

Docket # F.D. 30400-10/3/84 - PGS. -547 - 605

C O N T E N T S

<u>WITNESS</u>	<u>DIRECT</u>	<u>CROSS</u>	<u>REDIRECT</u>	<u>RECROSS</u>
Denman K. McNear				
By Mr. Raker		557		
By Mr. Prettyman		516		
By Mr. Craig		644		
By Mr. Delaney		645		
By Mr. Robert		656		
By Mr. Ratner		664		
By Mr. MacKenzie		684		
Bruce G. McPhee				
By Mr. Stephenson	699			
By Mr. Mayo		700		

E X H I B I T S

<u>Exhibit No.</u>	<u>IDENTIFIED</u>	<u>RECEIVED</u>
KCS-C-3	562	697
KCS-C-4	563	697
KSC-C-5	563	697
KSC-C-6	564	697
KCS-C-7	564	697
KCS-C-8	570	697
KCS-C-9	592	697
DRGW-C-2	621	698
DRGW-C-3	623	698
DRGW-C-4	710	
DRGW-C-5	727	

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BEFORE THE  
INTERSTATE COMMERCE COMMISSION

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In the Matter of: ;  
SANTA FE SOUTHERN PACIFIC CORPORATION : Finance Docket  
-- CONTROL -- : 30400 et al.  
SOUTHERN PACIFIC TRANSPORTATION :  
COMPANY ;  
----- x

Hearing Room A  
12th & Constitution, N.W.  
Washington, D.C.  
Wednesday, October 3, 1984

The hearing in the above-entitled matter was  
convened, pursuant to notice, at 9:30 a.m.

BEFORE:

JAMES E. HOPKINS,  
Administrative Law Judge

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## P R O C E E D I N G S

(9:30 a.m.)

JUDGE HOPKINS: Let's get back on the record.  
Mr. Baker?

Whereupon,

DENMAN K. McNEAR,

the witness on the stand at the time of recess, resumed  
the stand and, having been previously duly sworn, was  
examined and testified further as follows:

## CROSS EXAMINATION

BY MR. BAKER:

Q Mr. McNear, as president and chairman of  
Southern Pacific, could you briefly characterize your  
role in the formulation of SP's case in this  
proceeding?

A In our application?

Q Yes, sir.

A After the consummation of the agreement between  
Messrs. Biaggini and Mr. Schmidt in September of 1983  
and the approval by the boards in October of 1983, we  
then started to set up teams to go ahead and develop the  
data and the presentations for this application. And  
generally, there was some initiation of that in the  
latter part of '83.

It got increased emphasis and deadlines to

1 meet in the first part of '84 and, as Mr. Cera testified  
2 yesterday, during the first part of '84 Mr. Cera and I  
3 were working together and meeting once a week, either by  
4 phone or in person, to review the progress of the  
5 various teams that were involved in the traffic studies,  
6 the operating studies, the mechanical and engineering,  
7 to make sure that the project was on course, we were  
8 meeting our time dates, targets that we had set to file  
9 our application.

10 And at the same time, as the teams had any  
11 questions as they were preparing their specific parts of  
12 the application, we were there to review with them and  
13 resolve any problems they had.

14 Q And prior to the application being filed, you  
15 reviewed its content and you agree with the points being  
16 made in it, don't you?

17 A That's right.

18 Q In fact, you wouldn't have verified the  
19 application if you didn't, isn't that correct?

20 A Yes.

21 Q Now, you were also president of Southern  
22 Pacific at the time of the UP-MP-WP consolidation case  
23 before the Commission, isn't that the case?

24 A 1979-1980 period?

25 Q I think the application was filed at the end

1 of 1980. You were president at that time, were you?

2 A Yes, yes, sir.

3 Q Now, in that case Southern Pacific opposed  
4 both consolidations, both the consolidation of the Union  
5 Pacific with the Missouri Pacific and the consolidation  
6 of the Union Pacific with the Western Pacific, isn't  
7 that the case?

8 A That is correct.

9 Q And would you say that SP played a vigorous  
10 and prominent role in those proceedings?

11 A That was a big hurt to us.

12 Q But you were an active participant in the  
13 proceedings, weren't you?

14 A I was not personally, no, sir. I was not  
15 involved in the case.

16 Q You were not a witness?

17 A No, sir.

18 Q That doesn't mean that you were unconcerned  
19 and uninvolved, does it?

20 MR. STEPHENSON: That's a compound question.  
21 Unconcerned is one, uninvolved another.

22 JUDGE HOPKINS: Why don't you start with one  
23 and go to the other.

24 MR. WAKER: That's fine.

25 BY MR. WAKER: (Resuming)

1 Q The position taken by Southern Pacific in that  
2 case, as to that position, did you have any role in  
3 determining what the position ought to be, a position of  
4 opposition or no opposition?

5 A I supported the position of opposition, yes.

6 Q And you also supported the position, did you  
7 not, of seeking trackage rights in that proceeding in  
8 the event that the consolidations were approved?

9 A I agreed to that.

10 Q In fact, you verified the responsive  
11 applications on behalf of both Southern Pacific and the  
12 Cotton Belt, didn't you?

13 A If the record shows it I guess I did. I don't  
14 recall.

15 Q You don't recall?

16 A I can't remember what specifically I wrote or  
17 verified at this time. I haven't reviewed it.

18 Q Just to refresh your recollection, Mr. McNear,  
19 what I'm showing you is indicated as being volume one of  
20 the applications of the Southern Pacific and the Cotton  
21 Belt, and here on page 38 under the heading "Prayer for  
22 relief and signatures," is that your signature?

23 A That is, dated January 2nd, 1981.

24 Q And then verifications?

25 A Yes.



1 Q Thank you.

2 So is it fair to conclude, Mr. McNear, that  
3 since you signed the application and you verified it,  
4 that previously you also reviewed the contents and were  
5 satisfied with them?

6 A I had generally reviewed the contents, yes.

7 Q Now, do you recall that it was Southern  
8 Pacific's position in that case -- that's the UP-MP-WP  
9 consolidation case -- that motor carriers are not an  
10 adequate substitute for rail carriers in most  
11 transcontinental freight markets?

12 A I believe the record will show that that was  
13 our position at that time.

14 Q And do you recall that included in the case  
15 put in by the Southern Pacific in that proceeding was  
16 the testimony of an economist, Dr. Robert A. Nelson?

17 A I can't recall positively whether it was or  
18 not. But if it was there, I'll accept it.

19 Q And do you recall that one of SP's contentions  
20 in that case was that its shippers -- that's the  
21 SP-served shippers -- in California were heavily  
22 dependent on rail service?

23 A I can't recall that representation being  
24 made.

25 Q Do you recall whether Southern Pacific

1 introduced a study which quantified the anticipated  
2 increase in transportation costs which those shippers --  
3 that's the SP captive shippers -- would suffer if they  
4 were forced to shift from rail to truck, and SP's  
5 evidence indicated that on average those shippers would  
6 incur a 71 percent increase in transportation expenses?  
7 Do you recall that?

8 I do not recall that.

9 MR. BAKER: Your Honor, I think it probably  
10 will move along faster here if, rather than continuing  
11 to examine Mr. McNear on these matters, which obviously  
12 he doesn't recall, if what I did at this time is to mark  
13 certified copies of the record in that proceeding and  
14 the dispense with further cross-examination on those  
15 points.

16 I have several documents. The first that I'd  
17 like to have marked for identification is KCS-C-3, is a  
18 document filed in that proceeding by Southern Pacific.  
19 And in all cases, when I say Southern Pacific, also by  
20 its subsidiary, St. Louis, Southwestern Railway  
21 Company. And it's denominated SPT-44, and this is a  
22 copy that's certified by the Commissior Secretary.

23 JUDGE HOPKINS: It will be marked for  
24 identification.

25 (The document referred to

1 was marked Exhibit No.

2 KCS-C-3 for

3 identification.)

4 JUDGE HOPKINS: Mr. Baker, you gave me two. I  
5 don't need them. You might need them.

6 MR. BAKER: Next, Your Honor, I'd like to have  
7 marked for identification as KCS-C-4 a certified copy of  
8 another document introduced into evidence in that  
9 proceeding. It is denominated SPT-45.

10 JUDGE HOPKINS: It will be marked for  
11 identification.

12 (The document referred to

13 was marked Exhibit No.

14 KCS-C-4 for

15 identification.)

16 MR. BAKER: The third certified document that  
17 I would like to have marked for identification, Your  
18 Honor, and this one as KCS-C-5, is a letter that was  
19 introduced in that proceeding. It's a letter from  
20 counsel to the Southern Pacific, together with a series  
21 of revisions to the documents that I just had marked.  
22 This will be KCS-C-5.

23 JUDGE HOPKINS: That will be marked for  
24 identification.

25 (The document referred to

1 was marked Exhibit No.  
2 KCS-C-5 for  
3 identification.)

4 MR. BAKER: Now I'd like to have marked for  
5 identification, Your Honor, as KCS-C-6 for  
6 identification a certified copy of a verified statement  
7 introduced in those proceedings by Southern Pacific, the  
8 verified statement of Dr. Robert A. Nelson. And this  
9 was introduced in that proceeding as Exhibit  
10 SPT-HVS-107.

11 JUDGE HOPKINS: That will be marked for  
12 identification.

13 (The document referred to  
14 was marked Exhibit No.  
15 KCS-C-6 for  
16 identification.)

17 MR. BAKER: And the last of the verified  
18 documents, Your Honor, which I would like to have marked  
19 as KCS-C-7 for identification is a series of transcript  
20 references that relate, for example, to the introduction  
21 of these various documents into the record.

22 JUDGE HOPKINS: That will be marked for  
23 identification.

24 (The document referred to  
25 was marked Exhibit No.

1 KCS-C-7 for  
2 identification.)

3 BY MR. RAKER: (Resuming)

4 Q All right, Mr. McNear, now we can come back to  
5 the present, to this case, rather than the last one.  
6 But before we get to the specific facts of this case,  
7 let me pose to you what I think is a pretty simply  
8 hypothetical.

9 Assume that you are given the choice of making  
10 two investments. One of them is 100 percent ownership  
11 of a corner grocery, and again assume for the same price  
12 you could also get ten percent of AT&T. Which would you  
13 choose?

14 A I can't answer that question without much more  
15 facts.

16 Q All right. Now, as a railroad president you  
17 have these choices: 100 percent of American Motors'  
18 business or 50 percent of General Motors' business.  
19 Which would you take?

20 A With only that representation, I can't tell  
21 you.

22 Q You need more facts, is what you're saying.  
23 In other words, I think what you're saying is that a  
24 relatively small percentage of a very large pie might be  
25 more valuable than a very big percentage or even 100

1 percent of a very small pie. But what you have to know  
2 is what's the size of the pie, is that right?

3 A What I'm saying is you have to know the facts  
4 of the situation of both alternatives.

5 Q Fair enough. Now I'd like you to look at page  
6 5 of your verified statement, and in particular I'd like  
7 you to look at the first footnote, where you talk about  
8 railroads having lost market share during the period  
9 1929 to 1982. Do you see that?

10 A I do.

11 Q Do you think you have provided all the  
12 information there that one would need to know to  
13 determine whether railroads are in a true declining  
14 position?

15 A The footnote refers to my statement on the top  
16 of the page, indicating that the continued improvement  
17 of the U.S. interstate highway system in the 1960's and  
18 early 1970's has provided the trucking industry with a  
19 massive public subsidy with which to continue its  
20 incrcads in intercity rail market shares.

21 And then to support that, what I have  
22 indicated -- and the source of this is from the AAR Rail  
23 Facts of 1983 -- that the intercity freight tonnage,  
24 looking at the percentage share between rail and truck,  
25 indicates that rail has gone from 75 percent to 36

1 percent and trucks have increased from 3 percent to 23  
2 percent.

3 Q Well, look at the bottom of page 4, the  
4 introduction to the section that you just mentioned, Mr.  
5 McNear. There you say that the success of motor  
6 carriers relative to the rail industry over the past  
7 several decades is an undeniable fact and a significant  
8 factor underlying the need for this merger.

9 A I believe in that.

10 Q Why is it a factor that leads to the need for  
11 this merger?

12 A Today, with deregulation of the trucking  
13 industry, the increase in owner operator proprietary  
14 trucking, the deregulation of the rail industry, there  
15 is just tremendous competition for transportation needs,  
16 and that's by -- between railroads and between the other  
17 modes.

18 And for example, as was being discussed  
19 yesterday, we have two railroads competing, us and the  
20 Santa Fe, and the question was raised, with the  
21 combination of the two wouldn't there only be one  
22 railroad left in that corridor? Yes, but the other side  
23 of the equation was that there's also, parallel to the  
24 two railroads, there's also many truckers competing for  
25 that business, and that's the total transportation

1 business that we're addressing and what we're seeing  
2 here.

3 Q I don't think you are really focusing on what  
4 I'd like you to focus on, Mr. McNear, with my question.

5 A I'm focusing on my testimony here, Mr. Baker.

6 Q But I'd like you to focus on my questions.

7 A Yes, sure.

8 Q In the middle of the first paragraph on page  
9 5, you say that the continuing shift from rail to trucks  
10 poses a very real threat to SPT's long-term financial  
11 viability. Do you see that?

12 A Yes, sir.

13 Q Is the data that is indicated in the first  
14 footnote on page 5, is that data intended in any way to  
15 indicate that this shift that you were talking about  
16 constitutes a threat to SPT's long-term financial  
17 viability?

18 A The footnote gives the percentage market  
19 share, as I have discussed before, as a reference. The  
20 threat is what I just recited.

21 Q But do the percentage market shares give you  
22 the answer to the question when you don't know what the  
23 size of the market is? Didn't you indicate, in response  
24 to my hypotheticals, that you have to know more facts  
25 than apparently is provided in that footnote?



1 A Yes.

2 Q And isn't it the case that in fact the size of  
3 the pie is much larger? Isn't it the case that today or  
4 in 1982 railroads carried over twice as much traffic as  
5 they carried in 1929?

6 A I'm not sure of the total tonnage, but the  
7 total pie has increased and we are sharing a portion of  
8 it.

9 Q You don't find that surprising, though, the  
10 statement that I made, that today railroads carry twice  
11 the ton-miles of freight that they carried in 1929?

12 A I'll accept that.

13 Q And western railroads carry over three times  
14 the ton-miles that they carried in 1929?

15 A That's plausible, because many of the western  
16 railroads have great access to coal, which is a  
17 commodity that Southern Pacific does not have, and  
18 therefore that would reflect in the increased total  
19 tonnage handled by the western railroads.

20 Q All right. Now let's talk about SP. Is SP  
21 today carrying less ton-miles than it did in 1929?

22 A No, we're carrying more.

23 Q Considerably more?

24 A More than '29, but less than three or four  
25 years ago.

1 Q Now, a couple of years ago you made a public  
2 statement, didn't you, to the effect that rail was going  
3 to get a larger -- earn a larger share of the total  
4 transportation market, and that that rail share would  
5 increase through the remainder of the century?

6 A Can you give me a reference to that, please?

7 Q Of course I can.

8 A Thank you.

9 MR. BAKER: Your Honor, may I please have  
10 marked as KCS-C-8 for identification a document which is  
11 entitled "Keynote Address by Denman K. McNear," and the  
12 date of it is October 25, 1982. It's a document of ten  
13 pages plus the cover.

14 JUDGE HOPKINS: It will be marked for  
15 identification.

16 (The document referred to  
17 was marked Exhibit No.  
18 KCS-C-8 for  
19 identification.)

20 BY MR. BAKER: (Resuming)

21 Q I'd like you to look at page 3, Mr. McNear, at  
22 KCS-C-8 for identification.

23 A Yes, Mr. McNear.

24 Q Do you see the middle paragraph there? It  
25 says: "Last year America's railroads carried nearly 38

1 percent of the nation's intercity freight. That's the  
2 biggest market share we've had since 1974 and the  
3 largest single block of traffic in the national  
4 transportation system. Our share of the nation's  
5 transportation business is steadily rising and it will  
6 continue to rise for the rest of the century."

7 Now, you said that, didn't you?

8 A That's what I said. And once again, this was  
9 a speech I gave to the AAR Communications and Signal  
10 Division in St. Louis in October.

11 Q You're not saying you say different things to  
12 different audiences, are you?

13 A No, no.

14 Q But this was your view, this was your opinion;  
15 is that correct?

16 A Based on the facts.

17 Q Based on the facts. You took the facts and  
18 you applied your experience and your expertise and you  
19 came to this conclusion, isn't that correct?

20 A I was indicating to the audience that there  
21 was greater traffic and the railroads were sharing in  
22 it.

23 Q And in fact, that railroads would continue to  
24 share in an increase through the remainder of the  
25 century?

1 A This is an industry statement, yes.

2 Q I don't understand what you mean by "an  
3 industry statement."

4 A This is the total industry market of rail  
5 versus Southern Pacific Transportation Company, and its  
6 figures and its growth may be parallel, above or below  
7 the national level.

8 Q Now, when we come back, though, to the  
9 footnote on page 5, that's also an industry figure, is  
10 it not?

11 A That is correct.

12 Q And in fact, because it's an industry figure,  
13 it somewhat distorts, doesn't it, what has happened in  
14 the western states?

15 A It doesn't necessarily represent any  
16 geographic territory.

17 Q And in addition to that, because it includes  
18 all intercity freight tonnage, it also includes freight  
19 tonnage which railroads essentially have chosen no  
20 longer to compete for, isn't that the case?

21 A In some cases, and also includes the tonnage  
22 that is joint truck-rail-truck, which we're trying to  
23 do, to bring more on piggyback.

24 Q But the point is that this includes short haul  
25 markets as well as long haul, doesn't it?

1           A     It includes all intercity traffic handled by  
2 rail and truck.

3           Q     I just want to make clear for the record that  
4 the last item that we were talking about, the footnote  
5 on page 5, that that's page 5 of your verified statement  
6 rather than page 5 of KCS-8.

7           A     There were no footnotes on my speech, thank  
8 you.

9           Q     Now, in addition to railroads carrying more  
10 freight today than they carried in 1929, it's also the  
11 case that they carry it more efficiently. Isn't that  
12 the case?

13          A     In general terms, I agree with that.

14          Q     In other words, today railroads have, what is  
15 it, approximately 70, 71 percent of the route miles that  
16 they had back in 1929, isn't that right?

17          A     That's your figure. It sounds reasonable.

18          Q     There has been a considerable reduction in the  
19 number of employees of railroads during that period of  
20 time, hasn't there?

21          A     There has. There has also been a tremendous  
22 inflationary spiral in our other costs that remain.

23          Q     And I take it that your revenues have gone up  
24 as well, haven't they?

25          A     They've gone up by indexing, by volume.

1 Q And the problem that you have in terms of  
2 regulatory lag, where due to inflation your rate  
3 increases were unable during the regulatory period to  
4 keep up with inflation, now that's a thing of the past,  
5 essentially, under the Staggers Act, isn't it?

6 A Under the Staggers Act, they did pass through  
7 rate increases until just recently, when now we have to  
8 jointly do it, and that's becoming more difficult.

9 Q Now I'd like to turn to the second footnote on  
10 page 5 of your verified statement. It refers to a  
11 reduction in perishables business.

12 A Yes, sir.

13 Q And I'll try another hypothetical. You go to  
14 a stock broker and you say you want a recommendation,  
15 and he says: Well, I've got two stocks for you. Both  
16 of them came out at the same time. About five years ago  
17 they were new issues, and today both of them are selling  
18 for twice what they initially were issued at.

19 Is that enough information, or do you want to  
20 know what's happened during that five-year period?

21 A Probably that and some more.

22 Q So in other words, if one of the stocks had  
23 gone up a lot, but three or four months ago started on a  
24 precipitous decline, that would not be nearly as  
25 attractive, would it, as a stock that had stayed fairly

1       ever for four of those years but now has been steadily  
2       moving up?

3                You'd want to know about that information  
4       anyway, wouldn't you?

5                A       I'd want to know specifically what factors  
6       were affecting each individual stock in the past and for  
7       the future, just like in railroading when we look at  
8       what's happened to the industry in total versus a  
9       railroad in particular.

10              Q       Now, let's look at the data that you provided  
11       in the second footnote on page 5. In the first  
12       sentence, you report on rail share of perishable  
13       business and you show figures at three dates: 1962,  
14       1972, and 1982. Do you see that?

15              A       Yes, sir.

16              Q       And looking at that, one would think that  
17       there has been a steady decline in the rail share,  
18       wouldn't one?

19              A       There has been a steady decline in the  
20       percentage of the rail share, yes. That's what it  
21       indicates.

22              Q       That's not what your work papers show, is it,  
23       Mr. McNear?

24              A       The percentage?

25              Q       I'm talking about a steady decline. Did

1 something happen in the late seventies that caused  
2 perishables traffic to be more attractive to railroads  
3 and has increased rail share of perishables traffic?

4 A In the late seventies?

5 Q Yes.

6 A Well, let me just give you some figures of  
7 just relating to the Southern Pacific. In the year 1970  
8 we handled about 129,000 carloads. By '75 that had gone  
9 down to 74,000 carloads, and by '80 22,000 carloads;  
10 '82, 20,000; '83, 17,700.

11 So what's represented here are specific dates  
12 and percentages in the footnote, are the railroad's  
13 share of the perishables, and what I've tried to also  
14 indicate is to get to the specifics of Southern Pacific  
15 and what has been our experience.

16 And you'll notice, if you want to throw some  
17 percentages, just since 1970 to '83 it's 17 on 129.  
18 It's almost ten percent left; 90, 89 percent reduction.

19 Q Let's talk about what happened between 1972  
20 and 1982. Isn't the figure at 1982, the 21 percent --  
21 do you see that?

22 A Yes, sir.

23 Q Isn't that higher than, for example, what  
24 rail's share was in 1980?

25 A It may be.



1 Q Isn't it the case that the reduction in  
2 perishable traffic, rail share of perishable traffic, if  
3 you want to take a curve, that it reached a plateau in  
4 the late seventies and has actually started back up?

5 A Well, let me cite from our own Southern  
6 Pacific experience.

7 Q No, let's talk about -- the figure in footnote  
8 2 isn't Southern Pacific, is it?

9 A Well, you're giving me some numbers of a  
10 different year that I don't refer to, so I don't know.

11 Q I know that you haven't referred to it, but it  
12 was in your work papers, wasn't it?

13 A It may have been.

14 Q Do you have your work papers with you?

15 A No, I don't.

16 Q I have only a single copy.

17 (Witness examines document.)

18 A All right.

19 Q My first question is, Mr. McNear, don't your  
20 work papers indicate that, in terms of the rail versus  
21 truck share of perishables, that in fact there has been  
22 an increase in the rail share between 1980 and 1982?

