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SERVICE DATE - OCTOBER 16, 1998

SURFACE TRANSPORTATION BOARD

STB Finance Docket No. 33556

CANADIAN NATIONAL RAILWAY COMPANY, GRAND TRUNK CORPORATION, AND
GRAND TRUNK WESTERN RAILROAD INCORPORATED--CONTROL--ILLINOIS
CENTRAL CORPORATION, ILLINOIS CENTRAL RAILROAD COMPANY, CHICAGO,
CENTRAL AND PACIFIC RAILROAD COMPANY, AND CEDAR RIVER RAILROAD
COMPANY

Decision No. 12

Decided: October 15, 1998

We consider, in this decision: the CN/IC-27 appeal,¹ filed October 5, 1998,² by applicants³ and KCS;⁴ the CPR-10 reply,⁵ filed October 8, 1998, by CPR⁶ and NSR;⁷ the RUB-12 reply,⁸ filed October 8, 1998, by Rubicon⁹ and Uniroyal;¹⁰ and the UP-7 reply, filed October 9, 1998, by UP.¹¹

The CN/IC-27 Appeal. By order entered orally at a discovery conference, Administrative Law Judge Harfeld directed applicants and KCS to comply with certain discovery requests relating to the negotiation and implementation of two settlement agreements dated April 15, 1998: a CN/IC/KCS settlement agreement (the so-called Alliance agreement), that established, effective April 15, 1998, a 15-year CN/IC/KCS marketing alliance; and a CN/KCS settlement agreement (the so-called Access agreement), which provides that, if the CN/IC transaction is approved by the Board and implemented by applicants, IC and KCS will grant each other access to certain of each

¹ For ease of reference, this appeal, though designated CN/IC-27 and KCS-7, will be referred to as the CN/IC-27 appeal.

² The CN/IC-27 appeal was submitted for filing on October 2, 1998, but, because a check for the filing fee was not submitted until October 5, 1998, the appeal was not considered "filed" until October 5, 1998.

³ Canadian National Railway Company (CNR), Grand Trunk Corporation (GTC), and Grand Trunk Western Railroad Incorporated (GTW) are referred to collectively as CN. Illinois Central Corporation (IC Corp.), Illinois Central Railroad Company (ICR), Chicago, Central & Pacific Railroad Company (CCP), and Cedar River Railroad Company (CRRC) are referred to collectively as IC. CN and IC are referred to collectively as applicants.

⁴ Kansas City Southern Railway Company is referred to as KCS.

⁵ For ease of reference, this reply, though designated CPR-10 and NS-6, will be referred to as the CPR-10 reply.

⁶ Canadian Pacific Railway Company, Delaware and Hudson Railway Company, Inc., Soo Line Railroad Company, and St. Lawrence & Hudson Railway Company Limited are referred to collectively as CPR.

⁷ Norfolk Southern Railway Company is referred to as NSR.

⁸ For ease of reference, this reply, though designated RUB-12 and UCC-12, will be referred to as the RUB-12 reply.

⁹ Rubicon Inc. is referred to as Rubicon.

¹⁰ Uniroyal Chemical Company, Inc., is referred to as Uniroyal.

¹¹ Union Pacific Railroad Company is referred to as UP.

other's facilities (including certain facilities in Geismar, LA, as to which IC and KCS are opponents in a separate proceeding before the Board).¹² Applicants and KCS have accepted Judge Harfeld's order as respects *implementation*, but, in their CN/IC-27 appeal, have asked us to overturn Judge Harfeld's order as respects *negotiation*.¹³

