STB FINANCE DOCKET NO. 33388 (SUB-NO. 90)

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
(BUFFALO RATE STUDY)

Decision No. 4

Decided July 6, 2000

Board completes initial phase of 3-year review of Buffalo-area rates and switching fees following implementation of the "Conrail" merger.

BY THE BOARD:

One of the conditions we imposed in our decision approving the acquisition of control of Conrail by CSX[1] and NS[2] was a 3-year study of rail rates in the Buffalo, NY area (the Buffalo Rate Study or the Study) to follow the division of Conrail's assets, which occurred on June 1, 1999, (Split Date). We initiated our Buffalo Rate Study in *CSX Corp. et al. — Control — Conrail Inc. et al. — Buffalo Rate Study*, 4 S.T.B. 456 (1999) (*Decision No. 1*), and published at 64 Fed. Reg. 71,188 (1999), to examine linehaul and switching rates for rail movements into and out of the Buffalo area. We required CSX and NS to submit certain information and requested public comments to develop a more complete record. For the initial 6-month review, we required the carriers to provide all interested parties and the Board's staff 100% waybill files for the period beginning June 1, 1997, and ending November 30, 1999.

In Decision No. 2, served December 28, 1999,[3] at the request of CSX and NS, we extended by 4 weeks the due dates applicable to the initial 6-month review. In Decision No. 3, served February 24, 2000, at the request of the

[1] CSX Corporation and CSX Transportation, Inc., are referred to as CSX.

[2] Norfolk Southern Corporation and Norfolk Southern Railway Company are referred to as NS.

[3] Decision No. 2 was published at 65 Fed. Reg. 319 (2000).

Erie-Niagara Rail Steering Committee (ENRS), we further extended the deadlines applicable to comments and replies.[4]

DISCUSSION AND CONCLUSIONS

Overview

This decision completes the initial phase of our 3-year Buffalo Rate Study. As explained below, CSX and NS have developed a methodology that enables them to use rail waybill data to estimate rate trends for rail movements into and out of the Buffalo area for the period 2 years prior to and 6 months following the June 1, 1999, integration of Conrail into CSX and NS. The railroads present evidence to show that those rates have, on average, been reduced over this period. While the methodology appears to have been properly developed and applied, we await a full record of public comment on CSX's principal evidentiary submission, which appeared in CSX-2, its May 12, 2000, reply statement. We look forward to the development of a more complete public record as our Buffalo Rate Study moves into its next phase, rebased on a 12-month period ending on May 31 of each year of the 3-year study period (*i.e.*, May 31, 2000, May 31, 2001, and May 31, 2002).

CSX and NS have also submitted evidence to show that each is in compliance with all of the conditions related to switching that we imposed in the Buffalo area.[5] While the level of the switching rates in general and the scope of

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[4] CSX and NS submitted their comprehensive filings on February 11, 2000. *See,* CSX-1 (highly confidential version and redacted public version) and NS-1 (highly confidential version and redacted public version). ENRS filed comments on April 12, 2000. *See,* ENRS-1 (highly confidential version) and ENRS-2 (redacted public version). In a letter filed April 13, 2000, the United States Department of Transportation (DOT) advised that, although it takes no position on the competitive implications of the traffic data submitted by CSX and NS, DOT intends to submit substantive comments after reviewing the information covering the next phase of this oversight proceeding. CSX and NS filed separate replies to ENRS' comments on May 12, 2000 (CSX-2 and NS-2).

[5] Conrail's switching fees had been $450 within its Buffalo switching district and $390 at other points in the Niagara frontier area. A settlement agreement with the National Industrial Transportation League (NITL) retains switching for 10 years by CSX and NS for all facilities that received switching by Conrail to either of those carriers, and provides for an inflation-adjusted fee no higher than $250 for the first 5 years. We extended the switching component of the NITL agreement to situations where shortlines paid switching charges to Conrail and where Conrail received switching services from CSX or NS. *See, CSX Corp. Et Al. — Control — Conrail Inc. Et Al.*, 3 S.T.B. 196 (1998), Decision No. 89 *(Conrail)*, at 255. We also extended the NITL agreement (continued...)

the traffic covered by the Buffalo-area switching conditions we set in *Conrail* have been disputed by ENRS, there is no claim on this record that any local business or railroad does not have available the switching rate to which it is entitled pursuant to *Conrail.*

ENRS has also attempted to introduce into this Buffalo Rate Study its concerns with the deteriorating rail service levels that have plagued CSX, NS and their customers in the period immediately following the integration of Conrail into CSX and NS. As explained more fully below, we find that the proper forum for the service issues raised by ENRS is our *Conrail* general oversight proceeding, STB Finance Docket No. 33388 (Sub No. 91) (*General Oversight*).