23 A My work papers indicate that the rail share in  
24 1972 was 26.6 percent; in 1980 it was 15.5 percent; and  
25 in 1982 it's 20.7 percent. So it showed an increase

1 1982 over 1980 and a decrease from 1972.

2 Q And is it not important when one looks at  
3 statistics to look at something more than the beginning  
4 and end point? Is it not important to know what's  
5 happened in between?

6 A That's one consideration.

7 Q And you also looked at certain charts that  
8 were attached to that particular work paper, didn't you,  
9 Mr. McNear?

10 A I did.

11 Q And those charts indicate that SP's  
12 perishables business has been on the upswing beginning,  
13 let's say, in the late seventies, isn't that correct?

14 A In some of the commodities there has been a  
15 slight increase.

16 Q And in others it remained about constant?

17 A That's right. But I think once again, going  
18 back to what I said earlier, this trend goes back to  
19 1973, and you see a marked decrease from '73 to the  
20 current volume. I wish we were handling the volumes  
21 that we did years ago, but that just isn't the fact.  
22 The trucks are taking it away from us.

23 MR. RAKER: Your Honor, could that be  
24 stricken? It is unresponsive.

25 JUDGE HOPKINS: It is unresponsive and I'll

1 strike it.

2 Why don't you try and answer the questions  
3 without going on. Your attorney will be able to  
4 question you later on.

5 BY MR. BAKER: (Resuming)

6 Q One more footnote, Mr. McNear. It's the last  
7 one, on page 5 of your verified statement, and it deals  
8 with lumber traffic, doesn't it?

9 A It does.

10 Q And apparently the figures which you show come  
11 from a data base maintained by the Western Wood Products  
12 Association; is that correct?

13 A That is correct.

14 Q And as I understand it, what you are  
15 attempting by that footnote to demonstrate is that  
16 lumber, which is an important commodity for Southern  
17 Pacific, is highly subject to truck competition. Is  
18 that a fair statement?

19 A This is a footnote to the first paragraph on  
20 page 5, responding to those commodities that the  
21 Southern Pacific is very dependent on and its financial  
22 viability is very dependent on. And what this  
23 represents is that the share of lumber handled by trucks  
24 is increasing and it's a major concern of ours.

25 Q Now, the data that you use there is for all

1 lumber criginations in the western United States; is  
2 that correct?

3 A It's the Western Wood Products Association's  
4 report.

5 Q But it includes short hauls, long hauls,  
6 everything; is that correct?

7 A Yes, it would.

8 Q Now, the Western Wood Products Association  
9 also provides from their data base disaggregated  
10 infcration which would make it possible to look at the  
11 long haul share of -- look at the long haul traffic and  
12 the rail shre of long haul lumber traffic, isn't that  
13 the case?

14 A I assume they do.

15 Q Are you aware, Mr. McNear, that in the UP-MP  
16 case you put in, Southern Pacific put in, evidence which  
17 focussed on the long haul lumber market?

18 A I can't recollect what we put in today then.  
19 All I can say is what's happening to the lumber traffic  
20 today, and we're seeing long haul traffic right out of  
21 the Northwest, our territory, going across  
22 transcontinental points as well as down the coast, it's  
23 going all over by truck.

24 Q Would you look at KCS-C-3 for identification,  
25 please?

1 A Yes, sir. Page?

2 Q Page 16.

3 A Paragraph?

4 Q The last paragraph on the page, in fact the  
5 last sentence on the page. No, excuse me. It's not the  
6 last sentence. The penultimate sentence. It says:  
7 "According to the Western Wood Products Association,  
8 over 90 percent of West Coast lumber shipments to  
9 eastern states" -- and that's defined to mean states  
10 east of and including Nebraska, Kansas, Oklahoma and  
11 Texas -- "moved by rail in 1980."

12 A That's what it says, in 1980.

13 Q The first question is this: Do you think that  
14 it is a relevant statistic for purposes of a railroad  
15 merger and consideration of the anticompetitive  
16 consequences of a railroad merger to look at the long  
17 haul market for movement of lumber?

18 A I think it's a relevant statistic for the  
19 Commission and those people that are looking at this  
20 merger and the financial viability of Southern Pacific  
21 Company to look at what the market is in our territory  
22 and what we have, what is the total lumber being  
23 produced in our area, and what's the availability of it  
24 to be handled in transportation for years to come.

25 Q That wasn't my question. My question is, is

1 it relevant to look at the long haul market?

2 A What's your definition of "long haul"?

3 Q The same market that Southern Pacific deemed  
4 was relevant in the Union Pacific-Missouri Pacific case,  
5 namely movements from the West Coast to the states of  
6 Nebraska, Kansas, Oklahoma, and Texas, and all states  
7 east of that.

8 MR. STEPHENSON: Excuse me, Mr. Raker. Do you  
9 mean is it relevant to look at that in exclusion of  
10 anything else? Just that?

11 MR. RAKER: No, no, no. I am only asking, is  
12 that a relevant statistic?

13 THE WITNESS: That's their definition of "long  
14 haul." I would say long haul would be from Oregon to  
15 Arizona.

16 BY MR. RAKER: (Resuming)

17 Q That would be included in this, wouldn't it?

18 A No, not if I read "east of," and Arizona is  
19 west of Texas.

20 Q So what you're saying is that there is some  
21 long haul market that you would not include in this, all  
22 right. But is it your position, sir, that this  
23 percentage, this 90 percent figure, if one were to do  
24 the study today, that that figure would be less than 90  
25 percent?

1           A     That would be my presumption, yes. And the  
2 facts would prove whether I'm right or wrong.

3           Q     But it is your view, isn't it, that railroads  
4 should concentrate on those movements for which it's  
5 most efficient and leave the short haul business to  
6 trucks?

7           A     I think I've indicated before that we go for  
8 long haul and we go for short haul, and what we're  
9 trying to do in our piggyback operation is get a  
10 combination of the long haul for over the road and marry  
11 up with the truckers on their short haul economies, so  
12 we both provide a total minimum transportation cost to  
13 the customer.

14          Q     Would you turn to page 6 of your verified  
15 statement, please. You make references there, or  
16 reference, to studies which indicate that motor carrier  
17 costs may be reduced by as much as 20 percent. Do you  
18 see that?

19          A     I do, yes, up there on the top of the page, on  
20 page 6.

21          Q     I couldn't find anything in your work papers  
22 which indicates what those studies are. Could you give  
23 me a reference to them, please?

24          A     That's from my knowledge, and if it isn't in  
25 the work papers I think our counsel can make it

1 available.

2 MR. STEPHENSON: I can make that available to  
3 you. It's AAB truck cost model, which apparently was  
4 based on U.S. Department of Transportation's highway  
5 cost allocation studies, and I can get for you some more  
6 precision.

7 BY MR. RAKER: (Resuming)

8 Q Also on page 6, I would like to direct you to  
9 your comment that Southern Pacific is a light loaded  
10 railroad. Chemical traffic is very significant to  
11 Southern Pacific, isn't it?

12 A That's one of our major commodities.

13 Q And this is because the Gulf Coast that you  
14 cover so well is really the heartland of the  
15 petrochemical industry, isn't it?

16 A In the United States.

17 Q And is it the case that petrochemicals  
18 comprise about a third of SP's Gulf Coast originations?

19 A I've never looked at that specific figure.  
20 I've looked at chemicals as a total of our originations,  
21 not of a particular area.

22 Q And have you projected that there will be a 50  
23 percent increase in the movement of petrochemicals from  
24 the Gulf over the next decade?

25 A Mr. Baker, can you give me a place where I



1 said that and we can get on with it?

2 Q I'm going to try to do that right now.

3 A All right, let's go.

4 MR. BAKER: I don't think it's going to be  
5 necessary to have this marked, Your Honor.

6 BY MR. BAKER: (Resuming)

7 Q What I am showing you, Mr. McNear, is the  
8 text, or at least it purports to be the text, of an  
9 address by you given on May 13, 1983, in Houston,  
10 Texas. If you'd look, sir, at the top of page 3.

11 A Yes, sir.

12 Q It says: "Petrochemicals make up more than a  
13 thrd of SP's traffic that originates along the Gulf  
14 Coast."

15 A Yes, sir.

16 Q "We expect such shipments to increase 50  
17 percent in the next decade." Do you see that?

18 A I do, and this is my speech May 13th at  
19 Houston to the Hazardous Materials Advisory Council.

20 Q Right. And that was your opinion then, wasn't  
21 it, in 1983?

22 A In May of '83, yes.

23 Q Fifteen months ago?

24 A Yes.

25 Q Do you have a different opinion today?

1           A     My opinion today is still bright for the Gulf  
2 Coast. However, just like in the automobile industry,  
3 there are harbingers of competition offshore, and if  
4 producers of chemicals offshore import into the United  
5 States in the consuming areas of the eastern seaboard  
6 and the Great Lakes territory, it could have an impact  
7 on this projection that I made back in May of '83.

8           I hope it doesn't happen, for our sake. Keep  
9 it American.

10          Q     This is not a factor that concerned you in  
11 1983 or is it a factor that you took into account at  
12 that time? Which one?

13          A     It's not a factor that I took into account at  
14 that time.

15          Q     Now, chemicals, or at least a good deal of the  
16 chemical traffic, is rail dependent, isn't it?

17          A     It goes by truck and rail.

18          Q     In other words, what you would have to do is  
19 break it down. You can't just look at a two-digit SIC  
20 code, is that what you're saying? You have to break it  
21 down finer than that?

22          A     Well, I'm thinking that, just as I drive on  
23 the highway, I see chemicals going by truck when I'm  
24 down in New Orleans, Louisiana, Texas area, as well as  
25 by rail.

1 Q I think you're more expert than just any  
2 person who drives along the highway. I'm asking you for  
3 your opinion as the chief executive of a railroad.

4 MR. STEPHENSON: Wait a minute. I'll object  
5 that you haven't established that Mr. McNear is any  
6 expert on two-digit STCC codes, or four digit or  
7 whatever. If you want to establish that he is an  
8 expert, be my guest.

9 JUDGE HOPKINS: I don't think you want to go  
10 into that, do you, Mr. Baker, to establish that he is an  
11 expert on it?

12 MR. BAKER: No, not on STCC codes, Your  
13 Honor. The point is, though, that this is his speech  
14 and it was in his speech.

15 JUDGE HOPKINS: I understand.

16 BY MR. BAKER: (Resuming)

17 Q Now, a number of petrochemicals fall into the  
18 hazardous materials category, don't they?

19 A They do.

20 Q And it's because of that -- or at least that  
21 is one factor, is it not, that chemical traffic is  
22 largely rail dependent, isn't that right?

23 A I believe there are some requirements that it  
24 goes by rail. Others, depending on the degree of  
25 hazardous material, they can go by truck or any other

1 mode. A lot of it goes by water.

2 Q If both points are on the water, isn't that  
3 correct?

4 A And the Gulf Coast is on the water, and the  
5 consuming points at Wilmington, Delaware, and others on  
6 the East Coast are on the water, yes, sir.

7 Q And the West Coast is also on the water, isn't  
8 it?

9 A Yes, sir.

10 Q But to get to the West Coast from the Gulf  
11 Coast, you've got to go east to get through the Panama  
12 Canal, don't you?

13 A Yes, sir.

14 Q That's quite circuitous, isn't it?

15 A But a low rate. And I think you'll find  
16 there's quite a bit of traffic going from the Texas Gulf  
17 Coast area to southern California by water, somewhere  
18 probably, oh, 18, 20 percent.

19 Q Would you say that, with the exception of  
20 petroleum, the railroads move 70 percent of all  
21 hazardous materials?

22 A If there's a record of that I'd accept it.

23 Q Look at page 21 of the last document I showed  
24 you.

25 A All right. Yes, sir.

1 Q That's what it says, isn't it?

2 A Yes, sir. It also says, and for the record,  
3 the railroads are involved in only ten percent of the  
4 reportable accidents with hazardous material, and that's  
5 what I was trying to say to this audience in Houston.

6 Q Yes. That's a very good reason why these  
7 materials ought to move by rail, isn't it?

8 A We and the KCS are proud of that.

9 Q Right, sir.

10 Now, chemical traffic for the most part is  
11 also desirable and profitable traffic, isn't it?

12 A It's desirable traffic, it's competitive  
13 traffic, and we like to haul it. But once again, we've  
14 been talking about the hazardous nature, and if you have  
15 one derailment it may cost \$3 million, and it takes a  
16 lot of cars to make up that lost revenue on the margins  
17 that we're getting per car.

18 Q Now let me ask you, sir, do KCS and the  
19 Missouri Pacific compete with SP for the origination of  
20 chemical traffic on the Texas-Louisiana Gulf?

21 A We do.

22 Q Now, for movements to California today it's  
23 the case, isn't it, that KCS and MP have available joint  
24 routes with the Santa Fe that would be in competition  
25 with your single line route; is that correct?

1           A       That would be one movement. I'm sure we're  
2 handling some joint traffic with the KCS today.

3           Q       Probably you're handling joint traffic with  
4 the KCS today where KCS originates the traffic in  
5 competition with the Santa Fe, for example to Beaumont;  
6 isn't that correct?

7           A       Or the Missouri Pacific at Beaumont.

8           Q       Now, after the merger the merged company is  
9 going to have an incentive to cancel those joint routes,  
10 isn't it, in order to force the traffic over the single  
11 line route?

12          A       I think you pose a hypothetical question. As  
13 we look forward to how that traffic would be handled by  
14 merged carriers, certainly we would generally believe  
15 that it would be handled single line, and the reason for  
16 that is that normally the single line is the most  
17 efficient, least costly method, and for that reason it  
18 should flow that way from an economic standpoint and  
19 probably at the request or benefit of the customer.

20                   There will also be some cases where a joint  
21 line route may be the most economical, less costly, and  
22 there's factors that would come into this, whether it's  
23 less mileage, whether there is -- whether you take an  
24 empty return, whether it's private or railroad-owned  
25 equipment, whether it's the geography, the mountains,

1 and whether the shipper prefers that it goes on a joint  
2 line route.

3 So we're willing to look forward and work on  
4 any basis in handling the traffic for the customer.

5 Q In today's atmosphere, if a shipper were to  
6 say to the Southern Pacific, we don't like these route  
7 cancellations that you've employed -- in other words, a  
8 captive shipper to the Southern Pacific -- we don't like  
9 these route cancellations that the SP has employed, we  
10 want you to open up joint routes with the KCS, you would  
11 then go ahead and open up a joint route, would you?

12 A First of all, you're making a supposition in  
13 your question that shippers have complained about our  
14 joint rates and cancellations, and I refer that question  
15 to Mr. Edwards, because he knows whether any shippers  
16 have in fact come to him.

17 And I also refer to him the reply to the  
18 second part of your question, of what we'd work out to  
19 satisfy the shipper.

20 Q What's your policy on that?

21 A I just stated it: Our normal thing, that the  
22 single line rate -- or single line route, excuse me --  
23 is generally the most efficient, and certainly we would  
24 be looking for that movement, and the shipper should,  
25 too.





1 as Mr. Cena, though.

2 MR. BAKER: Well, actually you don't have that  
3 many more speeches, Mr. McNear.

4 BY MR. BAKER: (Resuming)

5 Q I notice that round about May of 1983 the  
6 public speeches ended. Is that because there was a  
7 policy decision made in conjunction with the merger that  
8 it would be best not to continue to make public  
9 remarks?

10 A None whatsoever.

11 Q Just a coincidence?

12 A Yes.

13 Q Now, what I'd like to discuss with you for a  
14 few moments is intermodal traffic. It's your view,  
15 isn't it, that intermodal traffic represents the optimum  
16 in transportation efficiency?

17 A For certain commodities, yes.

18 Q Well, at page 5 of KCS-C-9 you say there:  
19 "Perhaps the optimum in transportation efficiency  
20 results when the fuel efficiency of trains is combined  
21 with the flexible delivery capabilities of trucks."  
22 That's still your opinion, isn't it?

23 A I've already stated it in this record.

24 Q And intermodal traffic is quite important in  
25 SP's territory, isn't it?

1 A It is.

2 Q And a high percentage of SP's intermodal  
3 traffic is maritime intermodal, isn't it?

4 A That's part of it, both domestic and  
5 maritime. It's a combination.

6 Q But the maritime is quite a high percentage,  
7 isn't it?

8 A I wouldn't offhand be able to say, of our  
9 total intermodal, how much is container and how much is  
10 trailer.

11 Q And you've also made reference, haven't you,  
12 to the increasing importance of world trade and the  
13 effect that this has had on the increasing importance of  
14 maritime intermodal traffic?

15 A That is correct.

16 Q And this is essentially the point that you  
17 make in KCS-C-9 for identification. If you'd look over  
18 at page 6, you point out there at the beginning of the  
19 second paragraph that it's more economical to transport  
20 Far Eastern goods to Europe, not by an all-ocean route,  
21 but by sea to the U.S. West Coast and then thereafter by  
22 rail to the East Coast.

23 Do you see that?

24 A Referring to land bridge operations?

25 Q I think that's right. That is what you're

1 referring to, isn't it, a land bridge operation?

2 A That's what it reports here, yes.

3 Q And motor carriers are not competitive for  
4 maritime intermodal, are they?

5 A I have to think about that one. In what  
6 respect? In what arena are we talking about?

7 Q Well, what I am saying is, if you're going to  
8 take a land bridge operation such as the one that's  
9 described in your speech here, KCS-C-9, where a large  
10 container ship comes in at Long Beach, let's say, and  
11 has a load of containers, a number of which are going to  
12 move to the East Coast, where they will then get on a  
13 ship to go to Europe, do you believe that motor carriers  
14 are competitive for that movement from Long Beach to  
15 Savannah, let's say?

16 A Pricewise not, servicewise yes.

17 Q The same would be true, would it not, of a  
18 mini-bridge movement from Long Beach to New Orleans,  
19 let's say?

20 A Take New Orleans, take Kansas City, same  
21 distance. There's a good portion of it, I'd say, of  
22 traffic that's coming over the docks is going by truck  
23 versus rail.

24 Q In other words, you believe that there's a  
25 substantial amount of the mini-bridge traffic that comes

1 into, let's say, Long Beach and proceeds under the ocean  
2 transport waybill via truck, as distinguished from via  
3 rail; is that your testimony?

4 A I didn't refer to what kind of a billing it  
5 was under. I'm thinking of the benefits of truck  
6 delivery. The first example we're talking about is rail  
7 through to Savannah for export to Europe, and that, the  
8 logic of the benefits or the logic of the flow would be  
9 that rail would be the primary move.

10 As far as changing to mini-bridge and going  
11 internally, then the option really presents itself as to  
12 whether, for internal movements in the United States,  
13 there is the choice of truck versus rail.

14 Q Isn't it the case that even on the mini-bridge  
15 movements, Mr. McNear, that the shipper, let's say in  
16 the Far East, makes his arrangement with the maritime  
17 operator, and the maritime operator has his arrangement  
18 with the railroads here, and the container moves under a  
19 single waybill? Isn't that the case?

20 A I'm not positive on that. What I do know is  
21 that generally it's the stateside traffic officer  
22 representing the customer or the shipper that directs  
23 the flow of the traffic in the United States, and that's  
24 why for many years we didn't have a representative in  
25 Japan. We thought we could work with the people here,

1 whether in directing by rail or by truck, as far as the  
2 inland movement from the port.

3 Q Let's go on to the coal traffic. It's not  
4 necessary to originate coal to earn substantial coal  
5 transportation revenues, is it?

6 A I have a hangup on "substantial," your choice  
7 of the word "substantial."

8 Q All right. Let me give you an example, then.  
9 Is it your belief or understanding that KCS moves  
10 significant coal tonnage?

11 A I think they are handling a representative  
12 good amount of coal on their line.

13 Q Is it an amount you would call substantial?

14 A For that property, I'd say it is substantial.

15 Q And do you know whether KCS originates any of  
16 that coal?

17 A I don't believe so. They may have some  
18 lignite mines up in the upper part of their reaches, and  
19 I think most of its in interchange. That's my  
20 perception.

21 Q Now, it's also the case, is it not, that SF's  
22 domestic coal markets are expanding?

23 A Our participation in coal hauling, is that  
24 what you're referring to?

25 Q That's exactly what I'm talking about.

1           A     We have three principal power plants we  
2     serve. We've got some lesser smaller coal movements.  
3     In my opinion it isn't expanding as much as on other  
4     carriers.

5           Q     It isn't expanding at this point as much as  
6     you'd like, is it?

7           A     No, and the bloom is off in the Pacific Basin  
8     export.

9           Q     Why is that?

10          A     There's cheaper sources worldwide than western  
11     coal for the Pacific Rim.

12          Q     And do you consider this to be a permanent  
13     phenomenon?

14          A     The bloom is really off that subject. There  
15     was a lot of emphasis on it. We were involved, and I  
16     guess I gave some speeches at some conferences relating  
17     to that. And currently now, you talk to the Japanese,  
18     the Koreans, and the bloom is not there any more.

19          Q     When did the bloom go off the rose?

20          A     I would say about a year ago, the last year or  
21     two years. It was a prospective bloom. It was never a  
22     material bloom, because of the chick and egg process of  
23     who was going to make the contract, who was going to buy  
24     the coal. And they just went with external sources.

25

1 Q At one point you were, Southern Pacific, I  
2 guess, through a subsidiary, was attempting to establish  
3 a joint venture with the Bishops Gate Coal Corporation.  
4 What is the status of that?

5 A I don't know. That's not in my jurisdiction.

6 Q So that is something that may be proceeding,  
7 then?

8 A That is an SP Company, SP Land Company  
9 venture, and now it is part of the total land or  
10 resource group of the Santa Fe Southern Pacific  
11 Corporation. I don't know where it stands now.

12 Q Now, do you know where the coal reserves are  
13 that were intended to be developed?

14 A If I remember, they are in Utah.

15 Q At a point that could be served by SP?

16 A No, not to my recollection.

17 Q Carbon County, Utah?

18 A If that is where it is, that is where it is.

19 Q In any event, you were in the hearing room  
20 when Mr. Schmidt was on the stand, were you not?

21 A I was.

22 Q And so at least to that extent you are  
23 familiar with the document that was marked as KCS-C-1?

24 A That was the first time I heard anything on  
25 it, is during the cross. Yes, sir.

1 Q And have you had an opportunity -- I shouldn't  
2 ask you have you had an opportunity. Have you read it  
3 since then?

4 A I have not.

5 Q Are you aware from the cross that you heard  
6 that Santa Fe projects a substantial increase in the  
7 coal traffic in the regions served by the Santa Fe and  
8 the SP?