Applicants and KCS contend: that, as an adjunct to our preference for negotiated settlements,¹⁴ there is, in our proceedings, a "settlement privilege" that, absent compelling circumstances, bars discovery of confidential material related to settlement negotiations;¹⁵ that, in order to overcome the privilege, a party seeking discovery of privileged material must make specific, focused requests, and must demonstrate (not merely assert) a particular need for that specific material; that there has been, in this proceeding, no showing by any party of any specific or concrete need for any particular information concerning any particular aspect of the negotiation of either of the two relevant settlement agreements; and that, against this background, Judge Harfeld's order, if permitted to stand, will have a chilling effect as to future settlement agreements. Applicants and KCS further contend: that the two settlement agreements are indeed settlement agreements, i.e.,

¹² See Kansas City Southern Railway Company--Construction and Operation Exemption--Geismar Industrial Area Near Gonzales and Sorrento, LA, Finance Docket No. 32530 (STB served Aug. 27, 1998) (providing that the Finance Docket No. 32530 proceeding will be held in abeyance until the issuance of a final written decision in the STB Finance Docket No. 33556 proceeding).

¹³ We understand that, in the present context, *implementation* includes, among other things, *effects* (i.e., the part of Judge Harfeld's order that applicants and KCS have accepted directs applicants and KCS to comply with discovery requests respecting both implementation of the two settlement agreements and the effects of such implementation). We further understand that, in the present context, *negotiation* includes *background* and *purposes* (i.e., the part of Judge Harfeld's order that applicants and KCS have appealed directs applicants and KCS to comply with discovery requests respecting the negotiation of the two settlement agreements, the background of such negotiations, and the purposes served by the two settlement agreements).

¹⁴ See, e.g., CSX Corporation and CSX Transportation, Inc., Norfolk Southern Corporation and Norfolk Southern Railway Company--Control and Operating Leases/Agreements--Conrail Inc. and Consolidated Rail Corporation, STB Finance Docket No. 33388, Decision No. 89, slip op. at 58 (STB served July 23, 1998) (we noted "our direction that, whenever possible, disputes should be resolved by negotiated settlement between affected parties, rather than addressed by a resolution imposed by government decree").

¹⁵ See, e.g., Union Pacific Corporation and Union Pacific Railroad Company -- Control -- Missouri Pacific Corporation and Missouri Pacific Railroad Company, Finance Docket No. 30000, slip op. at 10 (ICC served Apr. 27, 1981) ("The determination of whether or not to allow or require discovery of confidential material requires a balancing of interests. While SPT's discovery of the withheld UP documents may have been useful, in either a tactical or commercial sense, it does not appear necessary in light of the materials already made available to SPT.").

agreements entered into in view of the opposition stance that KCS might otherwise have taken vis-à-vis the CN/IC application;¹⁶ and that applicants, although they have referred in the CN/IC application to the two settlement agreements, have not thereby waived the settlement privilege with respect to such agreements.¹⁷

Applicants and KCS indicate that, in the interest of avoiding the delay that would have been occasioned by a stay of Judge Harfeld's order pending their appeal thereof, they have complied with that order and have not sought a stay pending appeal.¹⁸ Applicants and KCS therefore suggest that, if we overturn Judge Harfeld's order as respects negotiation, we should also rule that documents or information respecting negotiation that have been produced by applicants and KCS in compliance with that order cannot be used by the recipients thereof in this proceeding, in their submissions or otherwise.

The CPR-10 Reply. CPR and NS agree that established precedent recognizes a settlement privilege, which, in appropriate cases, provides an important, but qualified, protection against discovery of genuine settlement negotiations. CPR and NSR insist, however, that applicants and KCS have not satisfied the stringent standards for overturning an administrative law judge's (ALJ's) discovery order, and that the CN/IC-27 appeal should therefore be denied.

CPR and NSR contend: that the Alliance and Access agreements are not "settlement agreements" within the meaning of the privilege;¹⁹ that, even if the Alliance and Access agreements

¹⁶ Applicants claim that they were well aware that KCS has opposed every major railroad merger since 1980. We think it appropriate to note, however, that, in reality, KCS has not opposed every major railroad merger since 1980. See CSX Corporation and CSX Transportation, Inc., Norfolk Southern Corporation and Norfolk Southern Railway Company--Control and Operating Leases/Agreements--Conrail Inc. and Consolidated Rail Corporation, STB Finance Docket No. 33388, Decision No. 89, slip op. at 204-06 (STB served July 23, 1998) (KCS was not directly involved in the CSX/NS/CR proceeding; its Gateway affiliates were involved, but their interests were narrowly focused).

