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Congress of the United States
Washington, DC 20515

Surface Transportation Board
395 E Street SW
Washington, DC 20423

Dear Chairman Oberman, Vice Chairman Primus, and Members Fuchs, Schultz, and Hedlund:

I write to ask the Surface Transportation Board (STB) to deny the proposed merger between the Canadian Pacific (CP) and Kansas City Southern (KCS) railroads (Docket No. FD 36500). The proposed merger represents a grave threat to competition in the domestic rail industry, which is already highly consolidated. It would likely lead to job losses, harm to other industries reliant on railroads, and more fragility in American supply chain infrastructure. Under 49 U.S. Code §11324, the Surface Transportation Board may authorize a merger only if the merger is consistent with the public interest. This merger fails that test and must be blocked.

As recently as 1976, 63 Class I railroads served the nation. Today, only seven remain. The largest four firms control at least 83 percent of the freight railroading market, while 78 percent of freight rail stations are captive to a single major railroad, making a critical method of American transportation monopoly dependent.

This was not always the case. From the end of the nineteenth century until 1980, railways were federally regulated and served the public good. Railroads, prohibited from price discriminating against shippers, operated on rail networks that connected the country. After the Staggers Act of 1980 deregulated the industry, an era of consolidation was ushered in, leading to today's highly concentrated market structure. Newly deregulated railroads, rather than continuing to serve as critical infrastructure for the American economy, shuttered unprofitable routes. They negotiated advantageous rates with their biggest shippers, leaving smaller firms out to dry, helping to spark the rise of big-box retail, and facilitating consolidation in adjacent industries. I

The proposed merger between CP and KCS would combine the sixth and seventh largest U.S. railroads by revenue. While CP and KCS connect directly at only one junction (Kansas City, MO), KCS connects with other railroads that compete directly with CP, and vice versa. The proposed transaction would give the merged firm additional leverage over competitors by allowing the merged firm to foreclose competition from other railroads, exert more extensive power over bottlenecks, and threaten the commercial viability of interchange rates. The combined firm would have the ability and a strong incentive to limit interchanges that facilitate alternative Class I carrier routes and instead favor its own long-haul routes. In particular, the merged rail carrier could significantly undermine competition at a critical international junction in Laredo, Texas, the gateway for 54% of all US-Mexico rail traffic. This reduction in competition would harm many shippers that lack viable alternatives to transnational rail service via Laredo.

CP and KCS argue that since the proposed transaction is an end-to-end merger (one between two railroads competing in different service areas with little direct competition), a merger should not raise concerns about competition. However, end-to-end mergers provide railroads with an extensive menu of options to limit competition, from denials of service to competitors who need track or facility access to the cancellation of reciprocal switching agreements and closure of critical gateways. In addition to these harms to competition, these mergers also threaten shippers, essential services, and rail network reliability. The STB's own guidelines specifically state that end-to-end mergers can degrade railroad competition, and that "any railroad combination" risks the merged carrier exploiting its increased market power.

Effects of Railroad Concentration on Shippers, Markets, and Industries

Concerns about the proposed CP-KCS merger have been thoroughly documented by rail-reliant American businesses both large and small. While each of the five other Class I railroad competitors outlined this merger's anticompetitive nature in comments to the STB, long-standing concerns regarding railroad consolidation's general adverse effects on smaller and independent shippers have been well documented long before the proposed merger.

Shippers have outlined the painful effects of such practices, having long complained that railroads' outsized market power allows them to exploit their customers. When it comes to rates themselves, shippers are at the mercy of dominant railroads. Dominant railroads increasingly alter service agreements, adding junk fees ("demurrage" and "accessorial" charges) while limiting service, including restricting car supply, shrinking loading windows, and throttling shipment sizes.

Unchecked market power has also increased the potential for railroads to collude by lowering their barriers to doing so. The STB itself has acknowledged that consolidation has "created the potential for monopolistic pricing" – in the past year alone, shippers have filed hundreds of lawsuits alleging price fixing by four of the seven Class I railroads.

