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SERVICE DATE - AUGUST 31, 2004

SURFACE TRANSPORTATION BOARD

STB Finance Docket No. 34342

KANSAS CITY SOUTHERN  
— CONTROL —  
THE KANSAS CITY SOUTHERN RAILWAY COMPANY,  
GATEWAY EASTERN RAILWAY COMPANY, AND  
THE TEXAS MEXICAN RAILWAY COMPANY

Decision No. 11

Decided: August 30, 2004

The procedural schedule governing this proceeding was adopted in Decision No. 2 (served June 9, 2003, and published at 68 FR 35474 on June 13, 2003) and suspended in Decision No. 10 (served October 8, 2003). For the reasons given in this decision, the Board is resuming the procedural schedule, and is inviting interested persons to file additional comments.

BACKGROUND

*The Parties.* Kansas City Southern (KCS), a noncarrier, controls two U.S. railroads: The Kansas City Southern Railway Company (KCSR), a wholly owned direct subsidiary of KCS; and Gateway Eastern Railway Company (GWER), a wholly owned indirect subsidiary of KCS. Mexrail, Inc. (Mexrail), a noncarrier, controls one U.S. railroad: The Texas Mexican Railway Company (Tex Mex or TM), a wholly owned direct subsidiary of Mexrail. Prior to May 9, 2003, and again from September 30, 2003, to August 16, 2004, Mexrail was a wholly owned direct subsidiary of TFM, S.A. de C.V. (TFM), a Mexican railroad. Ownership of TFM is divided two ways: Grupo Transportación Ferroviaria Mexicana, S.A. de C.V. (Grupo TFM), owns an 80% interest in TFM; and the Mexican Federal Government owns a 20% interest in TFM. Ownership of Grupo TFM is divided three ways: KCS owns, through two corporate chains, a 36.9% interest in Grupo TFM; TMM Multimodal, S.A. de C.V. (TMM Multimodal) owns a 38.5% interest in Grupo TFM; and TFM owns a 24.6% interest, with limited voting rights, in Grupo TFM (which, as has been noted, owns an 80% interest in TFM). And TMM Multimodal is a 96.3%-owned indirect subsidiary of Grupo TMM, S.A. (Grupo TMM).

*The Two Transactions.* On April 21, 2003, KCS and Grupo TMM announced a series of agreements that contemplated a KCS/TM transaction (the acquisition, by KCS, of control of Tex Mex) and a KCS/TFM transaction (the acquisition, by KCS, of control of TFM). The KCS/TM transaction was subject to the jurisdiction of the Board under 49 U.S.C. 11323(a)(5) ("Acquisition of control of a rail carrier by a person that is not a rail carrier but that controls any

number of rail carriers.”), and, therefore, the Board’s approval of the KCS/TM transaction was sought by KCS in the KCS/TM application, which KCS filed on May 14, 2003, and which the Board accepted for consideration in Decision No. 2 (served June 9, 2003). The KCS/TFM transaction was not subject to the jurisdiction of the Board, see Decision No. 2, slip op. at 7 n.15, and, therefore, the Board’s approval of the KCS/TFM transaction was not sought by KCS.

*The KCS/TM Transaction.* One of the agreements (here referred to as the First Mexrail Stock Purchase Agreement) announced on April 21, 2003, contemplated the acquisition by KCS, from TFM, of 51% of TFM’s 100% interest in Mexrail (in exchange for a cash payment of \$32,680,000). On May 9, 2003, KCS consummated the acquisition and acquired a direct 51% interest in Mexrail (and, therefore, an indirect 51% interest in Tex Mex). KCS advised, however, that, to avoid any violation of § 11323 et seq., it immediately placed its Mexrail shares (i.e., KCS’s 51% interest in Mexrail) into an independent irrevocable voting trust (here referred to as the First Mexrail Voting Trust) that was established pursuant to an agreement that KCS asserted was consistent with 49 CFR part 1013.

