAILWAY LIMITED; CANADIAN PACIFIC RAILWAY COMPANY; SOO LINE RAILROAD COMPANY; CENTRAL MAINE & QUEBEC RAILWAY US INC.; DAKOTA, MINNESOTA & EASTERN RAILROAD CORPORATION; AND DELAWARE & HUDSON RAILWAY COMPANY, INC. CANADIAN PACIFIC RAILWAY LIMITED, ET AL.

– CONTROL –

KANSAS CITY SOUTHERN; THE KANSAS CITY SOUTHERN RAILWAY COMPANY; GATEWAY EASTERN RAILWAY COMPANY; AND THE TEXAS MEXICAN RAILWAY COMPANY

APPLICANTS' REPLY TO UNION PACIFIC RAILROAD COMPANY'S MOTION TO COMPEL

William A. Mullins
Erin A. Glavich
BAKER & MILLER PLLC
2401 Pennsylvania Ave., N.W.
Suite 300
Washington, DC 20037
Telephone: (202) 663-7820
Facsimile: (202) 663-7849

Adam J. Godderz
THE KANSAS CITY SOUTHERN RAILWAY COMPANY
P.O. Box 219335
Kansas City, MO 64121-9335
Telephone: (816) 983-1360
Facsimile: (816) 983-1227

Counsel for KCS

David L. Meyer
Law Office of David L. Meyer
1105 S Street NW
Washington, D.C. 20009
Email: David@MeyerLawDC.com
Telephone: (202) 294-1399

Adam S. Paris
Sullivan & Cromwell LLP
1888 Century Park East
Los Angeles, CA 90067-1725
Email: parisa@sullcrom.com
Telephone: (310) 712-6663

Sophia A. Vandergrift
Sullivan & Cromwell LLP
1700 New York Avenue, N.W., Suite 700
Washington, D.C. 20006-5215
Email: vandergrifts@sullcrom.com
Telephone: (202) 956-7625

Jeffrey J. Ellis
Canadian Pacific
7550 Ogden Dale Road S.E.
Calgary, AB T2C 4X9 Canada
Email: Jeff_Ellis@cpr.ca
Telephone: (888) 333-6370
Counsel for CP

BEFORE THE
SURFACE TRANSPORTATION BOARD

FINANCE DOCKET No. 36500

CANADIAN PACIFIC RAILWAY LIMITED; CANADIAN PACIFIC RAILWAY COMPANY; SOO LINE RAILROAD COMPANY; CENTRAL MAINE & QUEBEC RAILWAY US INC.; DAKOTA, MINNESOTA & EASTERN RAILROAD CORPORATION; AND DELAWARE & HUDSON RAILWAY COMPANY, INC. CANADIAN PACIFIC RAILWAY LIMITED, ET AL.

– CONTROL –

KANSAS CITY SOUTHERN; THE KANSAS CITY SOUTHERN RAILWAY COMPANY; GATEWAY EASTERN RAILWAY COMPANY; AND THE TEXAS MEXICAN RAILWAY COMPANY

APPLICANTS' REPLY TO UNION PACIFIC RAILROAD COMPANY'S MOTION TO COMPEL

Canadian Pacific[1] and Kansas City Southern[2] (the "Applicants") file the following Reply to Union Pacific Railroad Company ("UP")'s Motion to Compel (UP-8), served on Applicants on January 27, 2022 (the "Motion to Compel" or "Motion").

[1] Canadian Pacific Railway Limited, Canadian Pacific Railway Company, and their U.S. rail carrier subsidiaries Soo Line Railroad Company, Central Maine & Quebec Railway US Inc., Dakota, Minnesota & Eastern Railroad Corporation, and Delaware and Hudson Railway Company, Inc. (collectively, "CP").

[2] Kansas City Southern, the Kansas City Southern Railway Company ("KCSR"), Gateway Eastern Railway Company, and The Texas Mexican Railway Company (collectively, "KCS"). KCS also has a subsidiary in Mexico, Kansas City Southern de Mexico ("KCSM"). KCSM is not an applicant in this proceeding. The Board does not have jurisdiction over KCSM as it operates in Mexico. KCSM provides rail service in Mexico pursuant to a Concession granted by the Mexican government. However, for purposes of this motion, KCS includes KCSM.

INTRODUCTION

UP issued three discovery requests seeking communications between KCS and KCSM concerning rates for cross-border traffic via the Laredo gateway. UP confirmed that the purpose of its discovery requests is to understand how KCS prices the Mexico-leg of cross-border traffic. *See* Mot.'s Ex. C, at 2-3 ("The issue that UP sought to address with its discovery requests [Nos. 94, 95, and 96 is]: how does KCS/KCSM price single-line movements and the rates it offers for interline movements when it is competing with UP for business moving between Mexican points and points in the U.S. served by KCS."); *see also* Mot. at 4 ("UP therefore propounded document requests designed to examine directly KCS's rate-setting practices when KCS presently has incentives to foreclose competition.").