9 A I believe that was his testimony.

10 Q And that those increases would be primarily in  
11 coal terminations?

12 MR. STEPHENSON: Your Honor, I think Mr.  
13 Schmidt's testimony and the exhibits should speak for  
14 themselves.

15 JUDGE HOPKINS: Why do you want to know  
16 whether he is aware of this?

17 MR. BAKER: I think that is right. That  
18 question could be stricken.

19 BY MR. BAKER: (Resuming)

20 Q I guess the point is in any event, Mr. McNear,  
21 you were not aware of this at the time you prepared your  
22 testimony, were you, that is, aware of the projections  
23 made by the Santa Fe?

24 A Not in that report, no.

25 Q Fine. Were you aware of it in any other



1 report?

2 A I don't know. I can't recall whether there  
3 was any mention made in the quarterly reports to the  
4 stockholders, the annual report. If I read it there, I  
5 would be aware of it. Otherwise, I don't recall any.

6 Q Now I would like to go back for a moment to  
7 one of the documents that we marked before. It is  
8 KCS-C-8 for identification.

9 A KCS-C-8?

10 Q Yes, 8. It is your address to the AAF  
11 Communications and Signal Division.

12 A Oh. All right, yes.

13 Q Earlier we referred to your projection that  
14 rail's share of the total transportation business will  
15 continue to rise for the remainder of the century. Do  
16 you recall that? That is the one on Page 3.

17 A Yes. Okay.

18 Q Now I'd like you to look at Page 4, and you  
19 will note there at the top of the page that you opine  
20 that the traffic available to the entire transportation  
21 industry will at least double during the next 20 years.

22 A I was waving the flag. Yes, sir.

23 Q You said what you believed.

24 A Yes, sure.

25 Q And you still believe that, don't you?

1 A Yes.

2 Q And then if you go down another couple of  
3 sentences, you see you also say, "I expect to see  
4 railroads handling a much greater percentage of the  
5 nation's intercity freight in the years just ahead," and  
6 you believe that?

7 A In the intermediate sense it is, but the big  
8 question, of course, is how much of that new traffic  
9 will be handled by railroads, and my answer is what you  
10 just read.

11 Q And that is your answer?

12 A That is our ambition, and through this merger  
13 we ought to be able to attack that problem and get more  
14 of that share.

15 Q But at the time that you made the statement,  
16 you were talking about railroads in general, weren't  
17 you? That had nothing to do with the merger.

18 A As long as this is being brought into this  
19 case, I think it is appropriate for my interpretation of  
20 that today.

21 Q Now I'd like you to look at Page 5. No, let's  
22 skip that, because I think I have already asked you  
23 about those points.

24 Q Would you agree, Mr. McNear, that the Southern  
25 Pacific is in the best physical shape that it has been

1 in for years?

2 A I would say that the Southern Pacific  
3 Transportation Company's main line core route structure  
4 is as good as it has been in many years. Yes.

5 Q And it has got one of the nation's newest and  
6 best maintained locomotive fleets?

7 A That's a fact.

8 Q And SP continued to make heavy investments in  
9 plant even during the recent recession years, didn't it?

10 A That's a fact.

11 Q And that adversely affected immediate  
12 earnings, didn't it?

13 A It has affected earnings as well as our  
14 working capital position, as I have indicated on Page 11  
15 of my testimony.

16 Q But it produces long-term benefits, doesn't  
17 it? At least you hope so.

18 A That is why you make the investment, but you  
19 also have to continue to make investments, and I think  
20 that is the point that I certainly subscribe to, and my  
21 concern in looking ahead is the availability of Southern  
22 Pacific Transportation Company to have the wherewithal  
23 where we can continue to make those investments and get  
24 the proper return to stay in business, because if you  
25 look at my table on 11, you see a completely different

1 picture there of declining income from operations, and I  
2 don't know whether, Your Honor, you would be interested  
3 in what the 1983 numbers are.

4 JUDGE HOPKINS: I think we are always  
5 interested.

6 BY MR. RAKER: (Resuming)

7 Q We can talk about the 1983 figures in a  
8 moment, Mr. McNear. Let's talk about the figures that  
9 are here for a moment, since you just brought them up.

10 A What figures are you referring to?

11 Q The figures on Page 11.

12 A Yes, sir.

13 Q Now, these are financial results of SFT,  
14 consolidated. Is that correct?

15 A These include our trucking and rail, yes, sir,  
16 if that is the definition of your consolidated.

17 Q And these figures are based on retirement  
18 accounting, aren't they?

19 A Betterment retirement accounting. Yes, sir.

20 Q My railroads now have to report on  
21 depreciation accounting, don't they?

22 A That is correct.

23 Q And Santa Fe Southern Pacific reports to its  
24 shareholders on the basis of depreciation accounting.  
25 Isn't that right?

1           A     We are glad that we are like the rest of the  
2 industries in the nation.

3           Q     And if these figures were converted to  
4 depreciation accounting, it would result in increased  
5 income, would it not?

6           A     Maybe I can help you on some of that.

7           Q     You can help me by answering that yes or no.

8           A     All right. Yes.

9           Q     Who made the decision to put these figures in  
10 based on retirement accounting?

11          A     This was a question as we were preparing our  
12 application to the Commission. I think the original  
13 request by the Commission was to have it on depreciation  
14 accounting, and we indicated to put in the records and  
15 go back it was impossible to convert all the previous  
16 years from depreciation to -- from retirement accounting  
17 to depreciation accounting, and we got the concurrence  
18 of the Commission that they would allow us to present  
19 our presentation on the historical retirement accounting  
20 basis.

21          Q     You are talking about the required pro formas,  
22 the exhibits to the application itself. Isn't that what  
23 you are talking about?

24          A     And we are trying to be consistent, yes, with  
25 the past data.

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1           Q     You are aware, aren't you, that in the 1983  
2     annual report of Santa Fe Southern Pacific, an  
3     adjustment was made to the railroad's figures going back  
4     at least to 1979 to indicate the added income from rail  
5     operations which would be reflected by going from  
6     betterment to depreciation accounting. Are you aware of  
7     that?

8           A     I knew there was a restatement. I don't know  
9     how far back it went.

10          Q     Were you aware of a note in that financial  
11     statement to the effect that, and I quote, "Management  
12     believes that depreciation accounting is preferable  
13     because it results in a more systematic allocation of  
14     costs to periods benefitted and conforms to the  
15     accounting practice now followed by the rail industry"?

16                     Are you aware of that?

17          A     I don't recall that specific note in the  
18     annual report.

19          Q     Now, if you will just look at Page 10, you  
20     refer to traffic diversions by SP as a result of the  
21     UP-MP-WF consolidation. Do you see that?

22          A     You are referring to where the ICC found that  
23     SP would sustain an annual diversion of \$70 million in  
24     1979 dollars?

25          Q     Right. And then you say, "We believe the

1 Commission's finding was short of the mark." Do you see  
2 that?

3 A We anticipated it was \$70 -- \$100 million.

4 Q Now, are you aware of the figures put in the  
5 application or I should say in a verified statement in  
6 support of the application in this case which projects --

7 A This case is referring to the UP-McP?

8 Q No, I am talking about in this current  
9 proceeding. Let me start the question over again.

10 Are you aware there is a verified statement  
11 that has been filed by Santa Fe and Southern Pacific  
12 which estimates the diversions which Southern Pacific  
13 would have incurred as a result of the UP-MP-WF  
14 proceeding, UP-MP-WF proceeding based on 1982 revenues?

15 MR. STEPHENSON: Mr. Baker, what are you  
16 referring to?

17 BY MR. BAKER: (Resuming)

18 Q This is the verified statement of Mr. Beyff.

19 A I know he is one of our witnesses. I have  
20 reviewed his testimony. I don't remember that  
21 particular point.

22 Q If I were to say to you that his testimony  
23 indicates that based on 1982 revenues Southern Pacific  
24 would have lost \$55.9 million of revenue, would you say  
25 in your opinion that that understates the net diversions



1 due to that merger?

2 A I have no basis of knowing whether that is  
3 right or wrong. I have not reviewed his working papers,  
4 his process, or how he derived that result, so I really  
5 don't know.

6 Q It is less than the \$70 million that is shown  
7 in the middle of Page 10, isn't it?

8 A The figure you just quoted is less than \$70  
9 million.

10 Q Now, the figure on Page 10 is based on '79  
11 revenues. The figure I just quoted is based on 1982  
12 revenues. Let me ask you the question, were 1982 freight  
13 revenues per revenue ton mile generally higher or lower  
14 than in 1979?

15 A I don't have the papers, supporting papers  
16 right here, but my assumption being, and it can be  
17 verified, that the total revenues in '79, revenue per  
18 ton mile or revenue per car mile, would have been higher  
19 than in 1980.

20 Q You think you were higher in '79?

21 A What I am trying to figure out is '79 versus  
22 '80. That is before Staggers, before rate indexing. It  
23 depends on how much competition was involved there. We  
24 are still under the jurisdiction of ratemaking with the  
25 ICC. So the best answer is, let the record say what it

1 is.

2 Q All right. One last area, Mr. McNear. I  
3 would like you to turn to Page 13. Actually, it may be  
4 helpful to you to look at the bottom of Page 12 first,  
5 because what I am talking about or going to ask you some  
6 questions on is the paragraph that begins at the bottom  
7 of Page 12 and runs over to the top of Page 13.

8 A Talking about our shippers?

9 Q Yes, sir.

10 A Yes, sir.

11 Q Now, you see in the second full sentence on  
12 Page 13 you say, "Although it is true that a few  
13 shippers at SPT Santa Fe common points will see their  
14 rail transportation options reduced many times that  
15 number are today dependent on SPT for rail service."

16 I left out a few words, but you see that,  
17 don't you?

18 A Yes, sir.

19 Q How many shippers can be served by both SF and  
20 Santa Fe at points where those two railroads are the  
21 only two competing railroads?

22 A You are putting that question another way.  
23 How many shippers will be left with just the combined  
24 Santa Fe Southern Pacific?

25 Q We will go from two to one exactly.

1           A       In rough numbers, it is about 4,000 shippers,  
2 and that is compared to our 20,000 single served  
3 shippers on Southern Pacific -- no, pardon me. Pardon  
4 me. It is about 2,500, 2,500 -- 2,500 that will be  
5 additional shippers who will only have one railroad  
6 servicing, whereas today Southern Pacific, as I indicate  
7 on the bottom of Page 12, has some 20,000 shippers that  
8 are exclusively served by us, and it is my understanding  
9 that Santa Fe has some 4,000 shippers exclusively  
10 served.

11           Q       And how did you arrive at the 2,500 number?

12           A       That is through our staff group, and looking  
13 at those points such as the Phoenix area, some of the  
14 stations in the San Joaquin Valley, and other specific  
15 points where there are the two railroads and there would  
16 only be the combined railroad.

17           Q       And you included all shippers located at those  
18 common points? Is that what you did?

19           A       I believe so. I can tell you if it is  
20 different, but that is my understanding.

21           MR. STEPHENSON: We can provide that for you.  
22 That is something we just recently got.

23           BY MR. RAKER: (Resuming)

24           Q       Thank you.

25                   How many -- Now, you used the term in that

1 sentence "shippers today dependent on SPT for rail  
2 service." What is that number?

3 A That is about less than tenfold. That is the  
4 ratio of our current 20,000 to the 2,500 additional  
5 shippers, if I understand your question.

6 Q All right. What you are saying is that the  
7 20,200 shippers exclusively served by SP, those are  
8 shippers dependent on SP for rail service. Is that what  
9 you are saying?

10 A That is one option of the transportation  
11 needs.

12 Q Yes. Now, if you will just go over to Page  
13 16 -- actually, I am talking about the sentence that  
14 begins at the bottom of Page 15 of your verified  
15 statement.

16 You talk about the ways in which direct rail  
17 competition will exist after the merger, and you will  
18 note that at the top of Page 16, one of those methods is  
19 referred to as TOFC access.

20 I take it that you concluded for some reason  
21 that TOFC access is not available to any of the 20,200  
22 exclusively served shippers. Is that right?

23 A If that is your reading of it. That certainly  
24 isn't the intent, because a lot of the 20,000 shippers,  
25 a good percentage of them would be along our coastline

1 between San Francisco and Los Angeles, and there are  
2 trucks, the Salinas Valley. That would be that, the  
3 perishable. We are getting competition from the UP and  
4 the Santa Fe, and truck competition by piggyback coming  
5 in there right now.

6 Q That is my confusion. That is why I asked you  
7 the question. When you say -- I asked you how many  
8 shippers are dependent on SP for rail service, and you  
9 seemed to say to me, well, it is all the shippers that  
10 are located at points exclusively served by SP.

11 A We have got 80,000 total shippers, if you are  
12 looking at our total shippers.

13 Q Eighty thousand total shippers at points  
14 exclusively served by SP?

15 A No, no, 20,000.

16 Q You have got 20,000 at points exclusively  
17 served by SP, correct?

18 A Yes.

19 Q How many of those shippers do not have  
20 available to them competition by other railroads via  
21 TOFC service?

22 A I would say not many, and the basis for that,  
23 just thinking over it geographically, we have got our  
24 shippers on our routes in Oregon, our lumber shippers,  
25 and today we are seeing lumber shipped or transported to

1 points on the BN and piggybacking out of the area.  
2 Another exclusive area for lumber shipping is on the  
3 Northwestern Pacific.

4 We have seen Santa Fe trailers come in there  
5 and go over to their terminal at Richmond. I have  
6 already mentioned the coast route, the perishable  
7 shippers, and then out of the Santa Barbara down there  
8 on the farther end there going into Los Angeles.

9 The one area where I have a little difficulty  
10 in seeing truck or TCFC substitution is in, for example,  
11 a mine to mouth copper haul in Arizona or New Mexico,  
12 and I can't really find a substitute there, but let me  
13 say this. If the price gets out of range, they are not  
14 adverse to putting in their own trucks.

15 Q All right. Now, let me ask you about another  
16 phrase that you have back on Page 13. You notice that  
17 in the very first sentence on the page you say "Some,"  
18 referring, I believe, to you 20,200 shippers at  
19 exclusively served points, "Some are totally dependent  
20 on SPT for transportation service." Why are other modes  
21 not available to them?

22 A I think in focusing on that sentence it is  
23 just the comment that I just made of some of these  
24 shippers in Arizona where today I would say they are  
25 totally dependent on us because they aren't going to

1 another mode.

2 If conditions come up, they do have the option  
3 if the costs are less. Their total transportation costs  
4 and service package are more beneficial to them than the  
5 other mode.

6 Q So in other words, if SP were to fail, let's  
7 say -- let's say SP were to go out of business. These  
8 people really aren't going to be hurt, are they?

9 A They would have to readjust their operations.  
10 They would be without a choice, and I think there have  
11 been a lot of questions pointed to me of choice of  
12 opportunity.

13 Q So you are agreeing now competition is pretty  
14 important, isn't it?

15 A There is a lot of competition.

16 JUDGE HOPKINS: Excuse me, Mr. Baker. Do you  
17 have any more?

18 MR. BAKER: I think one or two more questions,  
19 Your Honor.

20 JUDGE HOPKINS: Good. Let's finish.

21 BY MR. BAKER: (Resuming)

22 Q When you speak about motor carrier  
23 competition, Mr. McNear --

24 A Yes, Mr. Baker.

25 Q -- is it your view that motor carriers provide

1 effective competition today at the same level of rates  
2 that are charged by the SP?

3 A Not necessarily.

4 Q Higher rates?

5 A In some instances.

6 Q So in that sense motor carrier competition  
7 then does not discipline the market in terms of rates.  
8 Is that correct?

9 A The shipper in making his selection on what  
10 mode of transportation is looking at the total  
11 transportation package and its cost to him in doing  
12 business, and part of that is the direct rate of the  
13 transportation. The other portion of it is his money  
14 tied up in investment inventory.

15 And for that reason -- and I guess that's the  
16 reason that we see so much lumber and other commodities  
17 that you would normally think would be on the railroad  
18 going transcontinentally out of our territory or coming  
19 into our territory that are on the highway, instead of  
20 taking the low cost, rail cost of, say, piggyback  
21 service.

22 MR. RAKER: That is all I have, Your Honor.  
23 Thank you, Mr. McNear.

24 JUDGE HOPKINS: Let's take a 15-minute  
25 recess.



1 MR. KHARASCH: I would request at some time  
2 before Mr. McNear gets off the stand that we have a  
3 bench conference of lawyers.

4 JUDGE HOPKINS: Surely.

5 MR. STEPHENSON: I would just as soon do it  
6 now.

7 (Whereupon, a brief recess was taken.)

8 JUDGE HOPKINS: Let's come to order.

9 We would like to get this gentleman off some  
10 time today.

11 Mr. Prettyman, are you going to be next?

12 CROSS EXAMINATION

13 BY MR. PRETTYMAN:

14 Q Mr. McNear, I am Barry Prettyman representing  
15 the Rio Grande.

16 A Good morning, Mr. Prettyman.

17 Q Do you agree with Mr. Schmidt that the  
18 Southern Pacific is going to go out of business if it  
19 doesn't get this merger?

20 MR. STEPHENSON: I am sorry. I didn't hear  
21 the question. What about go out of business?

22 BY MR. PRETTYMAN: (Resuming)

23 Q That the Southern Pacific is going to go out  
24 of business if it doesn't get this merger.

25 A Let me address my concern and how it reacts to

1 Mr. Schmidt's concern.

2 Q Let me suggest that you say whether you agree  
3 with him or not, and then you can explain your answer.

4 A Yes, I do.

5 Q Now, do you want to explain?

6 A Elaborate? Probably a little bit in the  
7 explanation is referring for the record to Page 11 of my  
8 testimony, where I talk about the past record of  
9 Southern Pacific Transportation Company, focusing on the  
10 income from operations from 1973 to 1982, net working  
11 capital as of the end of the year for the same period,  
12 and then from that and the bottom of Page 12, that  
13 addresses the question of what I think the future holds  
14 for our company.

15 If you look at the trends that are given on  
16 Page 11, it shows that since the -- and once again, as  
17 we discussed earlier today, this is on depreciation  
18 accounting -- I will try to bridge that also -- that  
19 since '76, '77, really, we have been in a down mode,  
20 reflecting the economy, the shrink in the economy, '80,  
21 '81, going from an income of operations from 145 million  
22 in 1977 to a loss of 69 million, which again is on the  
23 betterment accounting basis in 1982.

24 For the record, the results for 1983 for  
25 Southern Pacific Transportation was a minus 143 million,

1 and as far as our first half of this year that is made  
2 public, we are slightly plus, but now I will transfer  
3 the 143 million 1983 was betterment accounting equated  
4 to depreciation accounting. That would be approximately  
5 1.9 million loss.

6 For the first half of this year, we have shown  
7 a slight profit of 35 million, but the real concern, and  
8 where this comes in answer to your question is, if you  
9 look more over at the working capital sheet, and you see  
10 that back in '76, '77, it was positive, above 100  
11 million, shrinking down until a minus 154 million in  
12 1982, taking away the benefit effect of 150 million  
13 contribution that was given to Southern Pacific  
14 Transportation Company from SPCo. in October, 1983.

15 So you can look at this trend without that  
16 transfusion in 1982. At the end of '82, it was 154  
17 million negative. At the end of 1983, without the  
18 benefit, it was 193 million negative. And at the end of  
19 six months it was 219 million negative.

20 So -- and these are the figures that Mr.  
21 Schmidt was referring to. He gets these financials.

22 MR. PRETTYMAN: Your Honor, I move to strike  
23 that. He can't testify what Mr. Schmidt was  
24 testifying.

25 JUDGE HOPKINS: He doesn't want to follow

1 through with that answer anyway. He has stopped. I  
2 will allow the motion to strike that part.

3 THE WITNESS: All right. So then, with that  
4 background, looking at what the statistics are and what  
5 are our trends -- I think your question is, what is the  
6 outlook for Southern Pacific Company and when, and I can  
7 say that we have not made any studies to date as to when  
8 and if Southern Pacific would go into bankruptcy, or  
9 what point in time.

10 Certainly we are very -- looking anxiously for  
11 a very positive decision by this Commission, and I can  
12 say right now that, and as I have indicated in my  
13 December affidavit, that looking at the period that we  
14 anticipate that it would take the Commission to hear  
15 this case and make its decision, our target date was the  
16 end of December, 1985, that it is still my opinion that  
17 unless we get some major strikes or anything else -- we  
18 are glad General Motors was settled -- that we can meet  
19 and be retained as a financially viable, competitive  
20 railroad during the process through 1985.

21 However, just looking at the picture and  
22 projections of our working capital and where they are  
23 now, it may be that during the first half of 1985, which  
24 traditionally for our carrier has been the cash drain  
25 months, that we may have to call upon some of our bank

1 balances to tide us over temporarily.

2 Then the question is after '86, what goes  
3 after '86? After January of '86, our company faces a  
4 \$28 million debt retirement, so we have to face that.  
5 As trying to project how soon in '86 or the years after,  
6 as to how long we can continue as a financially viable,  
7 competitive carrier, without really selling off bargain  
8 basement our other assets -- we have some \$500 million  
9 of lands and others that are not in the productive  
10 operation of our railroad, but that is not desirable.

11 So all I can say is that my projection of the  
12 financial viability and the capability of Southern  
13 Pacific Transportation Company to remain a viable  
14 carrier independently, my projection is much shorter  
15 than Mr. Schmidt's, and I read in the paper some  
16 economists indicating maybe some recessions in 1977 --  
17 '87 or '88.

18 If that comes to pass, that would shorten up  
19 my perspective.

20 BY MR. PRETTYMAN: (Resuming)

21 Q So if I understand your answer, I think you  
22 will remain in business until the Commission decides the  
23 case, but if you don't get -- if the merger doesn't go  
24 through, you will go under very shortly thereafter?

25 A As I have tried to indicate, there are

1 certainly trends dictating that. I can't say exactly  
2 how short, but it is in a short period of time.

3 Q When did you reach this conclusion?

4 A I think this conclusion of the necessity of  
5 the Southern Pacific Transportation, the rail properties  
6 to be -- to be merged or find another solution to the  
7 current trends, this came about in 1980, and as a  
8 company policy with Mr. Biaggini before me and myself, I  
9 near, this has been a corporate objective as far as for  
10 the railroads of seeking a solution.

11 Q So you decided in 1980 that absent this merger  
12 or a merger of this type, that you would go under?

13 A Something had to change, right.

14 MR. PRETTYMAN: You knew that back in '80.

15 Your Honor, I have marked for identification  
16 DFGW-C-2, an affidavit of Mr. McNear's and accompanying  
17 attachments.

18 JUDGE HOPKINS: That will be marked for  
19 identification.

20 (The document referred to  
21 was marked for  
22 identification as Exhibit  
23 Number DFGW-C-2.)