¹⁷ Applicants and KCS insist that no aspect of the negotiations that led to the two settlement agreements is revealed or referred to in the CN/IC application.

¹⁸ See 49 CFR 1115.2(f) ("The timely filing of an appeal to an initial decision [of an administrative law judge, individual Board Member, or employee board] will stay the effect of the action pending determination of the appeal.").

¹⁹ The Alliance and Access agreements, CPR and NSR claim, are not settlements of anything; they are, rather, prospective commercial arrangements of mutual benefit to the parties thereto. CPR and NSR note: that the two agreements were negotiated and entered into long before the CN/IC application was filed and long before any party (including KCS) had indicated any

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are settlement agreements within the meaning of the privilege, the privilege must yield in view of the relevance of, and the particularized need of CPR and NSR for, the disputed materials;²⁰ and that, in any event, any privilege that may have attached to negotiation materials respecting the Alliance and Access agreements was waived by applicants' decision to "saturate" the CN/IC application with discussion and analysis of the two agreements.²¹

CPR and NSR further contend, in essence, that, even if Judge Harfeld erred in ordering applicants and KCS to comply with discovery requests concerning negotiation of the Alliance and Access agreements, the CN/IC-27 appeal should nevertheless be denied because applicants and KCS, having voluntarily elected to produce the disputed materials respecting negotiation despite their appeal of Judge Harfeld's order, have thereby waived any otherwise applicable settlement privilege.²² And, CPR and NSR add, any objections that applicants and KCS may properly assert

¹⁹(...continued)

position on the proposed CN/IC consolidation; and that the core provisions of the agreements (the Alliance provisions establishing a 15-year strategic marketing alliance on interline traffic) were made effective immediately, without regard to approval by the Board, or consummation by applicants, of the CN/IC consolidation. CPR and NSR concede, of course, that the reciprocal grants of haulage and trackage rights and other provisions of the Access agreement are contingent on Board approval of the CN/IC consolidation. CPR and NSR insist, however, that this does not alter their analysis; the context and terms of the two agreements, CPR and NSR argue, strongly suggest that CN and KCS elected to make the Access agreement contingent on Board approval of the proposed consolidation both to minimize potential concerns about possible unlawful premature CN control of IC and to avoid Board review of the reciprocal trackage rights grants as "related" transactions in this proceeding.

²⁰ CPR and NSR claim that the materials relating to the negotiation of the Alliance and Access agreements are needed: to enable a clear understanding of the purposes the Alliance and Access agreements were intended to accomplish, and what their relationship is to the proposed CN/IC consolidation; to determine whether the "transaction" properly at issue in this proceeding includes, or does not include, the Alliance and Access agreements; and to determine whether the Alliance, in combination with the CN/IC consolidation, is the equivalent of a three-carrier merger requiring Board approval.

²¹ CPR and NSR contend that applicants' entirely voluntary decision to intertwine the Alliance/Access agreements and the CN/IC consolidation (by "permeating" the CN/IC application with references to and analyses of the Alliance and Access agreements) amounted to a waiver of any otherwise applicable settlement privilege.

²² CPR and NSR insist that, if applicants and KCS had wished to preserve their claim of privilege, they should have followed the normal procedures applicable in matters of this sort (i.e., they should have secured the practical equivalent of a stay by withholding production of the disputed
(continued...)

regarding other parties' use of Alliance/Access negotiation materials in their evidentiary submissions cannot properly be asserted in the form of a motion in limine, but should instead be asserted in the rebuttals that will be filed by applicants and KCS, or in appropriate motions to strike.²³

The RUB-12 Reply. Rubicon and Uniroyal urge the denial of the CN/IC-27 appeal for the reasons stated in the CPR-10 reply.