To that end, KCS produced documents which demonstrate how KCS/KCSM sets prices, including documents which discuss KCS's policies, procedures, and compliance program. KCS also produced documents which provide further detail regarding KCS's high level pricing strategy and considerations for certain opportunities. In response to KCS's production of its pricing policy, UP issued 30 new discovery requests on January 26, demanding a five-day turnaround. Without waiting for this discovery, UP filed this Motion to Compel on January 27, 2022. Counsel for KCS asked UP to review the new discovery, as it would directly address how KCS prices. *See* Exhibit A. UP refused to withdraw its Motion, again claiming that the purpose of the discovery was to understand "how KCS actually prices its single-line service and KCSM's interchange services where UP and KCS compete for business originating and terminating in Mexico." *Id.* Applicants responded to the 30 requests within five days, on January 31, 2022, and produced related documents the following day. UP did not supplement or amend its Motion to inform the Court that it received additional information. To date, KCS has produced:

KCS's pricing policy documents, which explain the policy underlying rates for Mexico-based movements, including procedures and specific factors KCS considers when making pricing decisions, Mexican regulations that may impact prices, and KCS's compliance program. These documents show how KCS determines rates for KCSM-carried traffic in Mexico, irrespective of the interline partner.

Rates justifications considered for rate differentiation made under the pricing policy.

Results of KCS's compliance program under the pricing policy.

Reports from KCS's "Pricing Review Board," which provide snapshots of considerations for specific bid opportunities between 2018 and 2021 and give insight to high-level strategy considerations for making rate offers. KCS produced the Pricing Review Board reports for certain commodity groups UP specifically requested such as grain, automotive, chemicals, and petroleum.

Long-range planning documents, which include specific opportunities, general considerations, and pricing strategy.

Additionally, KCS:

Responded to 30 discovery requests, on an expedited five-day turnaround, explaining in detail how the KCS Mexico-leg pricing policies worked. Multiple times, KCS explained that KCS has not, does not, and cannot discriminate in Mexico-leg rates regardless of whether UP or KCSR is the interline partner.

Explained how revenue and pricing was determined generally, including the underlying factors typically considered such as market conditions, operating and

cost considerations, types of service, volume, risk premiums, and asset availability, and explained that divisions between KCSR and KCSM were established for similar considerations such as mileage divisions, operating cost considerations, base costs (such as higher fuel costs in Mexico), and regulatory requirements.

Explained the meaning of "commercially reasonable" as used by Applicants in response to a number discovery requests as well as in the Application itself. *See, e.g.*, Ex. B, Applicants' Joint Responses and Objections to UP's First Set of Discovery, Nos. 61, 62, 65.

With substantial discovery responding to UP's requests, UP changed tacks, arguing it is entitled to broad discovery of thousands of KCS's day-to-day business documents in order to confirm KCS's past compliance in pricing with its obligations under the Board's 2004 "Tex Mex" Decision.[3] This broad discovery seeks information not on "how" KCSR/KCSM prices generally, but to confirm rate offers on an individual, customer-by-customer basis, including all potential discussions concerning possible rates or negotiating tactics for multiple commodities, routes, and possibilities, and for several years. *See* Mot. at 9 (a policy "is no substitute for discovery designed to explore whether the policy is being followed. UP's discovery requests are aimed at obtaining exactly that type of information.")(emphasis added).

Board precedent is very clear that, "discovery requests must be narrowly drawn, directed toward a relevant issue, and not used for a general fishing expedition." *Duke Energy Corp.* v. *Norfolk So. Rwy. Co.*, 2002 WL 1730020, at *3 (S.T.B., July 26, 2002). UP's requests are not

[3] *Kansas City Southern – Control – The Kansas City Southern Railway Co., et al.,* at *16-19. STB Fin. Docket 34342, Decision No. 12(served Nov. 29, 2004)("Tex Mex Decision")

reasonable, narrowly drawn, and are not directed to a relevant issue, and thus do not meet this well-established standard. To satisfy such broad requests, KCS would potentially have to search many thousands of documents, including years' worth of day-to-day email communications. Using search terms and a limited commodities list does not reduce the burden that UP seeks to impose. As KCS explained to UP, rates are developed over time on an individual customer basis. KCS would have to conduct a special study just to know for which customers, and for which lanes KCS competes with UP.

Concerns regarding a special study aside, the requests demand significant resources even using search terms. KCS ran a number of searches for UP and BNSF (which, in some of its requests, sought similar information). BNSF at least limited its requested searches to specific commodity products, and yet still the average terms yielded over 20,000 results per year. UP does not address the inherent overbreadth of requests that demand review of five years' worth of day-to-day communications. UP acknowledges in its Motion that its response has been to try different terms.

These discovery requests impose significant burden for little, if any, probative value. UP would have to reverse engineer each rate discussion on a granular, individual bid basis, with likely only pieces of each puzzle available. The value of any "example" would be questionable at best and likely subject to a distracting and expensive sideshow. For these reasons, the Court should deny UP's Motion to Compel.