Assessing Buffalo-Area Rate Trends

The Initial NS Submission. In its initial submission (NS-1), NS presented and applied a methodology — later adopted, with certain modifications, by CSX — that used rail waybill data to measure rate trends for rail movements into and out of the Buffalo area for the period 2 years prior to and 6 months following the June 1, 1999, integration of Conrail into CSX and NS.[6] NS examined rates for its "major movements" into and out of Buffalo. These were defined as movements into or out of the Buffalo area of a "commodity" (identified through use of 4-digit Standard Transportation Commodity Codes (STCC codes)) that generated revenues exceeding $20,000 for the 6 months subsequent to the Split Date. The 190 major movements identified by NS generated $44.2 million in revenue for that 6-month period, or about 90% of NS' total linehaul revenue from its movements into and out of Buffalo.

NS stated that its examination of these waybill data showed that, for its major movements, "linehaul rates to and from stations in the Buffalo area since June 1, 1999, have, for the most part, been the same as or lower than Conrail and/or NS rates for the same movements before June 1, 1999," [NS-1 at 2] and

[5](...continued)
to certain international rail movements into and out of Niagara Falls (*id.* at 287).

While the NITL agreement covered only post-integration switching by CSX for NS and NS for CSX, CSX explained that it had also negotiated voluntary agreements with both Canadian National Railway Company and its affiliates (collectively, CN) and Canadian Pacific Railway Company and its affiliates (collectively, CP) that provide lower switching fees for enlarged volumes than formerly available to CN and CP from Conrail in the Greater Buffalo area. In addition, the agreements provide increased access to CN and CP for cross-border truck competitive traffic. We imposed these CN and CP settlements as conditions to our approval of the transaction.

[6] The NS rate study was conducted by The Woodside Consulting Group and presented in the Verified Statement of John H. Williams.

that "no meaningful conclusions concerning rate trends could be determined" for the remaining non-major movements. NS-1 at 11.

ENRS' principal criticism of the NS rate study is that it did not disaggregate post-Split Date NS movements into those that were NS movements pre-Split Date and those that were Conrail movements pre-Split Date. We agree, however, with NS that it should not have ignored, and need not have separately computed, rate trends for what constitutes most of NS' major Buffalo-area movements — linehaul movements handled by NS both before and after the Split Date.[7] This is not a study of rate trends for only Buffalo-area traffic that formerly moved over Conrail. Instead, we have required CSX and NS "to submit information sufficient for us to determine the trend in rates for rail movements into and out of the Buffalo area for the period beginning June 1, 1997," [*Decision No. 1*, at 459], for the purpose of permitting us to determine "whether Buffalo-area shippers will be subjected to higher rates as a result of this transaction." *Conrail*, at 288-289.

The Initial CSX Submission. In its initial submission, CSX presented only generalized information about the large share of Buffalo-area traffic that it inherited from Conrail. As ENRS explains:

> CSX's eleven-page Initial Report presents no detailed revenue and traffic data or other evidence that could be used to determine or accurately evaluate whether or not freight rates in the Niagara Frontier area have increased, decreased or remained constant since the June 1, 1999 split date.

ENRS-2 , V.S. Hines, Sr., at 7. Perhaps to fill this data void, ENRS has presented the results of a shipper survey conducted by R. L. Hines & Associates, which is used to buttress ENRS' claim that many rail shippers in the Buffalo area have incurred rate increases since the Split Date and that the railroads have indicated that additional rate increases can be expected in the near future.

The ENRS Survey. The dominant theme of the ENRS survey is the service concerns of Buffalo-area rail shippers. We address this subject below. With respect to the small component of the survey addressed to rates, CSX states, and we agree, that the "survey provides no information that would allow the Board

[7] ENRS concedes that this concern is not relevant to the larger share of Conrail's Buffalo-area traffic that has been inherited by CSX, since CSX had only a minor presence in the area prior to taking over its Conrail lines. *See*, ENRS-2, V.S. Hines, Sr., at 12.

to assess the validity or magnitude of purported rate increases." CSX-2 at 5. As CSX has explained:

> The survey makes no attempt to establish that the 43 shippers are representative of CSXT and NS shippers. There is no explanation of the selection process, the criteria used to identify participants, the number of shippers who were asked to participate, the amount of traffic moved by such participants or the percentage of participants who responded.