*The KCS/TFM Transaction.* Two or more of the agreements announced on April 21, 2003, contemplated the acquisition by KCS of control of TFM. The KCS/TFM transaction envisioned by these agreements contemplated that KCS (which would be renamed “NAFTA Rail”) would acquire all of TMM Multimodal’s 38.5% interest in Grupo TFM, which, when combined with KCS’s 36.9% interest in Grupo TFM, would give KCS a controlling interest in Grupo TFM, and, therefore, a controlling interest in TFM. The KCS/TFM transaction further contemplated that TMM Multimodal would receive 18 million shares of the new NAFTA Rail representing an approximately 22% interest in the new NAFTA Rail, plus \$200 million in cash and a potential incentive payment of between \$100 million and \$180 million. KCS advised that the KCS/TFM transaction was subject to several contingencies, including (as pertinent for present purposes) the approval of the shareholders of Grupo TMM and the approval of the Mexican Foreign Investment Commission (MFIC).

*The Failure Of Two KCS/TFM Contingencies.* Two of the approvals on which the KCS/TFM transaction was said to be contingent have not yet been secured. (1) On August 18, 2003, Grupo TMM announced that its “shareholders, unanimously, did not approve” the sale, to KCS, of Grupo TMM’s interests in Grupo TFM. (2) On August 25, 2003, Grupo TMM announced that MFIC had been formally notified by Grupo TFM of the termination of the application that Grupo TFM had submitted to MFIC to permit KCS’s participation in more than 49% of Grupo TFM’s equity. On August 27, 2003, KCS announced that it had been advised that MFIC had deferred decision on KCS’s proposal to acquire control of Grupo TFM until after resolution of the dispute between KCS and Grupo TMM over the continued effectiveness of the KCS/TFM transaction agreement. On August 28, 2003, Grupo TMM announced that Grupo TFM had been advised of MFIC’s resolution to close the administrative process that had been initiated before MFIC.

*TFM's Exercise Of Its Option To Repurchase Its 51% Interest In Mexrail.* The First Mexrail Stock Purchase Agreement provided, in pertinent part, that "TFM shall retain the right to repurchase all of the Transferred Shares from KCS at any time [within 2 years of April 20, 2003] for an amount equal to the Purchase Price. Such right shall be unconditional and may be exercised in the sole discretion of TFM by written notice to KCS given by the Chairman of TFM and without any other corporate approvals of TFM or [Grupo TMM]." On August 27, 2003, the Chairman of TFM gave written notice to KCS that TFM was exercising its right to repurchase the 51% interest in Mexrail that KCS had acquired on May 9, 2003. On September 3, 2003, KCS gave the Trustee of the First Mexrail Voting Trust an "irrevocable" direction, "following receipt of an appropriate STB order (if required) and receipt of funds called for under the Mexrail Stock Purchase Agreement (the repurchase price shall be for the sum of US\$32,680,000.00) to deliver to TFM at the Repurchase Closing stock certificates representing the Transferred Shares endorsed in blank or accompanied by duly executed assignment documents."

*KCS's Intention To Achieve The KCS/TM Transaction.* In its KCS-18A pleading (filed September 2, 2003), KCS advised that it believed that it was likely that KCS would eventually succeed in acquiring control of Mexrail and Tex Mex. KCS further advised that it was not withdrawing the KCS/TM application. KCS expressed its belief that the application proceeding should continue.

*Trustee's Request For Guidance.* By letter dated September 5, 2003, the Trustee of the First Mexrail Voting Trust asked "that the Board provide such authority, direction or guidance as the Board deems appropriate" with respect to the proposed repurchase of the 51% interest in Mexrail that KCS had acquired, and placed in the First Mexrail Voting Trust, on May 9, 2003.

*Decision No. 9.* In Decision No. 9 (served September 23, 2003), the Board took two actions. (1) The Board noted that past cases had held that, when a controlling interest in a U.S. railroad has been placed in a voting trust pending action by the Board on a § 11323 control application, the Board has the authority to approve both a plan of divestiture and the sale (or other disposition) of the controlling interest held in the voting trust, even when (as was the situation here) the person acquiring the controlling interest (here, TFM) would not otherwise require authority under § 11323 to consummate such acquisition. The Board concluded, however, that there was, under the circumstances indicated by the record, no need to rule on the proposed transfer back to TFM of the 51% interest in Mexrail that KCS had acquired, and placed in the First Mexrail Voting Trust, on May 9, 2003. The Board explained that the "plan of divestiture" with respect to which the Trustee sought guidance would merely restore the status quo ante that had existed prior to May 9, 2003, and would leave KCS, TFM, and Tex Mex (and all other persons) in exactly the same positions they were in prior to KCS's acquisition of a 51% interest in Mexrail. (2) The Board announced that, in light of the then recent developments, it had serious reservations about going forward, at that time, with consideration of the KCS/TM application. The Board therefore invited interested parties to advise whether the procedural

schedule that had been adopted in Decision No. 2 should be suspended, pending a resolution of the uncertainties that then surrounded the KCS/TM application.