ARGUMENT

I. Because UP made improper assumptions about how KCS prices, its overly broad requests target the wrong information.

KCSM was granted a Concession by the Mexican government to provide exclusive rail service from the Laredo gateway into Mexico. If a U.S. carrier wants to participate in a

movement of traffic via the Laredo gateway, KCSM provides the Mexico-leg portion of the movement. Shippers have various choices of rail carriers for the U.S.-portion of the movement, depending on where the shipment is going. When quoting a rate for a movement that starts (or ends) in Mexico, KCSM provides the rate for the Mexico side and other U.S. carriers, such as UP and KCSR, provide the rate for the U.S. side.

This is the impetus for UP's discovery. UP contends that KCS's (and post-merger, CPKC's) control over KCSM pricing will provide KCS (or CPKC) with the ability to increase "the rate KCSM quotes for interline service with UP, so that a KCSM-UP option will no longer be a viable alternative for customers." Mot. at 3.[4] UP propounded discovery "to examine directly KCS's rate-setting practices when KCS presently has incentives to foreclose competition." Mot. at 4. The substance of UP's requests seeks KCS to "produce all documents the reflect communications between KCS and KCSM regarding rates (for KCS, KCSM, and UP) for traffic to be handled by UP via the Laredo gateway." *See* Mot. at 5.

UP propounded requests seeking communications between KCS and KCSM because it thought that KCSM and KCS operated separate pricing groups that developed rates between the two. Mot. at 5 ("Through these requests UP sought to obtain internal communications that would reveal KCS and KCSM pricing strategies where KCS competes with UP in the United States for business originated or terminated by KCSM in Mexico."). However, as was explained to UP in the meet and confer process on these requests, KCS has one core pricing team for both

[4] UP seems to argue that the discovery is aimed at confirming if KCS has manipulated KCSM rates in the past (Mot. at 4) while at the same time saying that KCS currently must cooperate with UP, and that the real threat is the merger and the future CPKC (Mot. at 3). Since UP is admitting that KCS currently cooperates with UP and provides commercially reasonable rates, then discovery of KCS's past rate discussions is pointless.

U.S. and Mexico. Communications between KCS and KCSM are not dispositive to understanding KCS pricing strategy.

Once KCS understood through meet-and-confers with counsel what information UP was interested in understanding, KCS produced pricing strategy reports and its pricing policy. These documents show KCS's pricing strategy considerations and how KCS prices the Mexico-leg of cross-border rates. Pursuant to UP's additional January 26 discovery requests, KCS produced, on an expedited five-day turnaround, substantial information on KCS's pricing practices for the Mexico-leg rates. UP (along with all other interested parties) is now in possession of KCS's pricing policy; 30 interrogatory responses that provide detailed information on how KCS's policies, procedures, and compliance program work; and information that demonstrates that KCS cannot discriminate Mexico-leg rates based on the interline partner. *See* Mot. at 3.

II. Because UP's discovery requests would require a special study and impose an obligation to conduct an unreasonable search, the requests impose undue burden on KCS that search terms cannot address.

UP originally stated that it issued these requests to understand KCS's pricing strategies for cross-border traffic via the Laredo gateway. *See* Mot. at 5. If this were all that was sought, then the above-enumerated discovery KCS produced would respond fully to these requests.

UP continues to seek this discovery, however, which indicates it is interested in more than simply "how" KCS prices. UP argues it is its right, and within the scope of proper discovery in this proceeding, to confirm the "commercial reasonableness" of every individual, customer-by-customer, rate offer made over the last five to 18 years. *See* Mot. at 9.

This far exceeds the bounds of appropriate discovery. UP's discovery seeks review of all of KCS's rate development documents for the past five to 18 years.[5] KCS explained to UP that its rates are developed over time, through an iterative process and on a granular level, by customer and by lane. Putting aside the effort involved to search for all responsive documents, and assuming KCS had a 100% return rate, KCS would have to produce thousands of documents. This is not a multi-year DOJ litigation, but a tightly scheduled regulatory proceeding.

The burden on KCS of searching for responsive documents to these requests is enormous. KCS does not track rate development by who the competitor may be. In order even to identify which documents are relevant, KCS would have to undertake a significant special study to figure out which customers and which lanes compete with UP—for every commodity. UP's Motion does not address the fact that its requests require a special study. *See* Mot. at 8.

The use of search terms does little to mitigate the undue and unreasonable burden placed on Applicants as a result of these requests. During the parties' December 1, 2021 meet and confer, UP suggested it would provide five commodities to limit searches, and KCS agreed that, if the searches were reasonable, it would produce responsive documents. UP waited three weeks—until mid-day on Friday, December 24, Christmas Eve—to identify its five commodities. *See* Mot.'s Ex. C at 16. KCS undertook further investigation of how to conduct searches and determined that, even with limited commodities and running searches, the results would be too burdensome. *See* Mot.'s Ex. C at 15. As KCS explained in its response on January

[5] UP originally sought documents for an 18-year period, from 2004 to present. Due to KCS's document retention policy, KCS informed UP during the first meet and confer that documents going back 18 years likely didn't exist, but that documents from around 2016 to present may exist.