24 BY MR. PRETTYMAN: (Resuming)

25 Q Tell us what this is, Mr. McNear.

1           A     This is an affidavit that I tendered to the  
2 United States District Court for the District of  
3 Columbia. This was prepared in response to the  
4 questions raised by the Union Pacific as we were  
5 attempting to close the merger of the Santa Fe  
6 Industries and the Southern Pacific Company in the  
7 latter part of December, 1973, and the Union Pacific  
8 made allegations --

9           Q     I just wanted you to identify the document.  
10 You don't have to explain it.

11           A     Look on Page 21 of your affidavit. This  
12 affidavit is dated December 7th, 1983?

13           A     Yes, sir. Page what?

14           Q     Page 21.

15           A     Twenty-one?

16           Q     Uh-huh. Let me read Paragraph 15. "SPT has  
17 adopted an aggressive yet realistic business plan for  
18 1984 under which it will remain strong and competitive.  
19 Execution of that business plan will place SPT in a  
20 sound competitive position going into 1985 and  
21 thereafter."

22           A     Is that your testimony?

23           A     Yes, sir, that is.

24           Q     Look over to Exhibit 8, which is right at the  
25 end of that document.

1 Have you found it?

2 A This is my memorandum of December 8th to all  
3 Southern Pacific Transportation Company employees?

4 Q Yes, sir. Look on Page 2 of that, the second  
5 paragraph. "I want to reemphasize that SPT faces the  
6 future as a strong and viable competitor. Its business  
7 plan for 1984 is competitive and realistic." Is that  
8 what you said?

9 A That's what I said.

10 Q And you meant that then?

11 A Yes.

12 MR. PRETTYMAN: Your Honor, I have marked for  
13 identification DRGW-C-3, which is a four-page document.

14 JUDGE HOPKINS: It will be marked for  
15 identification.

16 (The document referred to  
17 was marked for  
18 identification as Exhibit  
19 Number DRGW-C-3.)

20 BY MR. PRETTYMAN: (Resuming)

21 Q Tell us what this is, Mr. McNear, because it  
22 doesn't seem to be from anybody to anybody on the face  
23 of it. It is entitled Southern Pacific Transportation  
24 Company's Response.

25 A Give me a minute to review it here and see



1 whether I can focus on where it came from.

2 MR. PRETTYMAN: Sure.

3 Your Honor, I should say that the markings  
4 unfortunately are mine. They were not in the document.  
5 They should not be --

6 JUDGE HOPKINS: The emphasis points?

7 MR. PRETTYMAN: Yes, sir. It is not part of  
8 the original document.

9 MR. STEPHENSON: This points out the benefit  
10 of the notification plan, which was not followed in  
11 regard to this document. We don't know where the  
12 document came from or what it is, and these kinds of  
13 things can be shortcutted if you provide the documents  
14 in advance.

15 MR. PRETTYMAN: I didn't know until late last  
16 night, Your Honor, that I was going to use it today.

17 JUDGE HOPKINS: And you don't know where you  
18 got it? You got it in discovery?

19 MR. PRETTYMAN: Yes, sir, and also I believe  
20 we also got it from a shipper.

21 THE WITNESS: This is the first time I have  
22 seen this document, to my recollection, so proceed if  
23 you have any questions on it.

24 BY MR. PRETTYMAN: (Resuming)

25 Q It would appear since it comes from your file

1 and since it is entitled Southern Pacific Transportation  
2 Company's Response that it comes from Southern Pacific,  
3 wouldn't you say?

4 A We can draw that conclusion, yes.

5 Q Do you know whether it was addressed to  
6 shippers?

7 A I have no idea. That was going to be my  
8 comment. In response to whom? I don't know.

9 MR. STEPHENSON: Your Honor, if it would help,  
10 and I can say it unless you want it, but Mr. Smith knows  
11 a little more about this than I do. He can tell you  
12 what it is.

13 JUDGE HOPKINS: He is one of the attorneys of  
14 record, so if he can, let's have him tell us. Mr.  
15 Smith?

16 MR. SMITH: This document was in our document  
17 depository as material that was related to  
18 communications with shippers, and this appears to be a  
19 document that was put out by Southern Pacific to various  
20 shippers in response to a white paper of some sort that  
21 the Union Pacific had been circulating in opposition to  
22 the coming merger.

23 MR. PRETTYMAN: Thank you. That is helpful.

24 BY MR. PRETTYMAN: (Resuming)

25 Q This says on Page 2, Mr. McNear, in the part

1 that I have underlined, "Financially, SPT is and has  
2 been for many years independent and standing on its own  
3 feet." Correct?

4 A That's what the statement says.

5 Q And Page 3, "SPT is better prepared to provide  
6 excellent service to its customers than it has been in  
7 recent years." Correct?

8 A Correct.

9 Q And Page 4, "SPT has positioned itself for  
10 profitable future growth by improving its route  
11 structure, providing improved service that is  
12 competitive, and realizing significant gains in  
13 transportation efficiency." Correct?

14 A That's correct.

15 Q And this had to have been put out, if Mr.  
16 Smith is correct, fairly recently, if it is in response  
17 to a UP contention that relates to this merger.

18 MR. STEPHENSON: No, the holding company  
19 merger back in 1983.

20 MR. PRETTYMAN: Okay, 1983.

21 THE WITNESS: Let the record show whatever  
22 counsel has agreed to.

23 BY MR. PRETTYMAN: (Resuming)

24 Q I believe you said you heard Mr. Schmidt's  
25 testimony of two days ago. Do you agree with him about

1 the advantages of single line service? Do you remember  
2 his testimony in regard to the number of advantages of  
3 single line service?

4 A I remember it.

5 Q Do you agree with those statements that he  
6 made?

7 A I don't remember each one individually, but I  
8 agree with the concept and what he said at that time?

9 Q You say at the top of Page 3 of your testimony  
10 that customers and communities will benefit from, and I  
11 quote, "more direct routes in many areas." What areas  
12 are you referring to there?

13 A What I am specifically referring to there is  
14 that with the merger of the Atchison and the Southern  
15 Pacific, that the Southern Pacific customers will have  
16 direct access to Chicago and in return the Atchison  
17 customers will have direct access to points like St.  
18 Louis, Memphis, and New Orleans.

19 Q Did you have in mind any areas in California,  
20 Oregon?

21 A The Santa Fe customers once again would have  
22 direct access to Portland, Oregon, for example. Yes.

23 Q Well, what areas did you have on mind up on  
24 the west coast?

25 A For the Santa Fe shippers?

1 Q Yes.

2 A It would be there. It would also be, for  
3 example, Santa Barbara, Watsonville.

4 Q Everything north of San Francisco?

5 A North of Sacramento.

6 Q North of Sacramento. Excuse me.

7 A The Santa Fe gets to Sacramento.

8 Q Is that what you had in mind?

9 A That would be included.

10 Q You refer in the footnote on Page 7 to 18  
11 through trains a day interchanged by SP and the Rock  
12 Island at Tucumcari. When was that?

13 A I am not sure of the date. That was -- the  
14 source of that was Bill Honig, who was formerly vice  
15 president of operations of the Rock Island, and I think  
16 he is currently our vice president of purchasing, has  
17 been an operating officer for us. The 18 train is his  
18 projection.

19 My own recollection back in 1955 when I was  
20 train master at Tucumcari when the Rock Island was a  
21 viable interchange with us at that point, that we were  
22 running as many as probably 12 trains a day in both --  
23 combined in both directions.

24 Q I am just trying to pin down the time. That  
25 is in the fifties, the mid-fifties?

1           A     I couldn't say. I couldn't honestly say. I  
2     don't know whether the work papers -- or we can find out  
3     that specific thing. I think our lawyers can, if it is  
4     necessary.

5           Q     How many through trains do you run through  
6     there today?

7           A     We are averaging over eleven trains a day each  
8     way.

9           Q     Thank you.

10          A     Pardon me. Totally eleven trains combined  
11     directions.

12          Q     Should I understand you to say, Mr. McNear, on  
13     Page 18 that Rio Grande is only a theoretical  
14     beneficiary of the Central Pacific conditions because  
15     the business it gets from SPT is really due not to those  
16     conditions but to the SPT-Rio Grande solicitation  
17     agreement?

18                     Is that what you are saying?

19          A     In actuality, it goes on beyond theoretical.  
20     We are still under the conditions of the CP agreement.

21          Q     Yes. But you are saying that we are only a  
22     theoretical beneficiary because in fact the business is  
23     coming to us under the agreement and not under the  
24     conditions.

25                     Is that what you are saying here?

1           A     I don't quite understand the differentiation  
2 you are making there.

3           Q     Well, I am just trying to understand what you  
4 are saying. What do you mean by it?

5           A     I am trying to interpret what I have said  
6 there, too.

7           Q     Yes, I would like you to do that.

8           JUDGE HOPKINS: Take your time and read it.

9           THE WITNESS: I would say that the D&RG  
10 through our voluntary operating agreement is receiving  
11 more traffic over the Caden gateway today than would  
12 necessarily be prescribed to in the CP conditions.

13           BY MR. PRETTYMAN: (Resuming)

14           Q     Then we are benefitting from the conditions?  
15 So it is not a theoretical beneficiary? We are an  
16 actual beneficiary.

17           A     You are an actual beneficiary.

18           Q     I see. And in addition to that, we are  
19 getting additional business through the agreement?

20           A     That is correct.

21           Q     Right. And you say that in due course you  
22 will petition the Commission for removal of those  
23 conditions. Of course, you have actually done that,  
24 haven't you?

25           A     That is correct.

1 Q And in fact the Commission has reopened that  
2 case.

3 A They have reopened that case. They have  
4 denied it being included in this case, and they have  
5 also asked as a matter of record our agreement with the  
6 DERC.

7 Q And you say -- you said in your application to  
8 remove those conditions that any carrier intending it  
9 would be adversely affected could seek hearing in this  
10 proceeding, did you not?

11 A If that is what the language says, I will  
12 accept it.

13 Q Tell us a little bit about this agreement. Is  
14 it cancellable by either party?

15 A I believe the agreement's term is through some  
16 time in 1986. There is, as in most agreements of this  
17 type, a 30 or 60 day cancellation notice. We have also  
18 indicated in our application for the removal of the CP  
19 conditions that we will continue this agreement until  
20 that -- until after this case is decided.

21 Q The agreement itself provides that it is  
22 cancellable, but you are saying that you have given an  
23 assertion that it will continue until this case is  
24 decided?

25 A I believe that is the timing.



1 Q What are you referring to there,  
2 incidentally? Are you referring to when the Commission  
3 decides -- Excuse me. May I continue?

4 A Excuse me.

5 Q Are you referring to when the Commission  
6 decides the case, or when it gets through the courts, if  
7 it goes to the courts? Or what are you talking about?

8 A I don't know legally what date that would be.

9 Q I am not asking you legally. Excuse me, Mr.  
10 McNear. Let me finish my question.

11 What I am asking for, you gave a voluntary  
12 assertion to the Commission --

13 A That's right.

14 Q -- that it would remain in effect until the  
15 end of the proceeding. What did you mean?

16 A What I mean by that, it will remain in effect  
17 until the end of the proceeding, and it is beneficial to  
18 both parties that it remain in effect until we know what  
19 the decision of the Commission is.

20 Q My question is, do you mean that it will  
21 remain in effect until the Commission decides this case,  
22 or until the case is finally decided in the courts if it  
23 goes to the courts?

24 A I don't have any disagreement to having it  
25 stay in effect until after the Commission has made its

1 decision. That's my meaning of it.

2 Q So you are saying now on the record that it  
3 will remain in effect until the courts are through with  
4 the case?

5 A I would have to qualify that if conditions are  
6 imposed upon the merger. We would have to look at those  
7 conditions before agreeing to court, because you may get  
8 into operating with certain conditions imposed, and then  
9 it is in the court for final jurisdiction.

10 Q Right. So you may cancel it as soon as the  
11 Commission decides, depending upon what the conditions  
12 are.

13 A That would be my intent, yes.

14 Q And in any event, you are not giving any  
15 assurances about that agreement beyond that, are you?

16 A I am not in a position to.

17 Q That is right. You will not be the one to  
18 decide, will you?

19 A No. Mr. Cena responded to that question  
20 yesterday.

21 Q Mr. Cena and Mr. Schmidt will decide that.

22 JUDGE HOPKINS: Did you say yes, for the  
23 record?

24 THE WITNESS: Yes.

25 BY MR. PRETTYMAN: (Resuming)

1 Q Your diversion study assumed that the Central  
2 Pacific conditions would not be in effect after the  
3 merger, did they not?

4 A Referring to Page 18 now?

5 Q No, I am referring to your diversion study.

6 A Yes.

7 Q What did your diversion study assume in regard  
8 to the SPT-Rio Grande solicitation agreement?

9 A I don't know.

10 Q Well, don't you think that would make a  
11 difference, Mr. McNear, in view of your testimony that  
12 this agreement is so important?

13 A I don't know whether it did or didn't. You  
14 can ask the people that looked at that detail. I would  
15 assume it would, but I can't say here.

16 Q You would call that detail?

17 A That's the word I used.

18 Q Were you involved in the decision to engage  
19 Morgan Stanley to advise the SF in connection with the  
20 possible Santa Fe-SP merger?

21 A No, sir.

22 Q Do you have any idea when they were retained?  
23 Who did decide to retain them incidentally?

24 A That was Mr. Biaggini, the chief executive  
25 officer of the Southern Pacific Company.

1 Q Do you know when they were retained?

2 A I can't recall.

3 Q Did you work with the Morgan Stanley group at  
4 all?

5 A What is your definition of work with?

6 Q Well, did Mr. Sieger report to you at all in  
7 the course of his evaluation study?

8 A Who?

9 Q Sieger.

10 A During the study, as a part of senior  
11 management I sat in on review sessions that Morgan  
12 Stanley would conduct with Mr. Piaggini and the other  
13 senior members of our corporation. I would sit in on  
14 those meetings.

15 Q Did you supply any information to him?

16 A I don't know whether I specifically supplied  
17 information, but they were seeking information from our  
18 company as well as other sources.

19 Q Are you aware that in October of 1983 Solomon  
20 Brothers assigned a stand alone value to the SP Railroad  
21 of a negative \$200 million?

22 A I believe that I have seen that figure.

23 Q And are you aware of the fact that Morgan  
24 Stanley assigned a value to the railroad of from \$571  
25 million to \$852 million?

1           A       Once again, I am aware there was a big spread  
2 between two different investment bankers coming to a  
3 point in time of what was the value for both of their  
4 clients.

5           Q       Are you aware that they met in July or August  
6 of '83 and tried to reach an agreement, and that they  
7 couldn't agree?

8           A       I cannot verify that. They may or may not. I  
9 think they were there. Whether they met or not I don't  
10 know.

11          Q       Which opinion did you agree with?

12          A       On the valuation of the company?

13          Q       Uh-huh.

14          A       Neither one of those.

15          Q       Neither one? You had your own?

16          A       My opinion was, as we had determined back in  
17 1980, and looking at it from my position in the  
18 railroad, that a merger was an appropriate step to merge  
19 the railroads, and as far as what were the values and  
20 what was the final negotiated price that Mr. Schmidt and  
21 Mr. Biaggini decided upon, I concurred in the realm of  
22 reasonableness of where they were looking, and then it  
23 is just a matter of what finally they came up with,  
24 which they did.

25          Q       Well, what I am asking you is your own view of

1 the value of the railroad during this period. What  
2 position did you hold at this time?

3 A 1983?

4 Q Yes, sir.

5 A Chairman.

6 Q All right. You had one view of minus \$200  
7 million, and had another view of from \$571 to \$852  
8 million. Where did you come in?

9 A I hadn't prepared any study.

10 Q I know you didn't prepare something, but your  
11 view as chairman.

12 A It would be more than that.

13 Q More than what?

14 A Those figures.

15 Q More than \$852 million?

16 A Sure.

17

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1 Q How much more?

2 A There's many ways of valuating our property,  
3 and I just feel that it's more than \$150 million

4 Q Have you considered the possibility of selling  
5 all or part of the SPT to anyone other than the Santa Fe  
6 within the last ten years?

7 A I have not.

8 Q I mean management.

9 A Management. Yes.

10 Q To whom?

11 A Mr. Biacchini had some conversations with the  
12 Burlington Northern.

13 Q When was that?

14 A I would say some time between 1980 and 1983.

15 Q What happened in those discussions?

16 A No accord was reached.

17 Q And anybody else? Now, you understand, I'm  
18 happy to have the testimony about the discussions, but  
19 I'm not asking you whether you necessarily had  
20 discussions with other parties. I'm asking whether  
21 management considered the possibility of the sale of the  
22 railroad to another party, other than the Santa Fe.

23 A Yes.

24 Q To whom?

25 A We had an ongoing study looking at various

1 possibilities.

2 Q Tell us what they were.

3 A They would be looking at east or west of the  
4 river, and within the West.

5 Q Who in the East?

6 A They would be the carriers in the East.

7 Q You mean all of them?

8 A We considered whether that would be advisable,  
9 to look at joining either -- ConRail was looking for a  
10 home, you had Chessie and CSX. And really, when we  
11 looked at east of the river with ConRail, there would be  
12 a lot of competition, and really we saw in our own  
13 opinion that it would be better for ConRail to stay  
14 independent. That was our evaluation.

15 As far as CSX --

16 Q Excuse me. But you didn't want to do ConRail  
17 because you'd face a lot of competition.

18 A And we felt it was better structured for three  
19 carriers to remain in the East, as three regional  
20 carriers in the East.

21 Q Why would that be?

22 A Because, looking at a future merger of our  
23 property in the West, then you're really getting down to  
24 a balance, which I've also represented in my testimony,  
25 of three major eastern and three major western



1 carriers.

2 Q That's a better balance?

3 A That's right.

4 Q What about in the West? Who are you talking  
5 about?

6 A As I indicated, we looked at, once again,  
7 building up a major merger either with the Santa Fe or  
8 the Burlington Northern, and, whether your client, the  
9 D&RC, whether it fits in one or the other or what-not.

10 Q Well, tell us about that. What did you think  
11 about that?

12 A Our thoughts were that after the decision in  
13 the Missouri Pacific-UP consolidation, that with the  
14 agreement that we entered with them, we at Southern  
15 Pacific for the present were utilizing the efficient  
16 routes, and working together as friendly connections  
17 over Ogden to our best mutual interest.

18 Q So that's why you didn't merge?

19 A At that time, yes, right. The price was too  
20 high, too.

21 Q Anybody else in the West?

22 A I think that's it.

23 Q Did you ever study or make a valuation of the  
24 possibility of selling off segments of the railroad to a  
25 third party?

1           A     The direct answer would be no. One  
2     qualification would be in branch line abandonments,  
3     which would be a segment of our property, and our  
4     proceedings for that abandonment would look at  
5     liquidation, net liquidation value.

6           Q     I take it from your testimony this morning,  
7     Mr. McNear, that you thought that SP was more than  
8     justified in the UP-MoP-WP case in being alarmed at the  
9     impact on the SP of that merger?

10          A     I don't quite follow your question there.

11          Q     I take it from your testimony that you felt  
12     the SP was entirely justified in the UP case in being  
13     alarmed, being seriously disturbed about the impact of  
14     that case upon the SP?

15          A     Yes.

16          Q     And has that merger in fact harmed SP?

17          A     Yes, it has.

18          Q     In fact, you called the Commission's approval  
19     of that merger "the most devastating blow," which  
20     "created a competitive threat to SPT unparalleled by any  
21     rail consolidation in history," did you not?

22          A     Is that my quote or Mr. Biaggini's?

23          Q     Yours.

24          A     Sure.

25          Q     And I believe that your own projected loss

1 that you asserted in that case was some \$105 million?

2 A What page are you referring to?

3 Q I'm referring to your position in the UP  
4 case.

5 A It was somewhere over \$100 million, I recall.

6 Q Right, and that was based on a study of, I  
7 think, 1979 revenues?

8 A I don't recall the year that the traffic study  
9 was based on.

10 Q Do you recall whether your operating revenues  
11 in 1979 were on the order of \$2.223 billion?

12 A That sounds reasonable. I don't recall the  
13 specific.

14 Q So you were complaining about a loss of  
15 something less than five percent of your revenues?

16 A We were more concerned what it was going to do  
17 to the bottom line.

18 Q Okay. Now, is it also fair to say that you  
19 were concerned about the loss of your friendly  
20 connections over the central corridor?

21 A We were really concerned. That's why I think  
22 we said devastating, whatever those words were, because  
23 historically we'd been part and had been long-time  
24 friends.

25 Q Long-time friends with whom?

1 A The Union Pacific.

2 Q And you were concerned?

3 A And before that merger, there was a realm of  
4 possibility that we may ultimately merge with them. But  
5 they chose to go with two other partners.

6 Q Right. And so that was part of your serious  
7 concern, that you were going to lose your friendly  
8 connection with the UP over the central corridor, and in  
9 fact you lost that, didn't you?

10 A But we're still connecting with them in  
11 handling traffic.

12 Q But they give a lot of business to WP that  
13 they used to give to you, is that not right?

14 A That's a fact. And in fact, we have joint  
15 trackage over the -- through Nevada, as you are well  
16 aware, and pre-merger, which would be '79-'80, our car  
17 miles were some 70 percent; after the merger, '82, '83,  
18 it was 65 percent; and for the first seven months of  
19 this year it's down to 60 percent.

20 So that supports your position.

21 Q So that now, as Mr. Schmidt said, you find  
22 yourself encircled by the UP system and the BN system?

23 A And I think I've said it in my testimony, too,  
24 yes.

25 Q Does any analogy occur to you here, Mr.

1 McNear ?

2 A To the regional carriers?

3 Q Uh-huh.

4 A They're all encircled, yes, sir.

5 Q One other question. You referred yesterday to  
6 a Mr. Fitzgerald who was at the meeting last week.

7 Which Mr. Fitzgerald were you referring to?

8 A That must have been Tom Fitzgerald.

9 Q And what is his position?

10 A He's vice president of traffic for the Santa  
11 Fe.

12 Q Thank you.

13 MR. PRETTYMAN: One moment, Your Honor.

14 (Pause.)

15 MR. PRETTYMAN: That's all I have, Your  
16 Honor.

17 JUDGE HOPKINS: Thank you.

18 Who will be next? Mr. Craig?

19 CROSS EXAMINATION

20 BY MR. CRAIG:

21 Q Mr. McNear, my name is Peter Craig. I  
22 represent Amtrak in this proceeding.

23 A Good morning, Mr. Craig.

24 Q Were you here during the questioning of Mr.  
25 Cena?

1 A Yesterday, yes, I was in the audience, yes.

2 Q And did you hear his answers to my questions  
3 at that time?

4 A I heard his answers to your questions.

5 Q Do you agree with what he said?

6 A Yes, and in essence, to paraphrase it, we have  
7 contracts with Amtrak, both of our carriers; they extend  
8 beyond, hopefully, the merger date of this application;  
9 that they will remain in force; and from Southern  
10 Pacific's point, we work closely with Amtrak and will  
11 continue to.