CSX-2 at 5. Further, CSX states that a letter from CSX to its rail customers warning of future rate increases and introduced into the record by ENRS "was addressed to *all* CSXT customers over its 23-state service network. That letter concerned a *system-wide cost recovery* increase that would apply to various commodities for all shippers. That increase has nothing to do with the transaction and is not in the least targeted at Buffalo. [*Bold in original.*]" CSX-2 at 10. We agree that our Buffalo Rate Study is not intended to focus on whether the rapid and significant rise in diesel fuel prices, or any other adverse industry-wide cost trends, are eventually reflected in rail rates.

As noted above, the dominant theme of the survey is the service concerns of Buffalo-area shippers. ENRS explains why it believes that these service data are relevant to our Buffalo Rate Study:

> Even if rates were found to have remained fairly static since the split date, the deterioration of railroad service would have resulted in *de facto* rate increases for railroad customers in the Niagara Frontier area. As indicated recently in a letter from Congressman Jack Quinn to Chairman Linda Morgan, "they are paying the same, but getting less – which is an effective rate increase."[8]

ENRS-2, V.S. Hines, Sr., at 5. The system-wide service problems that were unfortunately the result of the early stages of the integration of Conrail into NS and CSX have caused serious and significant concerns for us, for the railroads, and, most notably, for their customers. But the evidence presented by ENRS does not purport to show that service deterioration in the Buffalo area was the result of any new market power inadvertently conferred by the Conrail transaction on CSX and NS, and through which the railroads could, in lieu of enhancing profitability by raising rates, choose to achieve that goal by lowering costs through a strategy of steadily declining service levels. Instead, the service problems have been system-wide, and have resulted in significant costs for both the railroads and their customers. The railroads are working diligently to

[8] We have made the correspondence between Congressman Quinn and Chairman Morgan a part of the public docket for this Buffalo Rate Study proceeding and for the Conrail general oversight proceeding.

overcome these service problems, and these efforts should prove successful well before the end of our 3-year Buffalo Rate Study. Further, the remedy that ENRS continues to seek, increased rail access for Buffalo-area shippers, does not purport to address the service concerns that have been presented on this record. Most notably, ENRS' preferred "remedy" for Buffalo-area shippers is the creation of a new Shared Assets Area (SAA), yet coordinating service in the SAAs initiated by the Conrail transaction has been part of the challenge in implementing that transaction.

Thus, we have determined that the proper forum to address the service concerns of Buffalo-area shippers is our Conrail general oversight proceeding:

> Other Buffalo-area matters specifically regarding the progress of implementation of the Conrail transaction and the workings of the various merger conditions should be submitted in the STB Finance Docket No. 33388 (Sub No. 91) general oversight proceeding.

General Oversight, 4 S.T.B. 491 (2000), at 494-95. Further, we have recently initiated another separate proceeding — *CSX Corp. et al. — Control — Conrail Inc. Et Al. — Buffalo Infrastructure*, 4 S.T.B. 917 (2000) [*Buffalo Area Infrastructure*] — to provide a forum for addressing those specific concerns of Buffalo-area shippers that link poor rail service to inadequate rail infrastructure.

The CSX Reply Comments. As noted above, we await a full record of public comment on CSX's principal evidentiary submission, which appeared in CSX-2, its May 12, 2000 reply comments.[9] We look forward to the development of a more complete public record as our 3-year Buffalo Rate Study moves into its next phase, rebased, as noted above, on a 12-month period ending on May 31 of each year.

CSX followed the methodology set out in NS' initial submission, but with certain modifications.[10] Like NS, CSX first examined all 1,703 "commodity"

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[9] The CSX rate study was conducted by Klick, Kent & Allen, Inc., a wholly owned subsidiary of FTI Consulting, Inc, and presented in the Verified Statement of John C. Klick and Michael J. Boyles.

[10] For example, rather than compare rates for Conrail movements during the 2 pre-Split Date years to CSX rates for the first 6 post-Split Date months, CSX separately showed that the Conrail rates had increased only fractionally (*i.e.*, by 0.1 percent) over the 2 pre-split years, and then focused its assessment on the last full year of Conrail rate data and the first 6 months of post-Split Date CSX rate data. Further, unlike NS, CSX was unable to find a suitable replacement for the final 2 months of Conrail's primary waybill file that had not been properly completed. And, as explained below, while NS assessed rate trends at the 4-digit STCC level, CSX determined that its commodity (continued...)

flows (identified through use of 4-digit STCC codes) on CSX movements into and/or out of the Buffalo area for the initial 6 post-Split Date months. And, like NS, CSX identified those movements — "major movements" — that generated more than $20,000 in revenues. The 522 "major movements" generated revenues of $83.4 million, and represented 93% of CSX's total Buffalo-area linehaul revenues.