5, 2022, the searches would return customer-by-customer granular discussions, unnecessary for the proceeding. Mot.'s Ex. C at 14-15. Attempts to explain why were met with UP's insistence to try terms. *See, e.g.*, Mot.'s Ex. C at 5-6, 8-9, 12. When KCS tried running terms with no success, UP's only response was to try more search terms.[6] *Id.*

As KCS explained, the requests misunderstand KCS pricing and the commodities are large; therefore, without a special study to know which customers and times period are at issue, search terms have to be broad:

> UP and competition with UP is not dispositive. Individual customers, individual lanes are. We ran your proposed search strings just as you suggested in order to try to narrow the request. 206 documents came back and that is with the fact that the search picks up iterations of "up" (such as duplicate, supposition, update, and up). Not a single document was responsive. Not one document had "KCSM-KCS" or "KCSM-UP." The vast majority of documents had nothing to do with pricing or rates. Not one document discussed UP, let alone in terms of lanes or rates or competition.
>
> This is why KCS originally ran just the commodities as terms when trying to determine the scope of a reasonable search. Benzene, the narrowest commodity you asked for, returned 13,000 documents for one year. There is no clear way to distinguish between rate discussions that are relevant [meaning a customer or lane in which UP or BNSF competes with KCS] and just any rate discussion without reading the document and knowing beforehand that UP and KCS compete for it.

See Mot.'s Ex. C at 1-2. UP's response was to file this Motion to Compel, which reneges on UP's agreement to limit commodities and now seeks an order compelling KCS to produce documents on <u>all</u> commodities. Mot. at 9. This request exponentially expands the burden.

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[6] It should be noted that while BNSF is seeking similarly broad discovery, BNSF agreed to and identified narrow searches on specific products (*e.g.*, "refrigerator" or "humidifier" or specific product ID codes). Yet even these, more limited search strings returned an unreasonable amount of hits. The string (("UP" OR "Union Pacific" OR "BNSF") AND KCSM) AND ("Ojo Seco" AND ("3632112" OR refrigerator)) returned <u>25,815 hits</u> for the year 2019 alone.

Nothing in UP's motion indicates why UP would need all commodities when it believed five was sufficient. UP's request is purely punitive. For this reason alone, UP's motion should be denied.

Discovery is broad, but it is not unlimited. Various principles provide discovery parameters, including undue burden or expense. 49 C.F.R. § 1114.21(c); *see also Tongue River Railroad Co., Inc.—Rail Construction & Operation—In Custer, Powder River & Rosebud Counties, Mont.*, 2014 WL 4457251, at *3 ("[D]iscovery may be denied if it would be unduly burdensome in relation to the likely value of the information sought."); *Canadian Pacific Railway Company—Control—Dakota, Minnesota & E. Railroad Corp.*, Finance Docket No. 35081 (STB Decision No. 8 served Mar. 27, 2008) ("CP/DME Dec. No. 8") at 4-5 (denying discovery where the request is so broad as to require review of all of the party's documents related to grain in order to determine if relevant documents exist.). UP seeks documents that represent, at a minimum, five years of KCS's ratemaking business. Search terms cannot overcome the foundational problems that such requests require a special study to make search terms viable.

III. The discovery sought by UP lacks probative value.

In 2004, the Board imposed a condition on KCS that it keep the Laredo gateway open on "commercially reasonable" terms as part of its approval of KCS's acquisition of the Texas Mexican Railway Company. *See* Tex Mex Decision at *16-19. The Board rejected UP's efforts at that time to impose stricter, more concrete conditions. *Id.* As UP indicated, "[t]he Board has said, for example, that party seeking conditions involving more than a promise of 'commercially reasonable rates' must 'rebut' the presumption that 'end-to-end' mergers – combinations of railroads that connect only a single point – will not affect consumers adversely." Mot. at 4. But the evidence is not aligned with UP's goals. Shippers who believed that KCS has attempted to

close the Laredo gateway, or offer non-commercially reasonable rates, had a number of avenues to complain, including to the Board. None have, ever. Applicants responded to numerous discovery requests aimed at "commercially reasonable" terms, and KCS confirmed that not a single shipper has complained they were not offered "commercially reasonable" terms. *See, e.g.*, Ex. B, Applicants' Joint Responses and Objections to UP's First Set of Discovery, Nos. 61, 62, 65 & 79. As nothing supports UP's efforts, the only remaining option is to fish through the KCS's rate discussion documents to try to engineer an example of KCS offering a "non-commercially reasonable" term.