12 And I do follow up on one exception condition  
13 that you asked, and Mr. Cerna said, what would be the  
14 impact of cost, and he didn't make a commitment and I  
15 can't make a commitment. But I can assure you that if  
16 there is any consideration involved in costs, we're  
17 going to certainly sit down and negotiate and probably  
18 will sit down and negotiate a consolidated agreement  
19 after the merger is effective.

20 MR. CRAIG: I have no further questions.  
21 Thank you.

22 JUDGE HOPKINS: Thank you.

23 Ms. Madigan?

24 CROSS EXAMINATION

25 BY MR. DELANEY:

1 Q I'm John Delaney with the Railway Labor  
2 Executives' Association. We just have a few questions  
3 for you, Mr. McNear.

4 My first line of questions concerns the actual  
5 impact on employees in terms of the number of employees  
6 furloughed and transferred, rather than jobs abolished  
7 or transferred. Since you assisted in the preparation  
8 of the merger study, do you know how many employees will  
9 be furloughed and/or transferred as a result of this  
10 proposed transaction?

11 A I don't have the exact numbers on that. It's  
12 in the testimony, and it's even hard to try to get the  
13 direct number from that. And I think Mr. Frestel or Mr.  
14 Peifer representing Southern Pacific Transportation  
15 Company can give you that response.

16 Q Can you confirm that SPT furloughed  
17 approximately 950 employees within the last week or so?

18 A We have taken action to furlough, primarily in  
19 our maintenance department employees, and there is good  
20 reason for that. I don't think anybody objected when we  
21 put these program people on earlier this year to do our  
22 seasonal program work. Now that the programs are  
23 nearing completion, we've taken them off.

24 And also, as I have indicated in my testimony  
25 to Mr. Prettyman, we're concerned of our financial

1 position, and some of that impact has been on where our  
2 cash position is.

3 MR. DELANEY: Your Honor, I'd like to make a  
4 motion to strike that.

5 JUDGE HOPKINS: I'm going to allow it. He was  
6 answering your question. He was just continuing. I'm  
7 leaving it in.

8 BY MR. DELANEY: (Resuming)

9 Q When did you first contemplate these  
10 furloughs?

11 A In the last 30, 60 days. This work was going  
12 to be culminated, and it's just a matter of when we'd be  
13 done. Also, we have had extraordinary work this year  
14 that we hadn't anticipated, some \$36 million for the  
15 maintenance of the Great Salt Lake, which is part of --

16 JUDGE HOPKINS: I'm letting him answer because  
17 then we get a clearer picture of what causes any of the  
18 problems. I'd like to have that in there.

19 MR. DELANEY: All right.

20 THE WITNESS: Because, Your Honor, we had an  
21 unexpected battle against the rise of the Great Salt  
22 Lake, and we put in \$36 million this year on top of what  
23 we did last year. That's \$50 million.

24 BY MR. DELANEY: (Resuming)

25 Q When did you make this decision to furlough



1 the employees, approximately?

2 A Mr. Mohan, our executive vice president, made  
3 that decision and he informed me that he was doing it.

4 Q Mister who?

5 A Mohan.

6 Q When was this decision made?

7 A I don't recall when he made the decision.

8 Q Were any other classes of crafts involved  
9 besides the maintenance of way, carmen, or the  
10 machinists?

11 A Maintenance of way, carmen, machinists. Part  
12 of that group comes into a change in our operation, and  
13 we're constantly changing our operation at Bakersfield,  
14 and we are eliminating our roundhouse back shop  
15 operation there. It was primarily to support our helper  
16 pool over the Tehatchepee Mountains.

17 We have come up with a more efficient way of  
18 doing that, and as a result of that reducing some of our  
19 switching and blocking to reduce the number of trains  
20 that are stopping in Bakersfield. There will also be  
21 some reductions in switchmen and clerical forces in  
22 support of the reduction in that terminal's operation.  
23 That work will be picked up at other locations.

24 Q So you have plans for other furloughs prior to  
25 the merger?

1           A       These furloughs are day to day decisions as  
2 we're meeting the economic conditions and our seasonal  
3 pattern of work, and these are completely unrelated to  
4 the merger. This is just prudent management of the  
5 property.

6           Q       Will you be offering these people protective  
7 conditions?

8           A       Under these furloughs, this is seasonal work.

9           Q       Is that a yes or a no?

10          A       Not to my knowledge.

11          Q       So that these furloughs -- well, were these  
12 furloughs indicated in the Santa Fe-Southern Pacific  
13 labor impact study?

14          A       They are completely independent of this merger  
15 application.

16          Q       Were any of the furloughs caused by closure of  
17 shops?

18          A       Not to my knowledge.

19          Q       Were any of the furloughs caused by traffic  
20 diversions?

21          A       No.

22          Q       Do you have an opinion as to whether the  
23 carriers in their primary and related applications are  
24 requesting that the Commission grant them any exemptions  
25 from any of the Railway labor Act obligations?

1           A     You'll have to ask either Mr. Frestel or Mr.  
2     Peifer that particular question.

3           Q     So I take it that your answer is no?

4           A     I'm not aware of it, so I don't have an  
5     opinion. I think I don't have the facts, so I don't  
6     have an opinion.

7           Q     Do you have any opinion as to whether the  
8     carriers are requesting any exemptions from the  
9     collective bargaining agreements?

10          A     Once again, that's a particular detail that's  
11     within their trade, and they should respond to that  
12     question.

13          Q     What I'd like to know is if you have some  
14     opinion on the subject.

15          A     I don't know what it is, so I can't respond to  
16     your question.

17          Q     So the answer is no?

18          A     Yes.

19          Q     Are there any elements or effects of the  
20     merger control transactions which you think that the  
21     Santa Fe-Southern Pacific could not effect with the  
22     carriers' current RIA obligations?

23          A     I don't know.

24          Q     How about for the collective bargaining  
25     agreement?

1 A Same answer. I don't know.

2 Q The PLEA recently was served with a notice of  
3 exemption in which SPT requested that it be permitted to  
4 relocate a line of railroad by abandoning a portion of  
5 SPT lines and acquiring trackage rights over Santa Fe  
6 and the Sierra Railroad between Stockton and Oakdale,  
7 California.

8 Are you familiar with this request?

9 A I'm familiar they were trying to negotiate  
10 with the Santa Fe to reduce redundancy in some trackage,  
11 branch line trackage, and get rights over their line to  
12 Oakdale.

13 Q So you are familiar with this request?

14 A If that follows and that's the proper  
15 procedure from a labor point. I'm not aware that they  
16 have, but if that's the proper procedure that would  
17 follow.

18 Q Has SPT filed any other such requests for  
19 relocation of trackage?

20 A I don't know whether we have, but I'm sure  
21 that as we continue in our day to day operation, where  
22 there are instances that come up, we will file such  
23 requests on similar situations.

24 Q Who would be able to give me a better answer?

25 MR. STEPHENSON: Mr. Lacy.

1 THE WITNESS: Well --

2 JUDGE HOPKINS: Well, you two argue it out  
3 here. Go ahead. Who do you say?

4 THE WITNESS: Mr. Lacy is one. He's our vice  
5 president of transportation. And my hangup or my delay  
6 in responding to you is not who the individual, whether  
7 we have any currently or what. And he's the man that in  
8 his mind is figuring out how to do these things and he  
9 can respond.

10 JUDGE HOPKINS: Thank you. No argument  
11 there.

12 BY MR. DEIANEY: (Resuming)

13 Q Does SPT have any plans to file such a request  
14 in the future?

15 A As I said, I don't know. You'll have to ask  
16 Mr. Lacy.

17 Q One or two more questions. Will SPT's rail  
18 and motor subsidiaries be using the same reporting marks  
19 as the merged carrier?

20 A You threw me by including the motor carriers  
21 in there.

22 Q Well, let's take them one at a time, then.  
23 Will the rail subsidiaries be using the same reporting  
24 process?

25 A My perception and understanding is that we

1 will be, similar to the BN merger, we will be coming out  
2 with a new single reporting mark for the combined  
3 system. And you had some discussion with Mr. Cena on  
4 the subsidiaries.

5 We have some subsidiaries and there may be  
6 some MWP cars, but you know, they're just about zero.  
7 So our two carriers, Southern Pacific Transportation  
8 Company and the Cotton Belt, SSW, marks, the Santa Fe  
9 marks, we would be in a program to consolidate them for  
10 reporting markings as you visually see them on the side  
11 of the car, and also, more importantly, in our internal  
12 documents for revenue accounting, car flow, car  
13 accounting.

14 Q So as far as the minimum number of cars that  
15 are involved, you really don't have an opinion?

16 A That's right.

17 Q Who would be able to give us an answer on  
18 that?

19 A I guess Mr. Lacy could check the records and  
20 see how many subsidiaries we have that have specific car  
21 markings.

22 Q All right. To the extent of SPT's ownership,  
23 what entity will control SPT's rail and motor carrier  
24 subsidiaries following the merger, to the extent of  
25 SPT's ownership?

1           A     Under the current application in the  
2 proceedings, it's my understanding that SPT and Santa Fe  
3 merge into Southern Pacific-Santa Fe Railway, and the  
4 subsidiaries of their respective would be part of that  
5 organization for the time being. Our trucking  
6 subsidiary as a subsidiary of Southern Pacific  
7 Transportation would be in the new railroad.

8           Q     What entity after the merger is going to set  
9 labor policy concerning the subsidiaries?

10          A     That would be, the ultimate policy would be  
11 through Mr. Cena, the designated chief operating  
12 officer, and where necessary concurrence by Mr.  
13 Schmitt.

14          Q     So we'll be talking with Mr. Cena?

15          A     Sure.

16               MR. DELANEY: That's all we have, Your Honor.

17               JUDGE HOPKINS: How many more? Mr. Roberts,  
18 how long will your questions take?

19               MR. ROBERTS: Ten to 15 minutes.

20               JUDGE HOPKINS: This might be a good time for  
21 the recess. And while we're still here, how many more  
22 have we got? Mr. MacKenzie?

23               MR. MacKENZIE: I've got about 15 minutes.

24               MR. PATNER: Department of Justice has about  
25 20 minutes.

1 JUDGE HOPKINS: And then what about recess?

2 MR. STEPHENSON: About 10, 15 minutes, I'd  
3 say.

4 JUDGE HOPKINS: I'm trying to figure out  
5 whether we could even complete him before we took a  
6 luncheon recess. But if everybody needs a luncheon  
7 recess right now, it might be wise.

8 Are you in a hurry to get out of town?

9 THE WITNESS: I'm at your disposal.

10 JUDGE HOPKINS: I'm just afraid that these  
11 times that we talk about sometimes extent into longer  
12 than they say they're going to be. So I think it would  
13 be better to recess now until 1:30.

14 (Whereupon, at 12:30 p.m., the hearing in the  
15 above-entitled matter was recessed, to reconvene at 1:30  
16 p.m. the same day.)

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## AFTERNOON SESSION

(1:32 p.m.)

1  
2  
3 JUDGE HOPKINS: Back on the record.

4 Mr. Roberts.

5 Whereupon,

6 DENMAN K. McNEAR,

7 the witness on the stand at the time of recess, resumed  
8 the stand and, having been previously duly sworn, was  
9 examined and testified further as follows:

10 CROSS EXAMINATION

11 BY MR. ROBERTS:

12 Q Good afternoon. My name is Barry Roberts and  
13 I represent Sunkist Growers, Inc.

14 Turning to page 3 of your statement, about the  
15 middle of the complete paragraph you make the statement  
16 that any reduction in competition between the Santa Fe  
17 and the Southern Pacific "will be offset by direct  
18 competition from other railroads, trucks, pipelines, et  
19 cetera."

20 Isn't that other competition basically what's  
21 already there?

22 A In the main, it would be the existing  
23 transportation, the total opportunity that the customer  
24 has to satisfy his transportation needs.

25 Q So that the only real change in the

1 competitive picture is going to be the elimination of  
2 competition between the Southern Pacific and the Santa  
3 Fe?

4 A Yes, and I think I testified earlier today you  
5 more or less have three lines. You've got two  
6 railroads, one less railroad, and you still have all the  
7 other competitive forces.

8 Q Now, you refer to the northern lines merger,  
9 and let me make sure I understand your testimony. It's  
10 my understanding that, in response to some earlier  
11 questions, you indicated that you believe the northern  
12 lines -- that is, the Burlington Northern -- has a rail  
13 monopoly in a substantial portion of the territory which  
14 it serves.

15 A I indicated that if you look at the map and  
16 you look at the northern lines, BN system, and how it is  
17 all over the northern tier, and if you look at what  
18 other -- other rail lines, which is your question, then  
19 in some areas in the Dakotas and Montana there is not  
20 other rail carriers.

21 Q So that in some areas the BN, Burlington  
22 Northern, does indeed have a monopoly on rail service?

23 A They would be the single carrier, except for  
24 the limits of piggyback.

25 Q What I don't understand is the relevance of

1 that fact to this proceeding. Let me ask you a  
2 question. Are you trying to tell the Commission that  
3 because the Burlington Northern has a monopoly on rail  
4 service in Montana and the Dakotas, that therefore you  
5 and the Santa Fe should now have a monopoly on rail  
6 service in parts of California and Arizona?

7 A No. What I'm trying to indicate is that if  
8 you look at the map and you look at the geographical  
9 location of the BN lines, you look at the geographical  
10 location of the UP, and you look at the geographical  
11 location of our combined systems, there are some  
12 similarities.

13 Q Now, going on to statements you make on pages  
14 12 and 13 of your statement, in particular the statement  
15 at the top of page 13, the first complete sentence.

16 A Yes.

17 Q "Some" -- and I assume the word "some," I  
18 assume, refers to shippers -- "are totally dependent on  
19 the Southern Pacific Transportation, SPT, for  
20 transportation service." Did I do that accurately?  
21 "Some are totally dependent on SPT for transportation  
22 service."

23 A Yes, sir, for rail transportation service.

24 Q It says "transportation service."

25 A And I think we reviewed that with one of the

1 previous crosses, and I indicated coming to mind the  
2 copper shippers down in Arizona and New Mexico.

3 Q Let me just ask you a general question with  
4 respect to that statement. Has the Southern Pacific in  
5 any proceeding before this Commission conceded that it  
6 has market dominance?

7 A I don't know.

8 Q Now, you were asked a number of questions by  
9 various counsel for connecting carriers, and my  
10 recollection is that yesterday, in response to a  
11 question by counsel for the MKT, you indicated that your  
12 policy on routing is what will be most beneficial to  
13 your customers, the shippers. Did I understand that  
14 correctly?

15 A That's one of the underlying factors.

16 Q Now, as you know, our client Sunkist ships  
17 fresh fruit, a perishable commodity. Would you agree  
18 that perishable commodities would require expedited  
19 handling and that time, transit time, is of major  
20 importance?

21 A By definition, perishable is perishable, and  
22 they require a quick in-transit time, and that's where  
23 we have lost a lot of the perishable business to trucks  
24 that are quicker and to airplanes.

25 Q Now, are you aware that for many years

1 shipments from a good part of the San Joaquin Valley --  
2 and I am referring to Sunkist fresh fruit shipments --  
3 that originated on the Southern Pacific moved over what  
4 you would call the Ogden gateway to Chicago? That is,  
5 SP-UP-C&NW into Chicago. Are you familiar with that  
6 route?

7 A Yes, sir.

8 Q And would you disagree if I were to tell you  
9 that historically we have received reliable seven-day  
10 service from the Southern Pacific on that route  
11 originating on the Southern Pacific into the New York  
12 metropolitan area?

13 A I'll accept that.

14 Q Now, are you aware that as of today Sunkist no  
15 longer has that routing available to it on shipments  
16 originating in the central and northern San Joaquin  
17 Valley?

18 A I am not.

19 Q Are you aware that as shipments must now move,  
20 that the only routing we have available is SP-Cotton  
21 Belt into East St. Louis, ConRail to New York?

22 A I'm not aware of that.

23 Q Now, if I were to tell you that reliable  
24 seven-day service has now gone to a consistent 10 to  
25 12-day service, would that be a matter of concern to

1 you?

2 A My concern would be involved with what our  
3 participation in the joint route would be, that we're  
4 doing our best effort.

5 Q Well, there's no doubt that you get greater  
6 participation in the longer route -- that is, down  
7 through Los Angeles, the southern route, that is,  
8 SP-Cotton Belt into East St. Louis -- than you did when  
9 we routed or when you allowed use to route through the  
10 Ogden gateway.

11 MR. STEPHENSON: I'll object to the question.  
12 It's argumentative. It assumes that we are preventing  
13 him from routing.

14 JUDGE HOPKINS: On that basis, it is a  
15 legitimate objection.

16 BY MR. ROBERTS: (Resuming)

17 Q If the evidence of record were to show that  
18 action of the Southern Pacific has denied the  
19 availability of the Ogden gateway to shippers of  
20 perishable commodities, so that the only alternative we  
21 have in terms of rail transportation from origins in the  
22 San Joaquin Valley is to ship the southern route, would  
23 you agree that the SP would have done that simply to get  
24 the long haul?

25 A No, I wouldn't.

1           Q     I see. Well, what motive might the SP have,  
2 assuming the evidence shows that we no longer have the  
3 Ogden route available to us, and further assuming the  
4 evidence shows that that provided reliable seven-day  
5 service, what motive would there be for the Southern  
6 Pacific to take action that would increase the average  
7 transit time by two to three days on perishable  
8 commodities?

9           A     As I had indicated before, I am not aware that  
10 we're the cause that is preventing traffic from going  
11 over Ogden. I remember a couple of years ago in  
12 conversations with Mr. Kenefick, who is president of the  
13 Union Pacific, on the perishable movement, that -- and  
14 this was after perishable was deregulated -- that he was  
15 concerned at his participation in what would be the  
16 competitive rate.

17                     And if I recall correctly, when we got  
18 perishable deregulated we were serving as the agent for  
19 the connecting lines over the Ogden gateway, and as long  
20 as they got so much we could price up and down the  
21 scale, to the advantage of both the shipper and we, the  
22 carrier. And they at that time had declined to go below  
23 a certain line, and you'll have to ask Mr. Edwards  
24 whether that conversation there relates to the facts you  
25 are presenting today.

1 Q And your desire to have the longer haul on  
2 SP-Cotton Belt didn't enter into those considerations?

3 A From a perishable point of view, once again  
4 recognizing it's a perishable commodity, it ought to go  
5 the shortest and most direct service route.

6 Q Are you representing to the Commission today  
7 that if this merger is approved, that the merged  
8 carriers will make every effort to see that perishable  
9 commodities move over the shortest, most efficient  
10 route, even if it involves connecting carriers?

11 A As I have indicated before, generally the  
12 shortest and quickest route is probably the most cost  
13 effective, and that's where the traffic should move and  
14 that would be for the benefit of both the carriers  
15 involved and the shippers.

16 Q Let me try that question again. Are you  
17 representing today that the policy of the merged  
18 carriers if the merger is approved will be to route  
19 perishable traffic over the shortest and most efficient  
20 route, even if it benefits some competing connecting  
21 carriers?

22 A I can't make the representation and the  
23 commitment of what the policy will be of the merged  
24 company.

25 Q So you have no policy? Is it that you have no



1 policy, or you simply don't want to represent what it  
2 will be?

3 A I don't represent what it will be.

4 Q Do you have a policy?

5 MR. STEPHENSON: Does he or the company have a  
6 policy?

7 BY MR. ROBERTS: (Resuming)

8 Q Has a policy been adopted that will apply to  
9 the merged carriers?

10 A The only specific indication is the material  
11 that was referred to on the first day and will be  
12 presented and discussed further by Mr. Fitzgerald.  
13 Now, that position indicates the plans affecting routes  
14 and gateways.

15 You are bringing in a completely different  
16 element on the time sensitiveness of the commodity,  
17 which may have a different factor; and we'll sit down  
18 with the involved carriers, I would interpret it.

19 MR. ROBERTS: I have no further questions.  
20 Thank you, Your Honor.

21 JUDGE HOIKINS: Who will be next?

22 CROSS EXAMINATION

23 BY MR. RATNER:

24 Q Mr. McNear, I'm James Ratner with the  
25 Department of Justice.

1 A Mr. Ratner.

2 Q In your verified statement on pages 5 to 7,  
3 you are describing the impact of trucks on rail  
4 competition, and on page 6 you referred to an unfair  
5 competitive advantage that trucks currently maintain.  
6 Do you see that in your testimony?

7 A I remember something of that context. I'm  
8 looking for the specific words. Can you help me?

9 MR. STEPHENSON: Five lines above "Teamster  
10 givebacks" on page 6.

11 THE WITNESS: Okay. "Such a transfer of user  
12 tax responsibility would further exacerbate an already  
13 unfair competitive advantage held by the trucking  
14 industry." Yes, sir.

15 BY MR. RATNER: (Resuming)

16 Q That unfair competitive advantage is an  
17 advantage over railroads, I assume?

18 A That's our perception, yes.

19 Q What's the nature of that advantage?

20 A This is referring back up to the Surface  
21 Transportation Act of 1982, and at that time the Act  
22 included some increased weight limits and size limits  
23 for the truckers up to 48, 50 feet, from 96 to 102  
24 inches, which as I indicated there is about a 20 percent  
25 increase in their volume capacity.

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1           And in coming to a determination on that, the  
2 legislation also considered -- and this is part of the  
3 facts from the DCT and other FRA studies, highway, I  
4 guess, studies -- as to the fair user charge, of the  
5 trucks paying their percentage fair user charge for the  
6 highway maintenance, development, and construction.  
7 This has been something that is nothing new.

8           And as part of that, they had scheduled  
9 increased user taxes and fuel taxes that came in to  
10 become effective in 1984, where they got the benefits  
11 starting January 1983. So that's what I'm referring  
12 to.

13           Q     Okay. What I'm asking you is, what is the  
14 advantage?

15           A     It reduces their costs.

16           Q     How does it reduce their cost?

17           A     For the trucker, if he's not paying his full  
18 share of the right of way that he is operating on, he  
19 has that benefit, where the railroad, having its private  
20 owned property, we're paying taxes on the property plus  
21 paying for the maintenance of it.

22           Q     So if I understand you, then, the advantage is  
23 that trucks aren't paying their full share of costs? Do  
24 I understand you right?

25           A     They're not paying what we feel is their

1 proportionate share of maintaining and building and  
2 constructing highways.

3 Q Why do you call that unfair?

4 A We're competing with them. We want to be on  
5 equal grounds. As far as for the benefit of the  
6 shipper, he benefits by it. He benefits by it, and all  
7 I'm saying is that gives us a relative, between trucks  
8 and rail, a disproportionate cost advantage, and we've  
9 got to devise and come up with something else to reduce  
10 our costs to be competitive with the total price the  
11 trucks can quote.