*Transfer Back To TFM Of The 51% Interest In Mexrail.* On September 30, 2003, TFM reacquired the 51% interest in Mexrail that KCS had acquired, and placed in the First Mexrail Voting Trust, on May 9, 2003.

*Decision No. 10.* In Decision No. 10 (served October 8, 2003), the Board announced that, “pending a resolution of the uncertainties that now surround KCS’s efforts to acquire control of Tex Mex,” it was suspending the procedural schedule that had been adopted in Decision No. 2. The Board explained that, because the First Mexrail Stock Purchase Agreement provided that, upon the repurchase by TFM of its 51% interest, “this Agreement shall automatically terminate and be of no further force or effect,” the KCS/TM transaction as originally contemplated was no longer a present possibility. The Board advised, however, that, because KCS was still seeking to acquire control of Tex Mex (and, therefore, a KCS/TM transaction was still possible), the Board would reinstate the procedural schedule “at such time as KCS demonstrates that there is a reasonable likelihood that it will be able to acquire control of Tex Mex.” The Board added: “If and when the uncertainties that now surround KCS’s efforts to acquire control of Tex Mex are resolved, the Board will, if appropriate, rule on the merits of the KCS/TM application.” Decision No. 10, slip op. at 3.

*Second Mexrail Stock Purchase Agreement.* On August 16, 2004, KCS, TFM, and Grupo TMM announced the execution of a revised Stock Purchase Agreement (here referred to as the Second Mexrail Stock Purchase Agreement) pursuant to which KCS that day acquired from TFM a 51% interest in Mexrail. KCS advised, in its Status Report filed August 16, 2004, that, pending approval of the KCS/TM application and to avoid any unauthorized control of Tex Mex, KCS would, immediately upon acquisition of the 51% interest in Mexrail, place its Mexrail shares into an independent voting trust (here referred to as the Second Mexrail Voting Trust) which (KCS asserted) is substantially identical to the previous voting trust. KCS further advised that the Second Mexrail Stock Purchase Agreement is substantially the same as the First Mexrail Stock Purchase Agreement, with these exceptions: (1) KCS is obligated to purchase the remaining 49% of Mexrail’s shares no later than October 31, 2005; (2) TFM has no right to repurchase the Mexrail shares; (3) KCS has agreed to repay certain debt owed by Mexrail and Tex Mex to TFM; and (4) in addition to obligating KCS and Mexrail for 5 years not to sell or lease their interest in the northern half of the International Rail Bridge at Laredo, the Second Mexrail Stock Purchase Agreement embodies KCS’s previous oral commitment to abide by known existing written contracts and protocols for operation of the Bridge.

*KCS/TFM Transaction Not Yet Resolved.* KCS advised, in its Status Report filed August 16, 2004, that KCS and Grupo TMM have not yet reached agreement with respect to the proposed KCS/TFM transaction, and, therefore, the KCS vs. Grupo TMM dispute respecting the

KCS/TFM transaction remains in litigation and negotiation. KCS noted, however, that the revised agreement to acquire control of Mexrail, and thereby Tex Mex, is separate and apart from KCS's efforts to acquire control of TFM itself and is not contingent on acquisition by KCS of control of TFM. And, KCS added, the elimination of TFM's repurchase right with respect to the Mexrail shares guarantees that the revised KCS/TM transaction can occur regardless of the outcome of any litigation or negotiation with respect to KCS's efforts to acquire control of TFM.

*Request For Reinstatement Of The Procedural Schedule.* KCS contends that, because the Second Mexrail Stock Purchase Agreement demonstrates a "reasonable likelihood" that KCS will acquire control of Tex Mex, the Board should now reinstate the procedural schedule that was issued in Decision No. 2 and should move toward issuance of a final decision on the merits of the KCS/TM application without further hearings or evidentiary submissions. KCS argues: that the differences between the previous KCS/TM transaction and the revised KCS/TM transaction are minor in nature; that these minor differences do not impact the evidence or analyses previously submitted in this proceeding; that, furthermore, these minor differences do not involve any changes in the substantive areas of concern that the Board considers in a "minor transaction," see 49 CFR 1180.2(c); and that, therefore, these minor differences do not require additions or modifications to the existing evidentiary record or a different statutory analysis than that already provided for in the record. KCS adds that, if the Board determines that the existing record does not warrant issuance of a final decision at this time, KCS does not object to a short time period for parties to file comments and replies.