The UP-7 Reply. UP believes that there is no need to determine whether Judge Harfeld was correct when he ruled that the settlement privilege did not apply to the negotiation of the Alliance and Access agreements and that applicants had in any event waived any such privilege. Those questions, UP insists, have been rendered moot by the production, by applicants and KCS, of the materials at issue. UP argues: that the settlement privilege is a qualified discovery privilege applicable to confidential settlement materials, not an evidentiary rule that prevents such material from becoming part of the evidentiary record before a finder of fact; that, once a party has chosen to produce confidential information related to asserted settlement negotiations, the privilege against discovery is necessarily lost; and that, therefore, whatever tactical objectives applicants and KCS may have had for producing documents and permitting deposition testimony concerning the subjects assertedly covered by settlement privilege, their conduct has destroyed the privilege and has mooted their appeal.

DISCUSSION AND CONCLUSIONS

Interlocutory appeals from discovery decisions issued by Judge Harfeld are governed by the stringent standard of 49 CFR 1115.1(c): "Such appeals are not favored; they will be granted only in

²²(...continued)
materials and filing a timely appeal).

²³ CPR and NSR insist that the request for an order barring the use of negotiation materials is in the nature of a motion in limine; and such a motion, CPR and NSR argue, has no place in agency proceedings. See Seaboard Air Line Railroad Company -- Merger -- Atlantic Coast Line Railroad Company (Petition to Remove Traffic Protective Conditions), Finance Docket No. 21215 (Sub-No. 5), slip op. at 1 (ICC served Mar. 22, 1994) ("[S]ubsequently striking any material that might turn out to be unduly broad will be a suitable remedy. The Commission is an administrative agency with expertise in transportation law, not a jury composed of laymen that must be protected from seeing inadmissible material."). See also CSX Corporation and CSX Transportation, Inc., Norfolk Southern Corporation and Norfolk Southern Railway Company--Control and Operating Leases/Agreements--Conrail Inc. and Consolidated Rail Corporation, STB Finance Docket No. 33388, Decision No. 51, slip op. at 2-4 (STB served Nov. 3, 1997) (motions in limine are not favored in Board proceedings; the better remedy is a motion to strike, filed subsequent to the submission of the offending material).

exceptional circumstances to correct a clear error of judgment or to prevent manifest injustice." See Union Pacific Corporation, Union Pacific Railroad Company and Missouri Pacific Railroad Company--Control--Chicago and North Western Transportation Company and Chicago and North Western Railway Company, Finance Docket No. 32133, Decision No. 17, slip op. at 9 (ICC served July 11, 1994) (applying the "stringent standard" of 49 CFR 1115.1(c) to an appeal of an interlocutory decision issued by former Chief Administrative Law Judge Paul S. Cross).²⁴ Because the CN/IC-27 appeal filed by applicants and KCS has not met this standard, it will be denied.

We agree with applicants and KCS that the Alliance and Access agreements are bona fide settlement agreements; these agreements represent the price that applicants had to pay to secure KCS's support for the CN/IC application. And it makes no difference, for this purpose, that the arrangements provided for by the Alliance and Access agreements do not appear to be directed at any anticompetitive consequences that might arguably flow from CN/IC common control. For purposes of the settlement privilege, it is enough that the Alliance and Access agreements were intended to settle any grievances KCS might otherwise have expressed vis-à-vis the CN/IC application.

We also agree with applicants and KCS that, absent compelling circumstances, the settlement privilege that has been recognized in our precedents would bar discovery, by opposing parties, of confidential material related to the negotiation of the Alliance and Access agreements. And we further agree with applicants and KCS that the settlement privilege was not waived by the presence, in the CN/IC application, of numerous references to the Alliance and Access agreements. These references tout the benefits of the two agreements, but do not reveal (and therefore do not waive the settlement privilege with respect to) the negotiations from which these two agreements ultimately emerged.