12 Q If trucks bore this full cost, then truck  
13 rates would rise?

14 A That's correct. I would assume they would,  
15 yes.

16 Q And there's no other advantage that you were  
17 referring to, other than the advantage that you've  
18 termed on page 5 "a massive public subsidy"?

19 A That's primarily it, and if the trucks' cost  
20 did rise we may get more in piggyback and use the  
21 efficiency of rail for the long haul and truck for the  
22 pickup and delivery.

23 Q The sentence right before the one we were  
24 talking about, that refers to a bill that would allow  
25 the trucking industry to have its cake and eat it, too.

1 A Yes, sir.

2 Q I'm familiar with the expression, but not its  
3 application right here. What are you referring to?

4 A Well, at the time this testimony was prepared  
5 it looked as if there would be further legislation that  
6 would eliminate or practically eliminate the entire  
7 increase in user and fuel taxes. And as I indicated  
8 before, part of the intent and the balance of the '82  
9 legislation was that trucks got the benefit of the  
10 increased size and capacity at that time and later they  
11 were to pay some offsetting additional charges.

12 And when I wrote this, it appeared that there  
13 may be legislation coming through that would have  
14 eliminated any increase on the truckers, either user or  
15 increased fuel taxes. As a matter of fact, those bills  
16 that I was referring to above there died in the House or  
17 the Congress, wherever.

18 But there was some compromise legislation  
19 increasing the fuel from about 9 to 15 cents and  
20 increasing the user tax from about \$204 to \$500, instead  
21 of the \$1600 that was initially in the Transportation  
22 Act bill.

23 Q Mr. McNear, on page 7, really starting on the  
24 bottom of page 6 --

25 A Yes, sir.

1 Q -- you indicate that since 1982 trucks have a  
2 competitive labor cost edge over rail.

3 A Wait a minute. What page is this, please?

4 Q Bottom of 6 and top of 7.

5 A Okay.

6 Q Is that a fair statement?

7 A Would you repeat your statement? I'm just  
8 reading.

9 Q Is it accurate that in your testimony you are  
10 indicating that since 1982 motor carriers had a  
11 competitive labor cost edge over rail?

12 A I think that merits explanation. What I'm  
13 saying is that this competitive labor edge, whether it's  
14 one way or another right now -- let's say it's fixed  
15 right now, the rates between what we pay our engineers  
16 and what the truck driver gets.

17 What I'm saying, during this period, under the  
18 labor contracts with the Teamsters, other than cost of  
19 living increases there was no general wage increase. So  
20 therefore, their costs that the truckers were charging  
21 or price the truckers could charge covering their costs  
22 were not increased, whereas we were still within a  
23 three-year contract with our labor and we had a ten  
24 percent per year increase, for example.

25 As I understand it, the Teamsters master

1 agreement had no increase in '83 or '84 other than the  
2 cost of living, where we were going on with the ten  
3 percent per year. That's what I'm trying to get at  
4 there.

5 Q I understand. Is it a fair statement to say,  
6 then, that during this period starting in 1982 trucking  
7 labor costs were lower than rail labor costs in a  
8 comparative sense?

9 A I'm still having trouble completely agreeing  
10 to your statement. I think you understand why.  
11 Whatever the base was, that gave them more advantage to  
12 reduce their total cost package.

13 Q Is rail a less labor intensive industry than  
14 motor carriers, do you know?

15 A Well, you can argue both ways on that.

16 Q Do you have any basis for knowing one way or  
17 another?

18 A No.

19 Q Is there any reason that in the future rail  
20 will always have a higher labor cost than motor carrier,  
21 in a comparative sense?

22 A I hadn't conceded that they were higher or  
23 lower. What I'm just thinking is, where you equate one  
24 truck and one rail, with one train with three or four  
25 men on the crew, versus how many trucks. I'm trying to



1 picture that in response to your question.

2 Q Well, per person.

3 A Oh, you're looking at the rates, the hourly  
4 rates? I'm having trouble understanding what you're  
5 asking, sir.

6 Q In your testimony you are suggesting that the  
7 wage rates that railroads are paying out since 1982 is  
8 higher than the wage rates that motor carriers are  
9 living with; is that correct?

10 A What I'm pointing out here is that during that  
11 period we had built-in increased rates that the truckers  
12 were not experiencing, and in fact in some cases there  
13 were sweetheart deals made and the rates of the truckers  
14 actually reduced. And our trucking subsidiary actually  
15 was able to negotiate some of those.

16 Q All I'm asking you is, is there any reason why  
17 that will continue to be the case over time?

18 A I think there's going to be constant give and  
19 take between carriers and shippers in wage  
20 negotiations.

21 Q On page 9 of your testimony, you state that,  
22 right before it says "CSX and Norfolk & Southern mergers  
23 and possible transcontinental consolidations," the  
24 sentence before that says: "As a result, the Staggers  
25 Act has greatly benefited carriers with wide geographic

1 reach, such as UP and PN, which can now provide the  
2 extended single system service under contract without  
3 the legal risk or practical problems of dealing with  
4 other carriers concerning joint rates."

5 Do you see that?

6 A Yes, sir.

7 Q What's the legal risk you are referring to?

8 A That's kind of a protective clause in there.  
9 If you ask me specifically what legal risks, there may  
10 be some. It's just an abundance of caution of putting  
11 it in that statement.

12 Q You don't have anything specific in mind?

13 A No.

14 Q What are the practical problems?

15 A Well, the advantage of single line service in  
16 making a contract, just the two of us, instead of  
17 including the young lady on the right to have to concur  
18 in it. We can go directly and come to terms without  
19 having to consider further delay of a third party. And  
20 under contract and Staggers, it gives us that  
21 opportunity to contract, where before Staggers for  
22 adjusting rates there was a period before the Commission  
23 and sometimes it would take delay. If you get to  
24 perishables, that hurt us.

25 Q I understand. I asked you about the practical

1 problems associated with dealing with other carriers  
2 concerning joint rates.

3 A Whether they agree or not.  
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1 Q On Page 18 of your testimony, you describe a  
2 voluntary agreement between the Denver and Rio Grande  
3 and Southern Pacific.

4 A I did.

5 Q And you say there are mutually beneficial  
6 objectives to having this agreement?

7 A There are.

8 Q Can you describe what your agreement does as  
9 far as solicitation between the two railroads?

10 A In addition to the terms of the Central  
11 Pacific conditions, we are working on areas outside the  
12 CP restrictions on soliciting for the Denver-Ogden  
13 gateway, and conversely the D&RG people are working for  
14 their best interests, and delivering to us under this  
15 agreement the traffic from the east coming west over the  
16 central corridor.

17 Q I am looking for a little bit more specific  
18 explanation of how that is to the benefit of Southern  
19 Pacific.

20 A One direct benefit that comes to mind is, a  
21 lot of this traffic is coming out of the Pacific  
22 Northwest, and if we can give a satisfied customer a  
23 joint route there instead of having the traffic go out  
24 over the northern lines or being trucked to a northern  
25 point and then going out on the BN.

1 Q Is it fair to say that the agreement  
2 facilitates efficiencies for the Southern Pacific?

3 A Yes, it does.

4 Q And you would assume so for the Denver and Rio  
5 Grande as well?

6 A That is why we are both in it voluntarily.

7 Q Does the agreement improve your ability to  
8 compete with the Union Pacific?

9 A Not necessarily.

10 Q Is that a yes or a no?

11 MR. STEPHENSON: It is a not necessarily.

12 JUDGE HOPKINS: It sounds like a yes and no.  
13 Would you explain?

14 BY MR. PATNER: (Resuming)

15 Q In what ways yes?

16 A Do you want to repeat the question?

17 Q Does the agreement you have with the Denver  
18 and Rio Grande improve Southern Pacific's ability or in  
19 a joint line movement both of the railroads' ability to  
20 compete with the Union Pacific?

21 A Yes.

22 Q In what way?

23 A It allows us to work with the D&RG versus the  
24 Union Pacific all the way out of the bay area on a  
25 single line haul.

1 Q Is it fair to say that traffic that might  
2 otherwise move on Union Pacific instead moves on  
3 Southern Pacific on the Denver and Rio Grande?

4 A Yes.

5 Q Does the agreement help Southern Pacific and  
6 presumably the Denver and Rio Grande help solicit  
7 traffic that might otherwise go to trucks?

8 A It sure could.

9 Q On Page 12, Mr. McNear, middle of the first  
10 paragraph, you describe Southern Pacific's dependence on  
11 autos, lumber, and consumer goods. Do you see that?

12 A Yes, sir.

13 Q If you know, what percentage of Southern  
14 Pacific total revenue do these commodities account for,  
15 say, in 1982?

16 A I don't know whether it is '82. I just have  
17 some margin notes here, autos about 8 percent, lumber 20  
18 percent, consumer goods 4 percent. I don't recall which  
19 year that was.

20 Q That was 20 and 8 and 4?

21 A Eight, 20, and 4.

22 Q So then by those figures roughly 65, 68  
23 percent of SP traffic is not of the nature which is  
24 dependent on the general economy?

25 A In this definition.

1 Q For this 22 percent or so --

2 A Thirty-two percent.

3 Q -- 32 percent -- I am sorry -- does the  
4 traffic noticeably improve when the economy is better?

5 A It certainly does, and as an example in the  
6 first half of this year lumber was good, interest rates  
7 went up, lumber, in direct correlation, our lumber  
8 loadings went down, our traffic.

9 Q You would say this is a cyclical problem for  
10 Southern Pacific, depending on whether the economy is  
11 down or the economy is up?

12 A That's right, yes.

13 Q Does Southern Pacific have any specific plans  
14 or programs designed to counteract the effect of well  
15 known cycles in the economy?

16 A One of our objectives was to merge with a  
17 carrier that had a base with products that were less  
18 cyclical, such as the Santa Fe.

19 Q Is the only thing the Southern Pacific  
20 considers about cycles in the economy is to merge with  
21 the Santa Fe?

22 A You are referring to the railroad, and not the  
23 total company in the cyclical counterbalance?

24 Q I am assuming this is just a railroad  
25 problem.

1           A     That is right. Well, it is a total corporate  
2 problem, but we are not addressing that here.

3           Q     All right. Yes, the railroad.

4           A     Yes. We have done that in signing up under  
5 the Staggers Act contracts with specific commodities  
6 where it is more or less a year-round business, and one  
7 that comes to mind is the rock, sand, and gravel for the  
8 construction business around the booming Houston area.

9           Q     Any other programs or policies designed to  
10 counteract the negative effects of cyclical effects in  
11 the economy?

12          A     I can't think of any right now. We  
13 continually look at them, but none come to mind.

14          Q     In terms of Southern Pacific traffic, was 1982  
15 a poor year for Southern Pacific?

16          A     Yes.

17          Q     How about 1983?

18          A     Yes. And I think I commented on that earlier  
19 when I was referring to Page 11, and it is a known fact  
20 that the economy generally started to revive in '83, but  
21 once again the products that we haul, we didn't see the  
22 increase in the economy and our participation in that, and  
23 and as I indicated earlier, where we had a 69 million  
24 income loss for operations in '82 on a betterment  
25 accounting basis, the net result in 1983 was negative



1 143 million, whereas I think the majority of the western  
2 carriers showed an increase in their operating income in  
3 '83 versus '82.

4 Q Perhaps to make sure you understood my  
5 question, I was only talking about traffic, and not  
6 operating costs, expenditures, income, et cetera. You  
7 understood that?

8 A Traffic means dollars to me.

9 Q If you try and answer it in terms of tonnage  
10 and volume and not dollars, does the answer change for  
11 1982?

12 A Eighty-two was a bad year for us.

13 Q In terms of tonnage?

14 A Volume, yes.

15 Q And 1983?

16 A Likewise. Now, as it relates to gross ton  
17 miles I don't recall.

18 Q On Pages 13, 14, and 15 of your testimony, Mr.  
19 McNear, starting on Page 13, below the Regained  
20 Competitive Rail Balance heading, second paragraph, you  
21 have been asked this before, and I don't intend to go  
22 into it in length, I am just going to try and cover a  
23 few things briefly, you state that BR is without  
24 effective rail competition in many parts of six northern  
25 tier states.

1 A I said that, and we've explained it.

2 Q On Page 14, you indicate that UP, like BN,  
3 dominates rail transportation in many regions.

4 A Yes, sir.

5 Q And on Page 15, the second sentence of the  
6 first full paragraph, you say that because of their  
7 dominant rail market positions and their lack of long  
8 lasting rail competition, BN and UP are able to focus  
9 against other transportation modes in a way that is  
10 better than Southern Pacific.

11 Can you describe for me the difference between  
12 focusing against other rail competition and focusing  
13 against truck competition from the perspective of  
14 Southern Pacific?

15 A What I had reference to here is that with, as  
16 we discussed before, their resources and their base in  
17 coal, in grain, and the volume that they move, that  
18 builds up a certain level of volume efficiency in  
19 operation, and the more volume you get, you have a  
20 better cost reduction.

21 So with that as a base, then they can look at  
22 the highway traffic and look at more or less from an  
23 incremental point of view picking up competitively with  
24 the highway soliciting for their business versus the  
25 trucks, and what I am trying to say here is, without as

1 strong a base on Southern Pacific, that is a leg up they  
2 have over us.

3 Q What does the strong base have to do with no  
4 effective rail competition?

5 Let me ask the question another way. If there  
6 were effective rail competition, would their base be as  
7 strong?

8 A It may not be.

9 Q Why not?

10 A There might be more competition.

11 Q They might not be able to make as much revenue  
12 from those commodities because they would lose some of  
13 it to the other railroad?

14 A That would be it, but we are all striving to  
15 make our rate of return as the Commission is looking at  
16 and we are all falling short of revenue adequacy in the  
17 railroad business.

18 Q Is it fair to say that absent effective rail  
19 competition, their rates on those commodities where you  
20 have described that they have a strong base might be  
21 higher?

22 A They might be higher, yes.

23 Q And you by this merger, is it fair to say, are  
24 attempting to equal the balance so that Southern Pacific  
25 and Santa Fe will have that same base?

1           A     What we are attempting to do here is to  
2 equalize from a rail point of view, given, as I said  
3 before, the other competitive nature of the total  
4 transportation market.

5           Q     I understand that. Are you trying to put  
6 yourself in a position similar to UP and BN where you  
7 have an effective base which is developed in part from a  
8 lack of rail competition?

9           A     The purpose of the merger is to put two  
10 regional carriers together so they can survive for the  
11 future, and if that puts us in that position as  
12 described in here, that is where we get.

13          Q     One of the ways -- is it fair to say then that  
14 one of the ways that you would be able to survive  
15 postmerger is due to an effective base which is  
16 developed in part through a lack of effective rail  
17 competition?

18          A     I don't take exception to that.

19          Q     One last point. Mr. McNear, on Page 5 --

20          A     Yes, sir.

21          Q     -- the second sentence on the page refers to a  
22 continuing shift from rail to truck, and I understand  
23 you have been asked about this before. You say it  
24 refers to a continuing shift from rail to truck?

25          A     Yes, sir.

1 Q. Are you referring to a shift of traffic from  
2 rail to truck, or the shift of the share from rail to  
3 truck?

4 A. In the share.

5 Q. Do you agree with me that a shift in share  
6 alone can be seriously misleading as to whether such a  
7 shift will in fact be harmful to railroads?

8 A. You have to look at both share and the total  
9 market.

10 Q. Can I run through a brief example with you and  
11 see if you agree with me about the example?

12 A. Sure.

13 Q. If in 1929 rail moves 20,000 tons, and truck  
14 moves none, rail has a 100 percent share?

15 A. Yes, sir.

16 Q. If in 1930 rail moves 50,000 tons and truck  
17 moves 25,000 tons, rail's share has dropped to 66.6 and  
18 truck's has increased from zero to 33.3. Is that  
19 correct?

20 A. Share. Yes, sir.

21 Q. And despite the fact that rail share has  
22 dropped and truck's has increased, rail total volume has  
23 improved?

24 A. That's right.

25 MR. RAKER: I have no other questions.

1 JUDGE HOPKINS: Thank you.

2 Mr. MacKenzie?

3 THE WITNESS: Good afternoon, Mr. MacKenzie.

4 CROSS EXAMINATION

5 BY MR. MAC KENZIE:

6 Q Good afternoon.

7 I would like to follow up at the start with a  
8 series of questions that may be a follow-up of Mr.  
9 Ratner's questions relating to shipper options, that is,  
10 shippers that may have the ability to choose one mode of  
11 transportation versus another for shipping needs,  
12 fulfilling shipping needs.

13 Would you agree that when the shipper  
14 considers the various factors that will benefit,  
15 facilitate the shipment of his goods and enable him to  
16 be competitive in his markets, that he considers a  
17 number of factors, and those factors might include the  
18 value of his commodity, its weight, its bulk, its  
19 perishability, its handling requirements?

20 Would you agree so far those are some of the  
21 considerations that the shipper thinks of?

22 A I would.

23 Q And in addition, does he not think of the  
24 distances that his goods have to be shipped?

25 A He would.

1 Q And perhaps one of the final major areas or  
2 factors he considers are the shipping times that will be  
3 involved in shipping his goods to its market or to its  
4 next point in transit?

5 A He would. He could.

6 Q And would you finally agree in that category  
7 that therefore he has a series of tradeoff  
8 considerations that he must evaluate when he is dealing  
9 with any of the modes of transportation that are  
10 available to him, whether it is rail, motor carrier, or  
11 water?

12 A And that results through the decisionmaking  
13 process, and then he accepts the price that is offered  
14 to him.

15 Q Yes, that is one thing we haven't mentioned,  
16 isn't it?

17 A Yes.

18 Q The price is one of the considerations,  
19 obviously.

20 A Certainly.

21 Q But just among the series of tradeoffs that he  
22 discusses, right, or he thinks about in his own mind  
23 when he makes his decision.

24 A When he accepts the price he is also thinking  
25 of those other considerations. I think we agree.

1 Q All right. Thank you.

2 Would you agree as far as California shippers  
3 are concerned that -- well, first of all, what we have  
4 asked or what we have established in the way of shipper  
5 considerations certainly applies to California shippers  
6 as well, correct?

7 MR. STEPHENSON: I am not sure I understand  
8 that question.

9 BY MR. MAC KENZIE: (Resuming)

10 Q Those considerations of the shipper apply to  
11 California shippers as well as any other shipper,  
12 correct?

13 A As a native Californian, I think we are equal  
14 to everybody else.

15 Q Would you agree that there are numbers and  
16 perhaps a significant number of shippers in California,  
17 based in California having plants or systems or  
18 businesses that practically speaking, because of these  
19 tradeoffs, are practically dependent upon either the  
20 Southern Pacific or the Santa Fe for their  
21 transportation services?

22 A I'd reverse the odds. I would say that more  
23 of them after they consider all those factors are more  
24 induced to go by truck than by rail.

25 Q All right. That's what I wanted to ask you



1 about.

2 A Sure.

3 Q Because we have indicated that there are a  
4 number of considerations for any particular shipper,  
5 trucking, or, for that matter, even water transportation  
6 really doesn't provide him with the range of shipping  
7 services and price that he needs in order to be  
8 competitive in his area.

9 Let's say the price is too high. The trucking  
10 charges are too high compared to rail or water. And  
11 that is an all-important factor for him.

12 Would you agree there are some who will do  
13 that?

14 A That is generally when we will handle  
15 perishable. Otherwise we won't handle it.

16 Q I wasn't just speaking of perishables.

17 A Well, you are asking my opinion. I am trying  
18 to relate it to what I base my opinion on.

19 Q To a particular good. I was not referring  
20 exclusively to perishables.

21 A I know you weren't. I was just using that as  
22 an example.

23 Q And wouldn't you agree that there are Santa Fe  
24 and SP shippers who in this discussion, this  
25 rationalization of the tradeoffs involved in his

1 business for his commodity have consistently opted for  
2 rail services because it comes down on the side of  
3 greater benefit to him?

4 A Do you have any in mind?

5 Q Well, let's see. I guess we could take sand  
6 and gravel, for instance. I don't think the particular  
7 commodity is so important, although I think we could say  
8 sand and gravel, let's say soda ash.

9 A Sand and gravel, our movement of sand and  
10 gravel, I think you can look at the statistics in  
11 California, and we are talking about California, have  
12 gone down. Fortunately, as I indicated earlier, we have  
13 been able to work through Staggers in recouping that  
14 business in Texas, but in California, I think you will  
15 find it is almost all truck.

16 Q But again, don't we have to look at the nature  
17 of the commodity, for instance, as one of the factors,  
18 the bulky nature of it, its weight, its shipping times?  
19 All those things have to come together, and I don't  
20 think you are maintaining that the trucks in all  
21 instances will provide the best method of providing  
22 shipping services for every shipper that is in  
23 California who has the ability to choose any one of the  
24 three.

25 A We certainly hope not.

1 Q Okay, and I assume you even know, perhaps, or  
2 your company certainly probably knows of those shippers  
3 of either Santa Fe or SP who consistently over the years  
4 have opted for rail services if not exclusively,  
5 practically exclusively.

6 A I am still trying to have you help me identify  
7 some of those.

8 Q Unfortunately, I am not in the railroad  
9 business. I don't know how many commodities, and how  
10 many are being shipped. I am asking you whether or not,  
11 do you know of any rail shippers in California that  
12 because of experience that you have found will more or  
13 less consistently use rail services only?

14 A I am having a hard time coming up with very  
15 many. You mentioned potash and the movement out of  
16 cerls trona. The majority of that goes by rail, but you  
17 know, years ago I thought lumber was captive to  
18 railroads. That is a dissipating perishable. We have  
19 lost perishable.

20 We have lost the inbound market in consumer  
21 goods from the west. We used to have consumer  
22 distribution warehouses where carloads of shipments  
23 would come in and then be processed and handed out to  
24 the department stores.

25 The Montgomery Wards and the Sears have chosen

1 to go in a more economical method through trailer loads,  
2 and now we are trying to compete to at least get them  
3 piggyback instead of direct over the highway.

4 So, if you can help me on some more.

5 Q Okay. When you say you have lost perishables,  
6 of course, with your new combination, you will not have  
7 lost, right, because the Santa Fe offers you a  
8 tremendous ability to penetrate markets with your use of  
9 intermodal services, do you not?

10 A We are feeling that competition right now.  
11 Yes, sir.

12 Q Which means usage of truck in combination with  
13 rail as an important factor that that shipper needs to  
14 provide his transportation services.

15 A And that will work in the Salinas Valley, in  
16 the San Joaquin Valley, all around. And also the UP is  
17 there.

18 Q Before you used the term in your testimony on  
19 Page 14 that it is true that "a few shippers at SP-Santa  
20 Fe common points will see their rail transportation  
21 options reduced from two to one."