Like NS, CSX had to determine the proper pricing basis for each movement. The waybill data provide revenues and tons per car, and the railroads' marketing departments were used to determine if the proper pricing basis for a particular commodity flow was a rate per ton or a rate per carload. Unlike NS, CSX found that the proper pricing basis for many of its Buffalo-area movements, most notably its chemicals traffic, could only be determined at the 7-digit STCC level.

CSX's 522 Buffalo-area "major movements" at the 4-digit STCC level corresponded to 788 movements at the 7-digit level. CSX focused its assessment of Buffalo-area rate trends on the 341 of these 7-digit STCC movements that had a pre-Split Date counterpart movement on Conrail.[11]

Like NS, CSX had to seek advice from its marketing personnel to deal with measurement problems inherent in using waybill data to estimate rate trends. CSX states that it sought to properly take into account rate variations based on minimum weights, car ownership, equipment type and size, volume discounts, and differing patterns of mileage allowance payment, and that additional problems that had to be overcome were related to the fact that the underlying Conrail and CSX waybill data were not consistently developed.[12]

After adjusting for all the anomalies in the databases, CSX concludes that its rail linehaul rates for the 341 major movements into and out of the Buffalo

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[10](...continued)
ratesetting process required it to disaggregate commodity flows to the 7-digit STCC digit level in order to accurately measure rate trends.

[11] CSX states that it did not anticipate that such a large percentage of its post-split Buffalo-area major movements would not have a pre-split counterpart on Conrail. It asserts that this finding "is a strong indication that shippers in this area are experiencing additional forms of benefits from the Conrail Transaction, *i.e.*, the ability to access new sources of supply for inbound products and new markets for outbound production * * *. CSX's ability to offer single-line service over longer hauls and its aggressive pursuit of business that Conrail had not sought are the major factors driving this trend." CSX-2, V.S. Klick and Boyles, at 11.

[12] For example, Conrail and CSX each used different Freight Station Accounting Codes to designate origin or destination points in their respective waybill files. And for certain commodity flows, the pre-split Conrail waybill revenues might represent revenues for the entire movement, while the post-split CSX waybill revenues might represent some form of multi-factor pricing and thus just show CSX's revenue share, suggesting a rate reduction when none had occurred; for other commodity flows, the reverse might be true.

area that had pre-Split Date counterparts on Conrail declined 8.9% over the first 6 post-Split Date months when compared to rates for those same movements in the 12 months prior to the Split Date, with rates decreasing on 105 (30%) of those movements and increasing on only 26 (7.6%). CSX asserts that, of the 26 movements where rates increased, only 2 had increases greater than 8%. For most of its major movements into and out of the Buffalo area, CSX states that it continued to charge the same rates that Conrail had charged, subject only to preexisting inflation adjustment provisions governing those rates.

Conclusions. This decision completes the initial phase of our 3-year Buffalo Rate Study. CSX and NS appear to have set out and applied an acceptable methodology for measuring rail linehaul rate trends into and out of the Buffalo area for the period preceding and following the division of Conrail's assets by and among CSX and NS. The railroads present evidence to show that, through the first 6 months following the division of Conrail, those rates have, on average, been reduced. We await a full record of public comment on CSX's principal evidentiary submission.[13] We look forward to a more complete public record as our Buffalo Rate Study moves into its next phase, rebased on a 12-month period ending on May 31 of each year.

We also find that CSX and NS are in compliance with all conditions related to switching that we imposed in the Buffalo area.

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

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[13] CSX has suggested that the difficult and laborious task of comparing Conrail and CSX waybill records could be eliminated in some later phase of this Buffalo Rate Study by focusing only on the more internally consistent CSX post-split waybill records:

> Having established that rates to and from the Buffalo/Niagara Falls area have not increased as a result of the initial transfer of its portion of Conrail to CSX — as we do in the balance of this verified statement — there may be more efficient (and more meaningful) ways to conduct * * * the future comparisons necessary to complete the three year study.

CSX-2, VS Klick and Boyles, at 11, fn. 6. We will not consider this suggestion until we have had the opportunity to review a full public record on this matter.

It is ordered:

1. The 3-year Buffalo rate study will continue, in accordance with the schedule set out in Decision No. 1 of this proceeding.

2. This decision is effective on July 7, 2000.

By the Board, Chairman Morgan, Vice Chairman Burkes, and Commissioner Clyburn.