Even if relitigating the 2004 acquisition were relevant (which it is not), if KCS is compelled to comply with these burdensome discovery requests, the results have little, if any, probative value. Assuming KCS performed a special study to determine which customers and lanes were responsive, a search would produce only pieces of rate discussions. Assuming UP could piece something together, it would then have to figure out whether that discussion is "commercially reasonable." The Board did not define "commercially reasonable" in its 2004 Tex Mex decision. *See* Tex Mex Decision at 19. There are no set metrics; there are no dollar caps. There is no ruler by which UP could even determine, at this later date and with full hindsight, whether a particular rate offered for one customer in 2019 for intermodal traffic between Mexico City and Kansas City is "commercially reasonable" without wild speculation. There is little benefit to such an exercise for this proceeding, and the *de minimus* value does not outweigh the burden on KCS to produce the documents that would be required to undertake it. *See Tongue River*, 2014 WL 4457251, at *3 ("[D]iscovery may be denied if it would be unduly burdensome in relation to the likely value of the information sought.").

CONCLUSION

Discovery in this matter must be appropriately limited to the impacts of the proposed merger, and whether CP's acquisition of KCS causes competitive harm or changes KCS's incentives. Applicants have produced significant volumes of information. Applicants have worked diligently and in good faith—spending an enormous amount of management and attorney time, money, and resources—in order to collect, review, and produce responsive documents. To date, Applicants have made 11 productions, culminating in a production of an additional 3,257 responsive documents, totaling more than 36,000 pages, as well as numerous narrative interrogatory responses and a number of informal, expedited discovery requests.

UP asked for and received discovery on how KCS prices the Mexico-leg of movements on which UP competes with KCS for cross-border traffic. Applicants have responded to interrogatories on pricing and "commercially reasonable" terms. To the extent UP argues that KCS's past pricing is relevant, UP has a multitude of methods to test its theory: KCS's pricing policies from 2015 to present; rate justification examples (setting out how and why rates differ); compliance program review results; a number of interrogatories relating to "commercially reasonable" terms; KCS's waybill data demonstrating the actual rates offered and accepted; and pricing strategy documents. All of this material has been produced and is in UP's possession.

The efforts required to review and produce five years' worth of email communications detailing customer-by-customer discussions is not justified. This is not an oversight case. There is no active complaint about KCS's compliance. No shipper or railroad received a "non-commercially reasonable" rate or ever complained to the Board about KCS pricing. Because the discovery sought by UP is unnecessary and burdensome, Your Honor should deny UP's Motion to Compel.

Respectfully submitted,

Dated: February 7, 2022

/s/ William A. Mullins

William A. Mullins
Erin A. Glavich
BAKER & MILLER PLLC
2401 Pennsylvania Ave., N.W.
Suite 300
Washington, DC 20037
Telephone: (202) 663-7820
Facsimile: (202) 663-7849

Adam J. Godderz
THE KANSAS CITY SOUTHERN RAILWAY COMPANY
P.O. Box 219335
Kansas City, MO 64121-9335
Telephone: (816) 983-1360
Facsimile: (816) 983-1227

Counsel for KCS

/s/ David L. Meyer

David L. Meyer
Law Office of David L. Meyer
1105 S Street NW
Washington, D.C. 20009
Email: David@MeyerLawDC.com
Telephone: (202) 294-1399

Adam S. Paris
Sullivan & Cromwell LLP
1888 Century Park East
Los Angeles, CA 90067-1725
Email: parisa@sullcrom.com
Telephone: (310) 712-6663

Sophia A. Vandergrift
Sullivan & Cromwell LLP
1700 New York Avenue, N.W., Suite 700
Washington, D.C. 20006-5215
Email: vandergrifts@sullcrom.com
Telephone: (202) 956-7625

Jeffrey J. Ellis
Canadian Pacific
7550 Ogden Dale Road S.E.
Calgary, AB T2C 4X9 Canada
Email: Jeff_Ellis@cpr.ca
Telephone: (888) 333-6370

Counsel for CP

CERTIFICATE OF SERVICE

I hereby certify that I have caused the foregoing Applicants' Reply to Union Pacific Railroad Company's Motion to Compel to be served electronically or by first-class mail, postage pre-paid, on all parties of record in these proceedings.

/s/ Julia Adrian
Julia Adrian

February 7, 2022

From: "Rosenthal, Michael" <mrosenthal@cov.com>
To: "WMullins@bakerandmiller.com" <WMullins@bakerandmiller.com>
Cc: David Meyer <David@MeyerLawDC.com>, "eglavich@bakerandmiller.com" <eglavich@bakerandmiller.com>

Date: Friday, January 28, 2022 11:13AM
Subject: RE: FD 36500 - Motion to compel

Bill,

As much as I'd like to find a simple solution, I can't see how the discovery responses would resolve the issues UP is trying to address through the motion to compel. The information UP is seeking through the motion to compel would address how KCS actually prices its single-line service and KCSM's interchange services where UP and KCS compete for business originating and terminating in Mexico. I don't see how an explanation of the policy document could provide equivalent information.