²⁴ We have noted, in most recent "major merger" proceedings, that interlocutory appeals from discovery decisions issued by the presiding administrative law judge are governed by the 49 CFR 1115.1(c) standard. See, e.g., CSX Corporation and CSX Transportation, Inc., Norfolk Southern Corporation and Norfolk Southern Railway Company--Control and Operating Leases/Agreements--Conrail Inc. and Consolidated Rail Corporation, STB Finance Docket No. 33388, Decision No. 6, slip op. at 7 (STB served May 30, 1997). See also Union Pacific Corporation, Union Pacific Railroad Company, and Missouri Pacific Railroad Company--Control and Merger--Southern Pacific Rail Corporation, Southern Pacific Transportation Company, St. Louis Southwestern Railway Company, SPCSL Corp., and The Denver and Rio Grande Western Railroad Company, Finance Docket No. 32760, Decision No. 6, slip op. at 13 (ICC served Oct. 19, 1995); Burlington Northern Inc. and Burlington Northern Railroad Company--Control and Merger--Santa Fe Pacific Corporation and The Atchison, Topeka and Santa Fe Railway Company, Finance Docket No. 32549, Decision No. 10, slip op. at 9-10 (ICC served Mar. 7, 1995).

We agree with the opposing parties, however, that, in the rather unusual context of the present case, Judge Harfeld's override of the settlement privilege was not a clear error of judgment and did not result in manifest injustice. It is clear that opposing parties intend to argue that the "transaction" at issue in this proceeding is a CN/IC/KCS transaction, not the CN/IC transaction presented by applicants. We do not intend to prejudge this argument; it suffices for present purposes merely to observe that, in the present state of the record, the argument is not entirely frivolous. In this context, therefore, we cannot brand as either "a clear error of judgment" or a "manifest injustice" Judge Harfeld's determination that the settlement privilege must yield to the need for discovery of the purposes the Alliance and Access agreements were intended to accomplish.

Given our resolution of the issues raised by the CN/IC-27 appeal, we have no occasion to address the argument that applicants and KCS, by producing documents and permitting deposition testimony concerning the subjects assertedly covered by settlement privilege, have destroyed the privilege and mooted their appeal.²⁵ Our denial of the CN/IC-27 appeal will allow opposing parties to use, in their evidentiary submissions, relevant information concerning the negotiation of the Alliance and Access agreements. Much of the information concerning negotiation may be of limited, if any, relevance to the matters at issue in this proceeding. We are prepared to entertain motions to strike if opposing parties present, in their evidentiary submissions, information that is not relevant to these matters. In view of the need for expeditious resolution of discovery disputes, the parties to this proceeding may wish to pursue, even at this late date, the establishment of discovery guidelines similar to those that have been used in prior proceedings.²⁶

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

It is ordered:

1. The CN/IC-27 appeal is denied.

²⁵ Given our resolution of the issues raised by the CN/IC-27 appeal, we also have no occasion to address: the arguments raised by applicants and KCS in their "reply" (designated CN/IC-29 and KCS-9) filed October 14, 1998; and the request by applicants and KCS for a waiver of the 49 CFR 1104.13(c) "reply to a reply" prohibition with respect to that "reply."

²⁶ See, e.g., CSX Corporation and CSX Transportation, Inc., Norfolk Southern Corporation and Norfolk Southern Railway Company--Control and Operating Leases/Agreements--Conrail Inc. and Consolidated Rail Corporation, STB Finance Docket No. 33388, Decision No. 10 (STB served June 27, 1997).

STB Finance Docket No. 33556

2. This decision is effective on the date of service.

By the Board, Chairman Morgan and Vice Chairman Owen.

Vernon A. Williams
Secretary