The harms of railroad concentration can be regionally acute. Due to the geographically limited nature of the production of specific commodities (soda ash and phosphate, for example), railroads with control over those geographic routes exert considerable market power over shippers of key commodities that may themselves play outsized roles in particular industries. Farmers in landlocked states such as Montana and the Dakotas, who are reliant on a single railroad monopoly, are forced to pay twice the rate of those in more competitive rail serviced regions. Rail consolidation also affects large-scale entities, including enormous multinational food conglomerates. In an STB comment, U.S. food and beverage giants, represented by a trade association representing PepsiCo, Kraft Heinz, General Mills, and the Kellogg Company as members, highlighted the adverse impacts of rail consolidation and protested corporations' captive status in many locations, outlining how further consolidation of the rail industry will only worsen their vulnerable position in rail shipping. The irony of market giants like Pepsi and General Mills, who in most other contexts wield significant leverage, complaining that other corporations have too much power over them should indicate the severity of this issue, and the leverage provided by a consolidated railroad system.

Effects on Service and Supply-Chain Disruptions

Railroad mergers lead to service disruptions and cause harm to both shippers and consumers. A 2015 study by the Transportation Research Board illustrated an array of service disruptions caused by numerous railroad mergers. In a comment to the STB on the proposed transaction, the United States Department of Agriculture highlighted the merger between Union Pacific and Southern Pacific Railroad, which caused "extraordinary" service delays that spread from terminals to a whole-of-network crisis. USDA warned of the proposed transaction's potential for service disruptions, identifying "significant" concerns with both temporary issues and permanent impacts brought on by increased volumes in past mergers. Service disruptions have become more regular as railroads have used their market power as a shield to pursue Precision Scheduled Railroading (PSR) schemes – a Wall-Street fueled profit-maximization plan focused on driving down a railroad's "operating ratio," (operating expenses as a percentage of revenue) – at the expense of capacity, service, and safety.

While proponents argue that PSR schemes promote efficiency, the drawbacks are clear. In a competitive market, railroads might take advantage of increased efficiency to invest in capacity, outcompeting rivals by lowering rates, or raising worker wages. In an uncompetitive market, railroads can cut costs by eliminating jobs and capacity, suffering few consequences – the "do less with less" approach.

PSR has led to increases in train length, maintenance delays, and safety concerns, contributing both to record railroad profits and today's supply chain crisis. In a September 2021 speech, STB Chairman Martin Oberman estimated that U.S. railroads have paid out $196 billion in stock buybacks or dividends to shareholders since 2010 – tens of billions more than they spent on physical rail and equipment they need to run their railroad. More consolidation will only further insulate railroads from competition and leave workers, businesses, and supply chains in an increasingly precarious position.

While the merging firms claim the transaction's end-to-end nature limits potential for service disruptions, the deal's proposed traffic patterns show the merged firm would push more volume through already-congested areas to cut costs at the expense of supply chain resiliency. Multiple Class I railroad competitors have noted that a proposed doubling of KCS traffic levels would threaten already-fragile Houston terminal facilities, which are themselves already falling victim to severe service disruptions after the Union Pacific-Southern Pacific merger.

Effects on Employment

In recent years, Class I railroad employment has plummeted to record low levels, in large part due to rail consolidation and subsequent PSR schemes. From 1980 to 2015, railroad jobs plummeted from 540,000 to 210,000 – a drop of more than 60%. Since 2015, railroads have cut a further 66,000 jobs – even as railroads generated more operating profit than any year since 1990. A Bureau of Labor Statistics analysis acknowledged PSR as the most widely accredited reason for the decrease in rail transportation employment. In 2019 alone, more than 20,000 rail workers lost their jobs in large part due to PSR schemes – leading one long-tenured rail worker to describe his job as "a funeral home."

Besides helping to cripple industry capacity and destroying the livelihoods of hundreds of thousands of American workers, the outsized market power of dominant Class I railroads also disadvantages those still employed by the industry. Railroad mergers leave rail workers fewer and more powerful employers with which to bargain. This year, more than 3,000 CP conductors, engineers and train and yard personnel voted for a strike over inadequate salary, benefits, and pensions. In response, CP physically locked employees out of facilities, publicly stating its refusal to accept a request for higher pension caps and initiating a multi-day work stoppage. Businesses reliant on CP for shipping service were forced to watch as already-fragile supply chains were further disrupted by corporate anti-labor action. To further illustrate the anti-labor behavior of major railroads, this year BNSF went to federal court to obtain a restraining order that would prevent its union employees from striking in anticipation of a widely criticized and draconian new labor policy.