Regards,

Mike

From: WMullins@bakerandmiller.com <WMullins@bakerandmiller.com>
Sent: Friday, January 28, 2022 10:51 AM
To: Rosenthal, Michael <mrosenthal@cov.com>
Cc: David Meyer <David@MeyerLawDC.com>; eglavich@bakerandmiller.com
Subject: Re: FD 36500 - Motion to compel

[EXTERNAL]

Mike

I would like to request that you review our answers to UP's 3rd set of discovery and then let's talk about your motion to compel. I think our answers to your 3rd set should go a long way to show how KCSR and KCSM set prices, the process, and provide you with the background and information that you need. If after you review the answers, we can then talk about your motion to compel.

William ("Bill") A. Mullins
Partner
Baker & Miller PLLC
Suite 300
2401 Pennsylvania Ave, N.W.
Washington, D.C. 20037
(202) 663-7823 (Direct)
(202) 663-7849 (Fax)
The above message may be privileged, confidential and protected from disclosure by attorney/client. work product or other privileges. If you believe that it has been sent to you in error, do not read it. Please reply to the sender that you have received the message in error. Then delete it. Thank you.

-----"Rosenthal, Michael" <mrosenthal@cov.com> wrote: -----

> To: Bill Mullins <wmullins@bakerandmiller.com>, David Meyer <David@MeyerLawDC.com>
> From: "Rosenthal, Michael" <mrosenthal@cov.com>
> Date: 01/27/2022 07:53PM
> Subject: FD 36500 - Motion to compel
>
> David and Bill, I've attached a highly confidential version of a motion to compel that we just filed. The only potentially HC information is in Exhibit C, and it would not be HC as to KCS.
>
> Regards,
>
> Mike

[attachment "UP8_MTC_HC_012722.pdf" removed by William Mullins/bakermiller]

EXHIBIT B

BEFORE THE
SURFACE TRANSPORTATION BOARD

Finance Docket No. 36500

CANADIAN PACIFIC RAILWAY LIMITED, *ET AL.*
– CONTROL –
KANSAS CITY SOUTHERN, *ET AL.*

KANSAS CITY SOUTHERN AND CANADIAN PACIFIC'S JOINT RESPONSES AND OBJECTIONS TO UNION PACIFIC RAILROAD COMPANY'S FIRST SET OF DISCOVERY REQUESTS

Pursuant to 49 C.F.R. Part 1114, Subpart B, Canadian Pacific Railway Limited, Canadian Pacific Railway Company, Soo Line Railroad Company, Central Maine & Quebec Railway US Inc., Dakota, Minnesota & Eastern Railroad Corporation, and Delaware and Hudson Railway Company, Inc. (collectively, "Canadian Pacific" or "CP") and Kansas City Southern, The Kansas City Southern Railway Company, Gateway Eastern Railway Company, and The Texas Mexican Railway Company (collectively, "KCS"; together with CP, the "Applicants") hereby respond and object as follows to Union Pacific Railroad Company's First Set of Discovery Requests to Applicants (the "UP Requests") served on November 8, 2021 in connection with the above-captioned proceeding.

GENERAL OBJECTIONS

The following General Objections apply to each of the UP Requests and shall have the same force and effect as if set forth in full in response to each individually numbered UP Request.

1. Applicants object to the UP Requests and to each Definition, Instruction and Request contained therein to the extent they purport to impose upon the Applicants burdens

information that is substantially old, and information and documents may no longer be available or complete, or difficult to find.

Subject to and without waiving the General Objections and the specific objections set forth above, Applicants will provide non-privileged and non-duplicative documents responsive to this Request that they are able to locate after a reasonable search (to the extent any such documents exist).

Request No. 61:

Describe in detail the meaning of the phrase "commercially reasonable terms" as used on page 17 of the Ottensmeyer VS.

Response to Request No. 61:

In addition to the General Objections set forth above, Applicants object to this Request on the grounds that it is unduly burdensome and not proportional to the needs of this proceeding. Applicants further object to this Request on the grounds that the Application speaks for itself. Applicants further object to this Request to the extent that it improperly calls for legal analysis, arguments or conclusions.

Subject to and without waiving the General Objections and the specific objections set forth above, Applicants respond that the phrase "commercially reasonable terms" as used in this context (Application Vol. 1 at 1-203) refers to the same commitment addressed in Applicants' Response to Request No. 40.

Request No. 62:

Describe in detail how KCS has implemented the condition on the KCS-TM-TFM transaction requiring it to "keep the Laredo gateway open on commercially reasonable terms," as described on page 21 of the Ottensmeyer VS.