22 What did you base that upon then? Did you  
23 make a study to determine for your satisfaction or to  
24 your satisfaction that there were so few that permitted  
25 you to use the term "a few shippers?"

1 A What page are we talking about?

2 Q Thirteen.

3 A I am on 14. Excuse me. And where, now?

4 Q The second sentence.

5 A This says, "Although it is true that a few  
6 shippers at Santa Fe Southern Pacific's common points  
7 will see their rail transportation options reduced from  
8 two to one after the merger, many times that number are  
9 today" -- underlined -- "dependent on SPT for rail  
10 service."

11 And I think I have already given those numbers  
12 in the record of some 20,000 versus some 2,500.

13 Q I want to talk to you about that later. What  
14 did you base this conclusion that there are only a few  
15 shippers who will be of the nature that they only have  
16 rail services or combinator rail-truck services?

17 A The few refers to the 2,500.

18 Q I see. But we have agreed, have we not, that  
19 there may be others that because of the tradeoff  
20 considerations may enlarge that figure?

21 A The sentence defines Santa Fe Southern Pacific  
22 common points, and that is the few in that respect.

23 Q As to the 20,200 captive shippers, let me ask  
24 a couple of clarifying questions on that and also how it  
25 relates to California.

1 A I beg your pardon?

2 Q And also how it relates to California.

3 A All right.

4 Q First of all, my notes indicate there are  
5 20,200 presently served exclusively by the SP  
6 nationally.

7 A Systemwide, yes.

8 Q Systemwide. There are in addition 2,500  
9 shippers who as a result of the merger will become  
10 exclusive as a result of the combination?

11 A To the merged carrier, yes.

12 Q Okay. That makes -- well, whatever the figure  
13 is. Then you mentioned 4,000 Santa Fe captive  
14 shippers. Was that a figure that you derived from  
15 premerger or postmerger?

16 A That is their comparable figure to our 20,000  
17 premerger.

18 Q So that is premerger?

19 A Yes, sir.

20 Q Do you know what their comparable figure is  
21 postmerger?

22 A We are in the same boat. It is 2,500.

23 Q So you add them all up, and there is 26,700  
24 captive shippers that will be exclusively served by  
25 either Santa Fe or Southern Pacific, correct?

1 A Rail served, yes.

2 Q All right. Now, how many of those exclusively  
3 served shippers, those 26,700, are located in  
4 California?

5 A I don't know.

6 Q Did anyone make a study of that to determine  
7 it?

8 A I don't know whether they have gone into that  
9 detail in drawing off these numbers.

10 Q Okay. Let me ask you then, do you know how  
11 many exclusive Southern Pacific shippers are in  
12 California?

13 A No, I do not.

14 Q In the Union Pacific case, I believe the  
15 record is clear that it was revealed there were some  
16 7,000 exclusively served shippers beholden to the  
17 Southern Pacific system.

18 A In California.

19 Q In California.

20 A That sounds -- one-third of our 20,000 Oregon,  
21 California, Oregon? That sounds like it is in the ball  
22 park.

23 Q Do you have any idea how many Santa Fe  
24 exclusively served shippers in California there are?

25 A I sure don't.

1 Q I assume Mr. Fitzgerald would probably have  
2 that figure.

3 Q I think he would be a good source.

4 MR. MOATES: For clarification --

5 THE WITNESS: Tom Fitzgerald.

6 MR. MCATES: I don't know if Mr. Fitzgerald  
7 has that at his fingertips or if he will have the time  
8 to make a special study, but if it is available we will  
9 provide that information.

10 JUDGE HOPKINS: Thank you.

11 BY MR. MAC KENZIE: (Resuming)

12 Q The next area of inquiry has to do with some  
13 of the questions I asked Mr. Cena, mostly relating to  
14 passenger service.

15 A Yes.

16 Q And he referred me to you. At least let me  
17 ask you these questions, and if you want to refer them  
18 to someone, I will acknowledge that. Do you know  
19 whether or not there has been established or assigned a  
20 line operating supervisor that is solely dedicated to  
21 the San Francisco-San Jose passenger service?

22 A I heard that question yesterday, and I haven't  
23 had the time to confirm whether it is actual or not. I  
24 know there is a former mechanical officer by the name of  
25 Ed Sile who is now looking after our Amtrak and commute



1 responsibilities.

2 I know he is working as much as he can with  
3 the CP, UC, and Caltrans in providing his expertise and  
4 knowledge in the acquisition of your new cars that you  
5 commented about yesterday, and if we have a hangup on a  
6 specific -- what the contract provides for of a specific  
7 line person, let me know after this meeting and we will  
8 sure get at it and correct it.

9 Q But as of now, are you saying there has not  
10 been anyone specifically assigned solely dedicated to  
11 the task of line operating supervisor in connection with  
12 the San Francisco-San Jose passenger service?

13 A What is your definition of line operator, so  
14 I can better respond or get the answer to you?

15 Q Thank you. I refer you to Page 16 of the  
16 contract between the state of California and Southern  
17 Pacific Transportation Company.

18 A Yes, sir.

19 Q Where it is provided that there will be  
20 established a line operating supervisor that is solely  
21 dedicated to the San Francisco-San Jose passenger  
22 service.

23 A All right. If that is in the contract, and we  
24 have got a point of contention, I have heard it, and I  
25 don't know whether there is one. I assume there is one,

1 but I can't say here.

2 Q I don't think there is one as of now, and this  
3 is why we are asking the question. The Department of  
4 Transportation is unable to find out who to deal with  
5 and who is responsible.

6 A We will get together after this hearing.

7 Q As to the new cars, I asked Mr. Cena, and I  
8 will ask you, are you aware that Caltrans will be  
9 providing Southern Pacific some 63 new cars in the  
10 spring of 1985 for the San Francisco-San Jose passenger  
11 service? Do you know if any provisions have been made  
12 to maintain these cars?

13 A Let me just see whether you misspoke  
14 yourself. They aren't providing us the cars. It is  
15 Caltrans cars for their service. It is not our  
16 ownership.

17 Q You are the operator, right?

18 A Under contract, yes.

19 Q Yes.

20 A As far as what the maintenance agreement is, I  
21 don't know, and I don't know whether the contract  
22 specifically covers that or not. If it doesn't, we will  
23 be glad to sit down with you and work it out.

24 Q Will there be a mechanical witness that would  
25 know whether or not mechanical maintenance services will

1 be provided?

2 A I don't anticipate any mechanical witness, but  
3 we will see if we can arrange for Mr. Lacy to make the  
4 proper response.

5 MR. MAC KENZIE: Okay. Thank you.

6 JUDGE HOPKINS: Is that all?

7 MR. MAC KENZIE: That is all.

8 JUDGE HOPKINS: Thank you.

9 Mr. Stephenson?

10 MR. STEPHENSON: Your Honor, I think we will  
11 have no redirect after all.

12 JUDGE HOPKINS: Thank you.

13 You are excused, sir.

14 (Witness excused.)

15 JUDGE HOPKINS: There were certain counsel's  
16 exhibits that haven't been received in evidence.

17 MR. RAKER: Your Honor, I would like to move  
18 the admission of KCS-C-3, 4, 5, 6, 7, 8, and 9.

19 JUDGE HOPKINS: Any objection?

20 MR. STEPHENSON: No objection.

21 JUDGE HOPKINS: They will be received in  
22 evidence.

23 (The documents referred to,  
24 previously marked for  
25 identification as Exhibits



1 come down and open up the room to the side, so I am not  
2 sure as to the one room whether we can use it. It is  
3 the International Trade Commission's, but there will be  
4 at least one room where you can put material.

5 MR. STEPHENSON: Has the witness been sworn,  
6 Your Honor?

7 JUDGE HOPKINS: Yes.

8 Whereupon,

9 BRUCE G. MCPHEE

10 was called as a witness, and having been first duly  
11 sworn, took the stand, was examined, and testified as  
12 follows:

13 DIRECT EXAMINATION

14 BY MR. STEPHENSON:

15 Q Mr. McPhee, this is your verified statement  
16 that I have placed in front of you?

17 A Yes, it is.

18 Q And with the exception of the errata that were  
19 filed several weeks ago with the Commission, do you have  
20 any changes or corrections or additions to your verified  
21 statement?

22 A No, I do not.

23 Q And this is your testimony in this case, and  
24 it is true and correct to the best of your knowledge and  
25 belief?

1 A That is correct.

2 MR. STEPHENSON: Your Honor, Mr. McPhee is  
3 tendered for cross examination.

4 JUDGE HOPKINS: Thank you.  
5 Who is going to start?

6 MR. MAYO: Your Honor, I will.

7 CROSS EXAMINATION

8 BY MR. MAYO:

9 Q Mr. McPhee, my name is George Mayo, and I  
10 represent the Rio Grande in this proceeding.

11 Let's begin by getting you to summarize what  
12 your responsibilities are as the Assistant Vice  
13 President of the Southern Pacific.

14 A I assist the chairman, Mr. McNear, in what  
15 matters he may indicate, and I provide financial support  
16 for the executive department, and I handle a number of  
17 diverse administrative matters.

18 Q When you say you provide financial support for  
19 the executive department, you mean you provide financial  
20 expertise to the executive department?

21 A Yes.

22 Q Now, you were appointed to your current  
23 position with the Southern Pacific in July, 1983, and  
24 before that you served as treasurer of both Southern  
25 Pacific Transportation Company and Southern Pacific

1 Company from May, 1976, to July, 1983.

2 Is that correct?

3 A That is correct.

4 Q How did your responsibilities as treasurer  
5 differ from your current responsibilities as an  
6 assistant vice president of the executive department?

7 A Well, as treasurer I was directly involved in  
8 the day to day financial operations of Southern Pacific  
9 Transportation Company and Southern Pacific Company,  
10 both in a treasury function and a financing function. I  
11 arranged most of the financing for Southern Pacific  
12 Transportation Company and for many of Southern Pacific  
13 Company's subsidiaries.

14 Q When you say you arranged financing, you are  
15 talking about financing for banks going to the capital  
16 markets? You mean all of the capital raising done by  
17 SPTC and Southern Pacific Company?

18 Is that right?

19 A That is correct.

20 Q And that changed when you became an assistant  
21 vice president in the executive department.

22 A That is correct.

23 Q Do you continue to have involvement with the  
24 capital raising functions of Southern Pacific  
25 Transportation Company?

1 A No.

2 Q Do you advise in that capacity, in that  
3 connection?

4 A Occasionally.

5 Q And who do you advise?

6 A Well, it would be Mr. McNear.

7 Q Now, just as background, to summarize what you  
8 had to say in your verified statement, and correct me if  
9 I am wrong -- I am really looking for just a broad  
10 summary of your testimony -- when I look on Page 2, it  
11 seems to me that you are making basically two points in  
12 your testimony.

13 In the first, and I am quoting from Page 2,  
14 you say that over the past ten years the financial  
15 health of SPT has eroded to a point where its long-term  
16 financial viability is in jeopardy. Then you go on to  
17 say, during the same period, other western railroads,  
18 particularly the Burlington Northern Railroad, Missouri  
19 Pacific Railroad, and the Union Pacific Railroad have  
20 increased their financial strength.

21 If you were looking -- and I am really not  
22 trying to hold you to this, I am just trying to  
23 establish a backdrop for our examination this afternoon,  
24 does that provide a general summary of the points that  
25 you make in your verified statement?



1 A Yes, that is true.

2 Q Now, getting a bit more specific, you say on  
3 Page 2 of your testimony, and I quote, "The recent  
4 recession reveals a serious weakness in SPT's ability to  
5 remain an independent, financially viable railroad."

6 Then you go on to Page 19 of your testimony,  
7 and you say that SPT faces an "uncertain future should  
8 SPT be left standing alone."

9 And then finally, on Page 20, you go on to say  
10 "Without such merger," referring to the merger that is  
11 before the Commission now, "SPT faces the prospect of no  
12 longer being an effective competitor. In fact, given  
13 time, competition from the large rail combinations that  
14 surround it together with other intermodal competition,  
15 SPT may cease to be financially viable and face possible  
16 dismemberment."

17 Now, Mr. McPhee, is it your view that unless  
18 this merger is approved by the Commission, that SPT is  
19 destined for bankruptcy?

20 A I think that SPT can survive for a period of  
21 time, and then their financial difficulties, if allowed  
22 to continue present trends, that they will face  
23 insolvency.

24 Q How long do you think that the company can  
25 survive before it faces insolvency?

1           A     If they use their other assets, their other  
2 nonoperating properties, and sell them, and provide  
3 cash, that will keep them going possibly through the  
4 period of trust, but I would say that even with those  
5 other assets, in two to five years Southern Pacific  
6 Transportation Company will face a complete loss of  
7 financial viability.

8           Q     Is that the roughly \$500 million in other  
9 assets that were referred to this morning by Mr.  
10 McNear?

11          A     That is correct.

12          Q     When did you come to the view that Southern  
13 Pacific was in this situation?

14          A     I have been advising management for  
15 approximately 12 years through my testimony and  
16 financial analysis that trends, financial ratios were  
17 adverse and trending downward, and I came to the  
18 conclusion comparatively recently, that is, the past  
19 several years, that if they were not reversed, we would  
20 be indeed in an extreme financial position.

21          Q     Have you seen any indication that these  
22 financial ratios, financial indicators may be reversed  
23 as of today?

24          A     No.

25          Q     And you say that you first came to this

1 conclusion a couple of years ago. Is that correct?

2 A Yes.

3 Q Now, you state on Page 20 of your testimony --  
4 you make a reference to the prospect of dismemberment of  
5 the Southern Pacific. What sort of dismemberment are  
6 you referring to there?

7 A Well, if the proposed merger is not  
8 consummated, I see no other alternative, and the only  
9 alternative might be bits and pieces to other interested  
10 parties.

11 Q Something in the nature of the Rock Island  
12 breakup?

13 A That is possible.

14 Q Does Southern Pacific have any contingency  
15 plans in connection with the prospect of a dismemberment  
16 at some point in the future?

17 A Well, the current prospect, of course, is the  
18 proposed merger, and beyond that we are looking at the  
19 assets necessary to continue to support SP  
20 Transportation Company, but as far as dismemberment or  
21 other alternatives, I am not aware of any studies to  
22 that effect.

23 Q Have there been discussions to your knowledge  
24 with respect to the possibility that if this merger is  
25 not approved by the Commission, dismemberment is

1 conceivably in the future of the Southern Pacific?

2 A Not to my knowledge, Mr. Mayo.

3 Q So this is basically your own personal view,  
4 but you haven't discussed this with anyone else. Is  
5 that correct?

6 A That is correct.

7 Q Does Southern Pacific have a schedule pursuant  
8 to which it is liquidating its nonrail assets to  
9 generate cash to keep it afloat during the pendency of  
10 the voting trust?

11 A Well, in effect, we are selling nonoperating  
12 property in order to provide cash to support SP  
13 Transportation Company during the period of voting  
14 trust.

15 Q And do you have a schedule which estimates how  
16 much cash you need to generate from that program?

17 A We don't have a precise schedule. We have a  
18 plan for this year to sell approximately -- we hope to  
19 sell approximately \$100 million worth of nonoperating  
20 properties, and we are formulating plans to sell  
21 nonoperating properties in 1985.

22 Q Do you have a dollar amount in mind in terms  
23 of the needs in 1985?

24 A Not in terms of needs, but I have consulted  
25 with the vice president in SP Transportation Company in

1 charge of real estate, in charge of these sales, and he  
2 has told me at the present time he sees about \$55  
3 million worth of properties that he would hope to sell  
4 in 1985.

5 Q So that is a lower amount than you needed in  
6 1984. Is that correct?

7 A That is correct. However, the process of  
8 selling real estate develops over a period of time. You  
9 don't sell it at one instant. And he is building this  
10 figure, and identifying other properties that may be  
11 potential sales properties.

12 Q Is he under direction to identify additional  
13 properties in a particular dollar amount for sale in  
14 1985?

15 A I believe he is under direction to identify  
16 potential sale properties. I do not know that he has  
17 been given a dollar amount.

18 Q Have you gone so far as to think in terms of  
19 property sales in 1986?

20 A No, sir.

21 Q And what will the proceeds of these sales be  
22 used for?

23 A They will be added to the working capital of  
24 Southern Pacific Transportation Company.

25 Q And that is used to meet your current

1 liabilities. Is that correct?

2 A That is correct.

3 Q Mr. McPhee, what materials did you review in  
4 preparing your statement? I take it you reviewed 10K's  
5 of the Southern Pacific. Is that right?

6 A Yes.

7 Q And the Form R1's for the Burlington Northern,  
8 Santa Fe, and the Union Pacific. Is that right?

9 A That is correct.

10 Q Anything else?

11 A In preparing for my testimony in support --

12 Q I am sorry, in drafting your verified  
13 statement.

14 A Yes, there are several other sources noted in  
15 the latter exhibits that refer to coal, grain, gross  
16 national product, housing starts, automobile production  
17 that are in the public sector, other sources.

18 Q In preparing your verified statement, did you  
19 examine the 1981, 1982 annual reports given to the  
20 shareholders for the Southern Pacific?

21

22

23

24

25

1           A     Not specifically, because I was preparing  
2 testimony that was focused on railroad operations and I  
3 wanted to limit it to that and not the broader non-rail  
4 lines of business.

5           Q     Had you read those documents?

6           A     Yes.

7           Q     Did you examine the annual reports provided to  
8 the shareholders for 1981 and 1982 for the Santa Fe?

9           A     No.

10          Q     Had you read those documents at the time you  
11 were preparing your verified statement?

12          A     No, I did not need to.

13          Q     Had you read the 1983 annual report of Santa  
14 Fe Southern Pacific at the time you prepared your draft  
15 verified statement?

16          A     I have read it. I'm not sure of the timing,  
17 because the submission of my verified statement was  
18 early in March and I'm not sure when I obtained a copy  
19 of the Santa Fe Southern Pacific Company annual report.

20          Q     And you have now, I take it, read the 1982  
21 annual report of the Santa Fe and the 1983 annual report  
22 of Santa Fe Southern Pacific, is that right?

23          A     I don't believe I've read the 1982 report of  
24 the Santa Fe. I've read the '83 combined report.

25               MR. MAYO: Your Honor, I'd like to have marked

1 for identification an affidavit of David A. Smith, to be  
2 marked DRGW-C-4. This is an affidavit that shows having  
3 been executed on December 8th, 1983, and purports to  
4 have been filed with the United States District Court  
5 for the District of Columbia.

6 JUDGE HOPKINS: It will be marked for  
7 identification.

8 (The document referred to  
9 was marked Exhibit No.  
10 DRGW-C-4 for  
11 identification.)

12 BY MR. MAYC: (Resuming)

13 Q Mr. McPhee, who is David A. Smith?

14 A He's the present treasurer of Southern  
15 Pacific, vice president and treasurer of Southern  
16 Pacific Transportation Company.

17 Q Did he succeed you as the treasurer of  
18 Southern Pacific?

19 A That is correct.

20 Q Did you assist Mr. Smith in the preparation of  
21 this affidavit?

22 A No, I did not.

23 Q Did you review the affidavit before it was  
24 filed with the district court on December 8th?

25 A No, I did not have that opportunity.



1 Q Did you ever discuss the December 8 affidavit  
2 with Mr. Smith?

3 A No, I have not.

4 Q Did you review this affidavit before you filed  
5 or prepared your verified statement in this proceeding?

6 A Yes, I did.

7 Q And why did you review the affidavit?

8 A Because it was a recent financial statement  
9 that was submitted on behalf of Southern Pacific  
10 Transportation Company.

11 Q Mr. McPhee, do you know how you were selected  
12 to serve as a witness in this proceeding?

13 A I have been a financial witness for Southern  
14 Pacific Transportation Company in many proceedings over  
15 the past decade.

16 Q And so they turned to you for your expertise;  
17 is that correct?

18 A That is correct.

19 Q Do you know whether Mr. Smith was ever  
20 considered as a witness for proffering testimony of the  
21 type that you are providing in this proceeding?

22 A In this proceeding?

23 Q Yes.

24 A I don't know.

25 Q You don't recall any discussions as to whether

1 you or Mr. Smith should provide the testimony that you  
2 have currently sponsored?

3 A No. Management came to me and asked me to  
4 provide testimony.

5 Q Who specifically?

6 A It was decided by our law department. Mr.  
7 Stephenson approached me.

8 Q Would you turn to page 3 of your verified  
9 statement. I'd like to know if you have any data which  
10 provides 1983 and mid-year 1984 dollar amounts for  
11 capital expenditures?

12 A For capital expenditures in 1983?

13 Q And for mid-year 1984.

14 A I don't have a mid-year figure for 1984. Let  
15 me see what I have for 1983.

16 Q Could you pull the mid-year off of a Form  
17 100?

18 A I don't have a 100 with me.

19 Q If I give you the Form 100, could you pull it  
20 off of that?

21 A I expect so.

22 For 1983, capital expenditures were listed at  
23 \$97.5 million. You must bear in mind that my figures  
24 are all on a retirement, replacement, betterment  
25 accounting basis, and the figure on a ratable

1 depreciation basis may differ. I believe on a ratable  
2 depreciation basis the figure is a little under \$300  
3 million for 1983.

4 Q Would 297.6 sound right?

5 A That would sound precise.

6 (Laughter.)

7 Q All right. Let's go to mid-year 1984. Now, I  
8 don't propose to burden the record with the 100.

9 JUDGE HOPKINS: Thank you.

10 THE WITNESS: The 100 from 1984? I thought  
11 you were saying a different document. I have a 100 for  
12 1984.

13 BY MR. MAYO: (Resuming)

14 Q Can you pull the capital expenditure dollar  
15 amount off of that?

16 A What page are you referring to?

17 Q On the 100?

18 A Yes.

19 Q I have no earthly idea.

20 JUDGE HOPKINS: You just know it's there.

21 (Laughter.)

22 THE WITNESS: Well, it would be after the  
23 statement of changes in financial position. And you're  
24 talking about expenditures for property. I'm talking  
25 about page 4. Look on page 4 under cash provided used

1 for investment activities, and you are referring  
2 generally to expenditures for property. You would be  
3 referring to the \$206 million figure.

4 BY MR. MAYO: (Resuming)

5 Q And that's depreciation accounting; is that  
6 correct?

7 A Yes, it is now.

8 Q And presumably betterment accounting would be  
9 somewhat lower?

10 A Yes.

11 Q Mr. McPhee, during the course of my  
12 examination from time to time I'm going to refer to the  
13 1982 annual report of the Southern Pacific and the 1983  
14 annual report of the Santa Fe Southern Pacific and the  
15 1982 annual report of Santa Fe. These reports were all  
16 included in the Santa Fe Southern Pacific application  
17 appearing in document number SFSP-4, volume number  
18 four. I have not made copies of these annual reports  
19 because they are in the record.