The proposed merger would also specifically harm the workers of Minnesota's Twin Cities, where CP currently maintains its headquarters. As part of the merger, CP has already announced that Minneapolis will not remain as the company's headquarters. The Minnesota Post warned that CP may "end up pocketing the 'easy' post-merger overhead and admin savings," leaving Minnesota stakeholders with "little to no restitution" – an all too familiar story when it comes to corporate mergers.

The proposed transaction also spells disaster for Americans living in the areas that would see vastly increased rail volume as a result. Eight Illinois towns representing 325,000 Americans located along the segment of the Elgin Subdivision – a Chicago commuter rail line utilized for freight by CP – have submitted comments to the STB highlighting the consequences of the near-tripling of rail traffic proposed in the region and strongly urging the transaction to be blocked. The towns investigated the costs required to mitigate the harms to their communities from the transaction, finding that the total represents $9.5 billion and as such will "dwarf any potential benefits to the merged railroad, the Coalition communities, or the Nation at large."

The Merger's Use of a Voting Trust

In order to blunt antitrust enforcement and save money on risk mitigation related transaction costs, the merging firms have chosen a particularly anticompetitive deal structure: a voting trust. Voting trusts allow shareholders of a merging firm to transfer control of their stock to leadership of the acquiring firm, bringing two competing firms under unified ownership. Whether in a horizontal (parallel) or vertical (end-to-end) merger, such a structure immediately provides clear incentives against competition, even if management remains separate – especially since firms can be incentivized to compete less aggressively against a firm in which they possess an ownership stake. The use of voting trusts in mergers was originally invented by Standard Oil over a century ago in the gilded age. Their novel use facilitated numerous illegal horizontal acquisitions and underpinned Standard Oil's quest to monopolize the oil industry. In this case, the use of a voting trust represents no less clear of an attempt to circumvent the STB's authority and has in effect consummated the transaction before the Board can review how the deal will harm competition.

The merging firms' usage of a voting trust in this transaction has also degraded the integrity of the review process. In a comment to the STB, the U.S. Department of Justice highlighted the brazenness of the merger's mechanics, criticizing the firms' use of a voting trust to consummate the deal before regulatory review and emphasizing its long-held position that the regulators' approval of voting trusts contradicts sound competition policy and undermines the STB's ability to maintain and restore competition, even if the deal is ultimately rejected.

The STB's own position on voting trusts in rail mergers is that their use should be reserved "only for those rare occasions when their use would be beneficial" to the public interest. In this case, usage of a voting trust directly contradicts the public interest, serving only the interest of the merging firms – who benefit from avoiding breakup fees, interim operating covenants, material adverse effect provisions, and other commonly used alternative risk-related negotiated stipulations that would raise deal costs. As pointed out by the DOJ, each firm voluntarily assumed the risks associated with the regulatory review of the proposed transaction. The use of a deal structure that may cause anticompetitive effects—even before the deal is formally approved—should not be permitted simply because it will save the merging firms on transaction costs.

Conclusion

Lack of competition has allowed railroads to gut capacity, capture and extort businesses, fire thousands of workers, and threaten the integrity of America's freight transport network and supply chains – all while extracting monopoly profits. While rail consolidation is lucrative for executives, financiers, and shareholders, its consequences are felt and borne by American businesses, workers, supply chains, and the U.S. economy at large. In a critical industry with significant barriers to entry (due to the high capital costs of establishing new railroads), preserving what little competition remains is of paramount importance to the integrity of the U.S. economy.

The merging firms' proposed transaction – the first Class I railroad merger in 20 years – would further reduce the number of major railroads from seven to six. This transaction would enrich the merging firms and their bankers, lawyers, and shareholders – at the expense of the public and the U.S economy. Handing dominant rail corporations more pricing power to wield against American workers and businesses during a time of high inflation will only hurt everyday Americans. More corporate consolidation of critical infrastructure during a supply chain crisis will exacerbate service disruptions, increase dominant railroads' pricing power, and enable anti- competitive corporate behavior.

By statute, the STB may authorize a merger only when it finds the transaction is consistent with the public interest. This merger must be denied.

Very truly yours,

Katie Porter

Representative Katie Porter