Response to Request No. 62:

In addition to the General Objections set forth above, Applicants object to this Request on the grounds that it is overly broad, unduly burdensome, and not proportional to the needs of this proceeding. Applicants further object to this Request to the extent that it improperly calls for a legal analysis, arguments, or conclusions. The KCS-TM-TFM transaction was approved in 2004, almost 17 years ago to the day. The condition that KCS "keep the Laredo gateway open on commercially reasonable terms" has been in place since that time. It is unduly burdensome and not proportional to the needs of this proceeding to describe in detail every interaction that has occurred between KCS and any other party regarding implementation of this condition since 2004. Further, Applicants object to this Request to the extent that it seeks a legal conclusion or legal analysis regarding which terms, or how terms, are "commercially reasonable" or to the extent the Request requires a special study regarding terms implemented since the KCS-Tex Mex-TFM transaction. Applicants further object to the extent this Request seeks confidential and proprietary information that is neither relevant nor proportional to the needs of this proceeding. Applicants further object to this Request to the extent it requires KCS to conduct a special study.

Subject to and without waiving the General Objections and the specific objections set forth above, Applicants incorporate by reference their Response to Request Nos. 40 and 61. Applicants further respond that applying KCS's commitment to "keep the Laredo gateway open on commercially reasonable terms" by its nature calls for flexibility in light of the specific circumstances of any individual shipper's request.

KCS notes that the Board declined in the 2004 proceeding to impose further conditions as proposed by BNSF, UP, other railroads and shippers, and further declined to more

definitively define "commercially reasonable terms." The Board also did not require the NITL Agreement to be imposed as a condition to the merger; allowing that to remain a private agreement between KCS and NITL. The Board held that any competitive concerns regarding the transaction were addressed by holding KCS to its pledges to keep the Laredo gateway open. *See KCS/Tex Mex*, Decision No. 12 at 17 (STB served Nov. 29, 2004).

Further, while KCS made the pledges willingly and voluntarily, parties were not without recourse if KCS failed to abide by its commitments. KCS submitted status reports following the consummation of the transaction to ensure a smooth transition. Parties could have brought issues before the Board in a variety of ways. No party has ever brought either a formal or informal complaint to the Board regarding KCS's implementation of the "Laredo Gateway" condition. The KCS-NITL Agreement provided dispute resolution where terms were unsatisfactory. No shipper since 2004 has raised a dispute under the NITL Agreement. As set forth in Mr. Ottensmeyer's Verified Statement, since the KCS-Tex Mex-TFM transaction, KCS confirms that "there has not been a single complaint from railroads or shippers that KCS and KCSM were foreclosing the Laredo gateway in any way." *See* Ottensmeyer VS at 22 (Application Vol. 1 at 1-208).

Request No. 63:

Identify the "Mexican law" that purportedly "requires KCSM to give a rate to/from the Laredo gateway." *See* Ottensmeyer VS, page 21, footnote 18.

Response to Request No. 63:

In addition to the General Objections set forth above, Applicants object to this Request on the grounds that it is unduly burdensome and not proportional to the needs of this proceeding, including because UP has the same access to "Mexican law" as KCS, all of which is

publicly available. Applicants note that the legal paradigm governing KCSM's predecessor was litigated extensively in the *KCS/Tex Mex* proceeding, in which UP submitted substantial comment and expert analysis of the Mexican law at issue here.

Subject to and without waiving the General Objections and the specific objections set forth above, Applicants respond that the "Mexican law" referred to in the Ottensmeyer V.S. at 21 n.18 (Application Vol. 1 at 1-207) is a shorthand for the body of legal principles applicable to and that interplay with rail rates in Mexico. This includes, without limitation, statutes, regulations, court opinions, decrees, and other official standards. The principal laws related to KCSM's use and enjoyment of the Concession granted it are the Concession Law and Mexican Railway Law and related regulations.

The principal laws related to KCSM's use and enjoyment of the Concession granted it are the Concession Law and the Regulatory Railway Service Law ("LRSF"). The LRSF obligates KCSM to provide public freight rail transportation service ("SPTFC") to all users on a non-discriminatory basis. KCSM also has the obligation to register its maximum freight rates with the Mexico's Railway Transport Regulatory Agency ("ARTF"). These maximum tariff rates are known as "TUCE" rates. KCSM has the right to offer shippers discounts from the TUCE rates. These are known as "Commercial rates." All Commercial rates are to be offered to shippers in a non-discriminatory manner. As a result of the interplay of these laws, if KCSM provides one shipper with a rate from Mexico to the Laredo gateway, it must in general also provide other shippers with a similar rate.

Request No. 64:

Produce all documents studying, analyzing, or discussing the "Mexican law" identified in response to Request No. 63.

Response to Request No. 64:

In addition to the General Objections set forth above, Applicants object to this Request on the grounds that it is overly broad, unduly burdensome, and not proportional to the needs of this proceeding. Applicants further object to this Request to the extent that it seeks documents protected from discovery by the attorney-client privilege, attorney work product doctrine or any other applicable privilege, protection, immunity, law, or rule. This Request is not limited in scope in any manner, either to KCSM, KSC, or in any way as to the operations of a railroad. This Request is not limited in geographic scope nor temporal scope. This Request is overbroad and unduly burdensome to the extent that it seeks documents not relevant or proportional to the needs of this proceeding. Further, this Request clearly seeks documents that are privileged and otherwise protected from disclosure.