*Environmental Matters.* As explained in detail in Decision No. 2, KCS provided sufficient information in its application to create a presumption that this matter does not require formal environmental review under the National Environmental Policy Act. However, to assist the Board's Section of Environmental Analysis (SEA) in determining whether preparation of an Environmental Impact Statement (EIS) or an Environmental Assessment (EA) is necessary, the Board directed KCS to prepare and distribute an Environmental Appendix providing additional details and explanation, and to submit a Safety Integration Plan (SIP), pursuant to the joint regulations adopted by the Federal Railroad Administration (FRA) and the Board to ensure adequate and coordinated consideration of safety integration issues. See 49 CFR parts 244 and 1106. The Board invited comments on both the Environmental Appendix and the SIP, and several comments were received. The Board indicated that, based on SEA's consideration of the comments and SEA's independent review of all available environmental information, SEA would then recommend to the Board whether there is a need for formal environmental review. The Board stated that it would then determine whether an EA or an EIS should be prepared, and that, even if no EA or EIS is warranted, it intended to include in any decision approving the transaction a condition requiring KCS to comply with the SIP.

*Other Pleadings.* By letter filed August 24, 2004, Union Pacific Railroad Company (UP) asks that the Board allow interested parties 60 days to file comments addressing the implications,

if any, of developments over the past year for the Board's treatment of the KCS/TM application. Interested parties, UP argues, need sufficient time to review the new agreement between KCS and TFM, conduct limited discovery regarding that agreement and its implications, and probe the status of KCS's ongoing efforts to acquire control of TFM. By pleading (designated DOT-6) filed August 26, 2004, the U.S. Department of Transportation (DOT) asks that the Board invite parties to submit comments within a reasonable period (DOT suggests, in particular, that the Board allow 30 days for comments and 15 days for replies). Interested parties, DOT argues, need time to consider whether changes in the new purchase agreement or other factors warrant new evidence or analysis, and to provide support for their views. DOT also states that KCS has advised FRA that it has resumed work on a SIP in this case. DOT adds that FRA anticipates working with KCS toward a final approval of the SIP.

### DISCUSSION AND CONCLUSIONS

In Decision No. 10, the Board suspended the previously adopted procedural schedule, pending a resolution of the uncertainties that then surrounded KCS's efforts to acquire control of Tex Mex. Because those uncertainties now appear to have been resolved, the procedural schedule will be resumed, and the Board will now begin to move toward issuance of a final decision on the merits of the KCS/TM application.

The Board notes, however, that almost a year has gone by since the procedural schedule was suspended. The Board also notes that, even by KCS's account, there are some differences between the KCS/TM transaction contemplated by the First Mexrail Stock Purchase Agreement and the KCS/TM transaction contemplated by the Second Mexrail Stock Purchase Agreement. Therefore, the Board thinks it best to give interested persons an opportunity to file any additional comments that may be appropriate given the change to the transaction. Interested persons also are invited to file updated or additional comments on any potential environmental issues that might result from the changes to the transaction. And KCS, of course, will be given an opportunity to respond to all such additional comments.

Furthermore, the Board will eliminate the requirement, imposed in Decision No. 10, that KCS file periodic status reports as to its acquisition of Tex Mex, but will continue the requirement that KCS file periodic status reports detailing new developments (if any) in its efforts to acquire control of TFM.

This action will not significantly affect either the quality of the human environment or the conservation of energy resources.

It is ordered:

1. The procedural schedule in this proceeding is resumed.

2. Interested persons may submit additional comments by September 30, 2004.
3. KCS may submit, by October 15, 2004, a reply to any additional comments filed by interested persons.
4. The requirement in Decision No. 10, ordering paragraph 2, that KCS file status reports is modified to require the status reports only as to its efforts to acquire control of TFM.
5. This decision is effective on the service date.

By the Board, Chairman Nober, Vice Chairman Mulvey, and Commissioner Buttrey.

Vernon A. Williams  
Secretary