20 A I have a copy, Mr. Mayo.

21 Q Sticking with the subject of capital  
22 expenditures for a moment, isn't it true, Mr. McPhee,  
23 that in July 1983 Southern Pacific began a three-year,  
24 900-mile rail program?

25 A That is correct.

1 Q And the SFSP annual report at pages 8 to 9  
2 characterized this program -- and I'm going to quote:

3 "During 1983, Southern Pacific began one of  
4 the most ambitious rail programs in its history,  
5 designed to upgrade large portions of its 7,500 mile  
6 core system. A total of 900 miles of new welded rail  
7 will be installed over the course of the three-year,  
8 \$200 million program.

9 "Plans call for installation of 300 miles of  
10 new rail, plus 250 miles of reconditioned rail, in 1984,  
11 compared with 269 miles of new and 252 miles of  
12 reconditioned rail last year. Reballasting of 2,640  
13 miles of roadbed will be accomplished in 1984, compared  
14 with 1,900 miles last year. And about two million ties  
15 will be replaced."

16 Mr. McPhee, would you agree with the statement  
17 made by Mr. Smith in paragraph 16 of his December 8  
18 affidavit, which we have marked as our Exhibit No. 4 --

19 A What was that reference again, please?

20 Q Paragraph 16.

21 -- to the effect that this 900-mile rail  
22 program is further evidence of management's commitment  
23 to ensure that SPT has a competitive operation in its  
24 major traffic corridors?

25 A Yes, it is a commitment to improve the

1 property, to remain operationally competitive.

2 Q Just for purposes of clarification -- and I  
3 think that the answer is probably that it's the  
4 difference between depreciation accounting and  
5 betterment accounting, but I'd like to confirm that. If  
6 you look at paragraph 15 of Mr. Smith's affidavit,  
7 compared to the data contained in your table on page 3,  
8 you show 1981 capital expenditures \$215.3 million,  
9 compared to Mr. Smith's figure of \$344 million.

10 Is that simply the difference of betterment  
11 versus depreciation accounting?

12 A Yes. I have those two figures compared in my  
13 own work papers and that is the difference between  
14 replacement and depreciation accounting.

15 Q And the same is true for the comparison  
16 between 1982 figures in your table and the figures shown  
17 in Mr. Smith's affidavit?

18 A That's correct.

19 Q Do you know whether the 1984 forecast  
20 contained in Mr. Smith's affidavit on capital  
21 expenditures of, on a depreciation basis, approximately  
22 \$350 million continues to hold?

23 A I think that has been reduced. I'm not sure  
24 what the figure is, however.

25 Q But as of mid-year, \$206.2 million of capital

1 expenditures had been spent by the railroad, is that  
2 right?

3 A That is what's reported in the 10Q as  
4 expenditures for property.

5 Q Would you look at the net working capital  
6 figures on page 3. This is again a rather technical  
7 matter. Mr. McNear this morning provided us with  
8 working capital figures in 1983 of negative \$193 million  
9 and in mid-year 1984 negative \$219 million, and he  
10 stated that those figures were on a betterment  
11 accounting basis.

12 Does net working capital differ depending upon  
13 stating net working capital on a betterment accounting  
14 basis as opposed to depreciation?

15 A It shouldn't differ. It should not differ.

16 Q Can I get you to check what the net working  
17 capital figure was in 1983 and at mid-year 1984? Do you  
18 have the 10K's there?

19 A Yes, I do. The net working capital figure,  
20 well, let me take it off the 10K. Net working capital  
21 at the end of 1983 was a negative \$74 million.

22 Q And at mid-year 1984?

23 A Net working capital was negative \$99 million.  
24 I believe Mr. McNear had adjusted it. Those figures  
25 included a net contribution from the parent company, the

1 figures that Mr. McNear used. The figures -- and he  
2 adjusted working capital for the absence of that net  
3 contribution.

4 Now, I am giving you a working capital figure  
5 directly off the 10K and the 10Q.

6 Q That's the \$150 million contribution?

7 A It's a \$150 million contribution net of some  
8 repayments of advances to the parent company.

9 Q You're not making any repayment of the \$150  
10 million to the parent company at this point, are you?

11 A No.

12 Q Now, turning to the total debt column, which  
13 appears on page 3, in 1980 Southern Pacific had  
14 outstanding debt of \$1,336,800,000. By 1982 this had  
15 been reduced to \$1,061,400,000; is that correct?

16 A That is correct.

17 Q And this reduction was the product of a  
18 concerted effort by Southern Pacific management to  
19 reduce Southern Pacific's indebtedness, wasn't it?

20 A Not necessarily.

21 Q What was it a product of?

22 A It's a product of reducing your capital  
23 programs and having to pay off maturing debt.

24 Q Wasn't one of the goals of that reduction of  
25 debt to strengthen the corporation financially?



1           A     That was one of the goals in part, but as a  
2 matter of fact economic circumstance forced that  
3 reduction of debt. When the large equipment program of  
4 the late seventies and early eighties was completed and  
5 we went into the recession of '81-'82, the capital  
6 programs were necessarily cut back. Yet debt continued  
7 to mature and it was necessary to use the cash flow from  
8 depreciation to pay off this maturing debt.

9           Q     In paying off the maturing debt, you thereby  
10 took that debt off of your books, eliminating an  
11 obligation of the corporation, at least in the eyes of  
12 the financial community, strengthening the corporation  
13 somewhat, isn't that right?

14          A     That's part of the story, yes.

15          Q     Now, would you agree with the computation that  
16 appears in paragraph 10 of Mr. Smith's affidavit that  
17 this retirement of debt reduced SP's ratio of debt to  
18 total capitalization from 36.9 percent as of December  
19 31, 1980, to 28.8 percent as of September 30, 1983?

20          A     That's in paragraph 10?

21          Q     That's correct.

22          A     That may be true.

23          Q     Do you have any reason to believe that Mr.  
24 Smith was incorrect?

25          A     No.

1 Q Would you further agree with Mr. Smith's  
2 statement in paragraph 10 of his affidavit that SPT's  
3 1983 28.8 percent ratio of debt to total capitalization  
4 "is in line with other financially strong  
5 corporations"?

6 A Yes, I'd agree with that. But that's only one  
7 of the ratios involved.

8 Q Now, what was the company's year end 1983  
9 dollar amount of outstanding debt?

10 A Year end 1983, approximately \$940 million.

11 Q Do you know if as of today that amount has  
12 changed materially?

13 A I would not think it's changed materially.

14 Q Do you think it's gone up, gone down, in any  
15 respect?

16 A I think it's about the same.

17 Q So that with that amount of debt outstanding,  
18 is your ratio of debt to total capitalization today  
19 somewhere around 28 percent?

20 A Let me check the debt outstanding right now.  
21 As of the June 30 1984, it's very little change from year  
22 end '83.

23 Q So that you think that, if you did the  
24 computation, your ratio of debt to total capitalization  
25 would be approximately 28 percent?

1 A Approximately.

2 Q Now, Mr. McPhee, from time to time Southern  
3 Pacific develops long-term forecasts of its operating  
4 and financial performance, doesn't it?

5 A It has on occasion.

6 Q But it doesn't do it on a regular basis. It  
7 doesn't produce each year, for example, a five-year  
8 forecast?

9 A No, it does not.

10 Q Other companies do that. For example, Santa  
11 Fe does that, is that right?

12 A I'm not aware of Santa Fe's policy.

13 Q Are you familiar with the five-year forecast  
14 of Southern Pacific Railroad performance developed for  
15 the company by E. Phillip Anderson during May of 1983?

16 A Yes.

17 Q Who is Mr. Anderson?

18 A Mr. Anderson is an assistant in the executive  
19 department who's experienced in railroad operations.

20 Q And how long has he held that position?

21 A I'm not sure exactly how long.

22 Q Can you give me a rough approximation?

23 A He's been in railroad operations and in  
24 railroad management for many years, 15, 17, something  
25 like that.

1 Q And he's been with the company for quite some  
2 time, is that right?

3 A Yes, that's what I'm saying.

4 Q Did you become involved in the development of  
5 those projections?

6 A I asked Mr. Anderson at one point to develop  
7 some forecasts. He used his people and resources to  
8 develop such forecasts. I was not involved in the  
9 development of the forecast in that sense, but I asked  
10 him to make such a forecast.

11 Q So he was making his forecasts in response to  
12 your request; is that correct?

13 A Yes, when I was treasurer of Southern Pacific  
14 Transportation Company.

15 Q And in the course of developing the forecast,  
16 he used various resources within the company, going to  
17 various operating departments of the company to get  
18 their estimate of how the company was likely to perform  
19 over time, is that right?

20 A That is correct.

21 Q So he went to the traffic people to get their  
22 views of the traffic, went to the operating people to  
23 get their views of the future operations, et cetera; is  
24 that right?

25 A That is correct.

1 Q Now, Mr. Anderson's projections forecast a  
2 substantial improvement in the railroad's financial and  
3 operating performance, didn't it?

4 A He forecast a recovery from the recession we  
5 were then experiencing.

6 Q And in fact, forecasted that the railroad was  
7 going to perform much better than it had been  
8 performing, at least during the recession; is that  
9 correct?

10 A That is correct.

11 MR. STEPHENSON: As a precautionary matter, I  
12 don't know if Mr. Mayo plans to go into the numbers, but  
13 if he plans to go into the numbers beyond 1983 we are  
14 going to insist, with Your Honor's -- of course you run  
15 the courtroom, but we're going to request the courtroom  
16 be cleared.

17 This is a five-year forecast. We have SEC  
18 disclosure problems if the forecast is disclosed beyond  
19 1983. This matter has been produced pursuant to the  
20 protective order and it is a very sensitive matter. He  
21 has every right to go into it, but we're just asking  
22 that it be done outside of the public scrutiny and that  
23 this portion of the transcript be put under seal.

24 MR. MAYO: We don't have a problem. I don't  
25 intend to go into the specifics.

1 JUDGE HOPKINS: That handles that.

2 BY MR. MAYO: (Resuming)

3 Q Mr. McPhee, how were Mr. Anderson's  
4 projections employed by the company after they were  
5 developed? How were his projections employed by the  
6 company after they were developed?

7 A They were used in several ways, as I  
8 understand. One, he made the initial projection of what  
9 would happen under depreciation accounting versus  
10 retirement accounting. Number two, the forecasts were  
11 used in conjunction with the financing that was going on  
12 in the steel rail program that you mentioned. And  
13 number three, I believe they were ultimately provided to  
14 the investment bankers, who took them and used them to  
15 make some sort of assessment in conjunction with the  
16 proposed merger.

17 Q Now, in connection with obtaining the funding  
18 for the three-year rail program, were the projections  
19 provided to lenders in conjunction with your discussions  
20 with those lenders in obtaining the financing for that  
21 program?

22 A We had gone through a period of negotiation  
23 with the banks regarding the financing of what we call  
24 the steel rail program, and as we approached a period  
25 when the banks were going to meet with us and we were

1 going to have a presentation to the representatives of  
2 the banks, the banks made it clear to us that they would  
3 have to have some estimate, some projection of what we  
4 expected what our operating performance would be in the  
5 future in order to further consider the loan to the  
6 company.

7 Q And those projections which you supplied the  
8 banks provided the banks with that estimate; is that  
9 correct?

10 A Yes, we did.

11 Q And to your knowledge, the banks relied upon  
12 those estimates in extending the funding to you for the  
13 three-year rail program, is that right?

14 A In part.

15 Q In connection with the investment bankers,  
16 these forecasts were provided to Morgan Stanley? Is  
17 that who you were referring to?

18 A That is correct.

19 Q And Morgan Stanley was given the projections  
20 so that Morgan Stanley could employ them in conjunction  
21 with its valuation analysis of the Southern Pacific, is  
22 that right?

23 A Yes, I believe so.

24 Q And Southern Pacific provided those forecasts  
25 to Morgan Stanley because at the time they represented

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1 Southern Pacific's best estimate about what your future  
2 performance was going to be, is that right?

3 A That is correct.

4 Q Now, in May 1983 Mr. Biaggini and Mr. Krebs  
5 made a presentation to the New York financial analysts.  
6 Are you familiar with that presentation?

7 A No.

8 Q You have no information with regard to any  
9 financial presentation made by Mr. Biaggini and MR.  
10 Krebs to the New York financial analysts?

11 A No.

12 Q In 1983, do you have any familiarity with any  
13 presentations made by Southern Pacific officials to  
14 financial analysts anywhere, during the year 1983?

15 A Not to financial analysts. I was not a part  
16 of that proceeding.

17 Q To anyone else?

18 A Well, you furnished me last night a copy of a  
19 document, which I reviewed, that involved a presentation  
20 by management to employees.

21 Q Let me come back to that. Let me stick with  
22 the financial community.

23 My question went to, when you said -- when you  
24 suggested that there may have been someone else who had  
25 had one of these presentations made to them. I was



1 respect to the company's performance over the last  
2 several years and where the company saw itself going?

3 A Yes.

4 Q And that presentation is captured in the  
5 document we have marked as DRGW-C-5; is that correct?

6 A Yes.

7 Q Did the company make these kinds of  
8 presentations from time to time to its employees?

9 A This was a new concerted effort to improve  
10 communications with employees.

11 Q Do you know what the impetus of that was?

12 A I believe Mr. Krebs, then president of the  
13 railroad, felt that this was a need that had been not  
14 serviced, completely serviced properly in the past, and  
15 endeavored to improve relations with the employees.  
16 Also, there were some concerns he had about rumors of  
17 merger in the marketplace, and there were concerns he  
18 had.

19 It was part of his efforts to improve  
20 performance on the railroad by motivating employees. It  
21 was part of his efforts to also communicate that the  
22 railroad had some serious concerns about their condition  
23 and their competition, which was a result of the UI  
24 merger. And there were a number of reasons why this  
25 program was undertaken.

1 Q Doesn't this document, this presentation,  
2 suggest that there were some reasons for optimism about  
3 the future of the railroad?

4 A It was kind of a pep talk to the employees,  
5 but it also cautioned them that there were serious  
6 competitive and financial problems.

7 Q It cautioned them with respect to competitive  
8 and financial problems, but it also provided them data  
9 suggesting that the railroad was making some progress in  
10 terms of efficiencies in its position in the market, is  
11 that right?

12 A It pointed out that they were making some  
13 operational improvements, while the total car loadings  
14 had declined precipitously and while we were not  
15 generating the profits of competing railroads.

16 Q Let's go through and look at the document for  
17 a moment. Now, if you look at page 21 of the document,  
18 it notes that the railroad is maintaining its market  
19 share vis a vis the other western railroads in terms of  
20 total car loading at roughly the 14 to 16 percent level,  
21 but that that market is shrinking because of the  
22 recession, is that right?

23 A Page 21? Yes, because on page 20 it points  
24 out the decline in car loadings. But the market share  
25 looks relatively level.

1 Q Now, on page 34 the document points out that  
2 train and engine crew costs declined between 1978 and  
3 1983 in constant dollars, reflecting an efficiency gain  
4 of 4.2 percent each year; is that right?

5 A Let me get to page 34. Now again, Mr. Mayo,  
6 please?

7 Q The document points out that Southern Pacific  
8 train and engine crew costs declined between 1978 and  
9 1983 in constant dollars, reflecting an efficiency gain  
10 of 4.2 percent each year?

11 A Yes.

12 Q Then on page 35 it points out that SPT fuel  
13 consumption is trending downwards and has been between  
14 1978 and 1983, is that right?

15 A Yes. We were making some operational  
16 improvements. We were working very hard to make  
17 operational improvements during this period.

18 Q Then on page 36 it points out that the  
19 railroad had enjoyed improvement in its loss and damage  
20 ratios between 1978 and 1983, correct?

21 A We were making some operational improvements,  
22 despite our financial difficulties.

23 Q Page 37, it points out that the railroad  
24 increased its average train speed between 1980 and 1983,  
25 and that as a consequence equipment utilization had

1 improved?

2 A Yes.

3 Q Then on page 38, it points out an improvement  
4 between 1978 and '83 in average time in terminals?

5 A Yes.

6 Q Page 39, it points out that there has been  
7 improvement in lost days due to injuries between 1978  
8 and 1983?

9 A Yes.

10 Q Then on page 40, there has been improvement in  
11 miles of slow orders between 1978 and '83?

12 A What page?

13 Q Page 40.

14 A Yes.

15 Q And on page 41, it goes into the three-year  
16 rail program that we've already discussed; is that  
17 correct?

18 A Yes.

19 Q Page 42, it notes that the railroad has kept  
20 its capital expenditures up during the recession, is  
21 that right?

22 A Let me take a look at that. Actually, it  
23 shows declining capital expenditures.

24 Q I'm really only reading from the text. You  
25 see that on page 42?

1           A     Well, there's two 42's in all of this. One is  
2 a slide presentation. One is a slide and the other is  
3 the text that goes with the slide. So what 42 are you  
4 talking to?

5           Q     Let's stay with the text. I like the text  
6 better.

7           A     I noticed you've been selecting certain items  
8 out of the text.

9                     (Laughter.)

10          Q     You see that on page 42?

11          A     Well, it says on page 42, just reading right  
12 off of here, it says "has kept its capital expenditures  
13 up during the recession. It spent about \$140 million  
14 last year" -- which I take it is referring to 1982.  
15 Then it says "going to spend about \$93 million in 1983,"  
16 which are both levels of capital expenditures that are  
17 substantially below the immediately preceding years.

18          Q     That's correct. But then we are about to turn  
19 to the three-year rail program, which kicked capital  
20 expenditures back up, is that right?

21          A     Well, part of that's a shift into depreciation  
22 accounting, too.

23          Q     Right. But you agree that you are about to  
24 embark, again looking at the dates here --

25          A     By virtue of the support of the financing,

1 yes. They would not have been undertaken without the  
2 financing.

3 Q I agree with all that. Still, you agree  
4 that --

5 A Let's turn the page.

6 Q You agree you were about to embark on extended  
7 capital expenditures, right?

8 A As far as the roadway, the track structure,  
9 yes.

10 Q Then on page 44 you note that you had stored  
11 your new best locomotives so you could be ready when  
12 higher business volume came about, is that right?

13 A Yes, that was the objective.

14 Q Page 45 notes that the company had bought a  
15 lot of cars at the end of the last economic upswing and  
16 won't need many new cars in the future.

17 A We certainly didn't. We have quite a few idle  
18 boxcars.

19 Q Then page 47 provides something of a grand  
20 summary, extending over to page 48. It begins by  
21 saying: "In summary, we see SP has positioned itself  
22 for a profitable future growth by," and then it goes on  
23 to list a number of factors. Do you see that?

24 A I see the positioning. I see the statement,  
25 yes.



1 Q It says that Southern Pacific has improved its  
2 route structure, it's eliminated over 1,000 miles of  
3 unprofitable lines since 1977. It says you're providing  
4 crew service that is competitive, increasing  
5 profitability per carload, and lowering the operating  
6 breakeven point.

7 A Where is this?

8 Q On page 47.

9 You are realizing significant gains in  
10 transportation efficiency.

11 A This is based on what was said earlier.

12 Q Right.

13 And you flip over to page 48 and it says:  
14 "Moreover, at the same time costs of transportation were  
15 reduced. Maintenance productivity gains have led to  
16 better track maintenance. SP's car fleet has purposely  
17 been shrunk due to traffic exchanges. The locomotive  
18 fleet capacity in reserve is over 20 percent."

19 Do you see all of that?

20 A I see that. I'm acknowledging that it's in  
21 this paper. I cannot testify as to the accuracy of  
22 these statements outside of the financial area.

23 Q Let's turn to page 2 of your statement.

24 A Page 2.

25 Q You there indicate that Southern Pacific's

1 traffic mix differs from that of its competitors, and  
2 you note: "Other western railroads have major traffic  
3 components in coal and grain, which serve to support  
4 their revenues, to enhance their financial strength, and  
5 to cushion the adverse impact of the recent recession."

6 Do you see that?

7 A Yes.

8 Q Now, you don't mean to suggest that coal  
9 traffic is immune from economic, business and political  
10 influences, do you?

11 A I'm not saying it's immune, but I'm saying  
12 that there is a substantial and growing base in coal  
13 that other major western railroads have enjoyed and  
14 Southern Pacific Transportation Company has not.

15 Q But coal volume, coal traffic, can fluctuate  
16 depending upon influences such as the economy, politics,  
17 and the like, is that right?

18 A I'm not sure it does. On page 17 of my  
19 testimony, I am showing the coal, bituminous coal  
20 production in thousands of tons between 1973 and 1982,  
21 and I would direct your attention to the fact that it  
22 has grown 40 percent over that period.

23 Q Why don't you look at page 6 of the Santa Fe  
24 1982 annual report, and there you will find the  
25 following quote: "Consumption of coal decreased in the

1 Southwest during 1982 as a result of the national  
2 program to conserve energy and a general decline in  
3 industrial activity."

4 Then it goes on to report that "Santa Fe's  
5 1982 coal shipments declined 12 percent." Is that  
6 right?

7 A That may be correct, but that has nothing to  
8 do with the growth of coal on the Burlington Northern  
9 and the Union Pacific.

10 Q I will agree that it does not address those  
11 two railroads. I think that it does address the Santa  
12 Fe; is that correct?

13 A Yes, it may.

14 Q Now, let's turn to grain traffic. Grain  
15 traffic is also subject to economic, business and  
16 political influences, isn't that right?

17 A Yes, more so than coal.

18 Q For example, as noted in the 1983 Santa Fe  
19 Southern Pacific annual report on page 7, discussing  
20 wheat, which is the largest source of bulk grain  
21 shipment on the Santa Fe, the report says: "Softened  
22 export demand, drought conditions, and the payment in  
23 kind program, which encouraged farmers to leave fields  
24 fallow, combined to reduce carloads of wheat and other  
25 grain traffic by about 14 percent."

1 Is that right?

2 A That may be in the Santa Fe report. I'm not  
3 testifying as to the Santa Fe traffic mix.

4 Q You're testifying about grain in general?

5 A Grain in general, and pointing out the  
6 financial improvements made by other major western  
7 roads.

8 Q Who haul grain?

9 A Who haul grain, yes.

10 Q But the grain fluctuates just as can other  
11 commodities, isn't that right?

12 A It can fluctuate, but it fluctuates more  
13 narrowly than, as far as I can see, auto and housing  
14 starts fluctuate.

15 JUDGE HOPKINS: Mr. Mayo, I'm afraid we've got  
16 to stop now and recess until 9:30 tomorrow morning in  
17 Hearing Room B.

18 (Whereupon, at 3:33 p.m., the hearing in the  
19 above-entitled matter was recessed, to reconvene at 9:30  
20 a.m. on Thursday, October 4, 1984.)

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