Subject to and without waiving the General Objections and the specific objections set forth above, Applicants will provide non-privileged and non-duplicative documents responsive to this Request that they are able to locate after a reasonable search (to the extent any such documents exist).

Request No. 65:

Identify the "remedies" that shippers will purportedly have "to ensure" KCSM provides commercially reasonable rates and terms to/from the Laredo gateway so shippers can "utilize KCSM/UP or KCSM/BNSF routings." *See* Ottensmeyer VS, page 22.

Response to Request No. 65:

In addition to the General Objections set forth above, Applicants object to this Request on the grounds that it is overbroad, unduly burdensome, and not proportional to the

needs of this proceeding. Applicants further object to this Request to the extent that it improperly calls for legal analysis, arguments or conclusions.

Subject to and without waiving the General Objections and the specific objections set forth above, Applicants respond that among the remedies available to shippers to ensure that CPKC keeps the Laredo gateway open on commercially reasonable terms are: (a) enforcement of the agreement entered into between KCS and NITL to do so with respect to traffic affected by the KCS/Tex Mex/TFM transaction, which provides contractual remedies (*see* Verified Statement of John Brooks at 21 (Application Vol. 1 at 1-232)), (b) enforcement of the condition imposed on KCS in the *KCS/Tex Mex* proceeding requiring KCS to honor its commitment to keep the Laredo gateway open on commercially reasonable terms, which provides remedies available to the Board to enforce compliance with this commitment; and (c), as noted in Applicants' response to Request No. 14, enforcement of the condition that Applicants anticipate the Board will impose requiring them to honor the commitment they have made in this proceeding to keep the Laredo gateway open on commercially reasonable terms. In addition, and more fundamentally, Applicants will be disciplined by the marketplace, in the sense that they would face the loss of traffic opportunities to alternative rail routes or other transportation options were they to insist on commercially unreasonable terms or otherwise "close" a gateway that shippers would prefer to use.

Request No. 66:

Produce all documents supporting the statement on page 22 of the Ottensmeyer VS that "if the combined CP/KCS tried to raise rates on KCSM movements that are not rail dependent, the traffic would shift to motor or water carriage."

intended to provide illustrations of the kinds of obstacles referenced in the quoted phrase from Paragraph 33 (*see* Application Vol. 1 at 1-228).

Request No. 78:

Describe the meaning of the phrase "traffic that naturally flowed over our route network," as the phrase is used on page 17 of the Brooks VS.

Response to Request No. 78:

In addition to the General Objections set forth above, Applicants object to this Request on the grounds that it is unduly burdensome and not proportional to the needs of this proceeding. Applicants further object to this Request on the grounds that the Brooks VS speaks for itself.

Subject to and without waiving the General Objections and the specific objections set forth above, Applicants respond that the quoted phrase (Application Vol. 1 at 1-228) refers to traffic that shippers chose to route via CP-KCS interline routes even in the absence of an alignment of economic interests between the two railroads and resulting investments by them in service or rate improvements that would have made CP-KCS interline routes more attractive relative to the alternatives available at the time.

Request No. 79:

Identify any shipper that has inquired about arbitrating a dispute under the agreement between KCS and The National Industrial Transportation League on page 20 of the Brooks VS, and produce all documents regarding any such inquiry.

Response to Request No. 79:

In addition to the General Objections set forth above, Applicants object to this Request on the grounds that it is overly broad, unduly burdensome, and not proportional to the

needs of this proceeding. The KCS-NITL Agreement was entered into in 2004, 17 years ago, and has been in effect since that time. It is unduly burdensome to identify "any shipper" and produce responsive documents regarding a shipper that has only made "inquiry" about the arbitration provisions of the agreement from 2004 to date, nor is such effort proportional to the needs of this proceeding. Applicants further object to this Request to the extent that it seeks confidential and proprietary information that is not relevant to the subject matter of the proceeding.

Subject to and without waiving the General Objections and the specific objections set forth above, Applicants can respond that no shippers have invoked the Agreement's dispute resolution and, based on reasonable inquiry, no shippers have even "inquired" about the Agreement's arbitration remedy in at least the past 13 years.

Request No. 80:

Produce all documents studying, analyzing, or discussing the meaning of the phrase "commercially reasonable rates and terms," as used on page 22 of the Brooks VS.

Response to Request No. 80:

In addition to the General Objections set forth above, Applicants object to this request on the grounds that it is overly broad, unduly burdensome, and not proportional to the needs of this proceeding. Applicants have previously defined "commercially reasonable terms" (Requests No. 40, 61, & 71), and responded to Requests relating to how the conditions and terms requiring "commercially reasonable terms" have been and will be implemented (Requests No. 62 & 65), and incorporate those Responses by reference. Because the application of the "commercially reasonable terms" standard is by its nature flexible, the Request could be read as encompassing nearly every document that "discusses" a rate or term relating to the Laredo

EXHIBIT 20

[REDACTED]