STB FINANCE DOCKET NO. 33388 (SUB-NO. 91)

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
(GENERAL OVERSIGHT)

Decision No. 3

Decided November 29, 2000

The Board denies the request by Indiana Power and Light Company for imposition of additional conditions on the CSX/NS/Conrail merger.

BY THE BOARD:

In this decision concerning oversight of *CSX/NS/Conrail*[1] merger conditions related to Indianapolis Power and Light Company (IP&L), we are denying that company's request that we impose additional conditions.

BACKGROUND

In Decision No. 89 in the *CSX/NS/Conrail* proceeding, 3 S.T.B. 196 (1998), we approved, subject to various conditions (including, but not limited to, a 5-year general oversight condition): (1) the acquisition of control of Conrail Inc., and Consolidated Rail Corporation (collectively, Conrail) by (a) CSX Corporation and CSX Transportation, Inc. (collectively, CSX) and (b) Norfolk Southern Corporation and Norfolk Southern Railway Company (collectively, NS); and (2) the division of the assets of Conrail by and between CSX and NS. The acquisition of control of Conrail by CSX and NS took place on August 22, 1998 (this is the date that has been referred to as the Control Date). The division of the assets of Conrail by and between CSX and NS took place on June 1, 1999 (this is the date that has generally been referred to as Day One; it has also been

[1] *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 (*CSX/NS/Conrail*).

referred to as the Closing Date and the Split Date). In approving that transaction, we imposed certain conditions, among others, at the request of IP&L.[2]

IP&L is an electric utility company operating two coal-fired plants in the Indianapolis area. The Stout plant is served directly only by The Indiana Rail Road Company (INRD), an 89%-owned CSX subsidiary that provides single-line service from Southern Indiana coal fields. The Perry K plant is located on a former Conrail line that was obtained by CSX through this transaction. We imposed a condition at Stout even though that plant was solely served by INRD both before and after the transaction. We agreed with IP&L's argument that it could credibly threaten to build a rail connection to nearby Conrail lines, and that that threat had induced INRD to publish what IP&L characterized as very competitive switching charges[3] permitting Conrail (and its joint line partner Indiana Southern Railroad, Inc. (ISRR)) access to the Stout plant. To preserve that competition at Stout, we preserved IP&L's build-out option, making available to it trackage rights for it to be served by a second carrier such as ISRR or NS in the event that IP&L actually does construct the build-out that it said was feasible.[4] As an additional safeguard suggested by the U.S. Department of Justice, we gave NS trackage rights over certain of CSX's lines, including INRD, thus permitting NS to reach the Stout plant directly. In conjunction with this additional remedy, we permitted NS to interchange coal traffic at milepost 6 with ISRR, which also originates the Southern Indiana coal that IP&L currently prefers.[5] We found no need to impose specific conditions concerning the Perry K plant because it was solely served by Conrail before and it now would be solely served by CSX.[6]

In *CSX/NS/Conrail* Decision No. 96, 3 S.T.B. 764 (1998), we denied IP&L's requests for additional relief at Stout and Perry K. We also found that milepost 6 may not be a feasible point of interchange for an NS/ISRR joint-line service, and we directed CSX, NS, and ISRR to negotiate an appropriate solution and report back to us. In *CSX/NS/Conrail* Decision No. 115, 4 S.T.B. 25 (1999),

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[2] This decision will deal only with oversight issues relating to IP&L. We will address other oversight issues in a separate decision.

[3] "Switching" is a railroad service performed under yard rules and regulations. It can involve assembling or classifying or changing the position of rail cars. Here, it involves those car movements necessary to complete the through transportation into (and out of) Stout.

[4] Alternatively, one of these carriers could build in to the Stout plant. The trackage rights to connect the build-out point to ISRR or NS would be necessary because the (formerly independent) nearby Conrail lines are now under the control of CSX.

[5] IP&L has acknowledged that it will likely be forced to obtain coal from other lower-sulphur sources in the near future to comply with the Clean Air Act.

[6] We accepted applicants' offer, and imposed it as a condition, that CSX would make permanently available cost-based switching at Perry K. We found that this arrangement would improve the pre-transaction competitive situation at Perry K.

we noted our approval of a plan negotiated among these parties to interchange traffic at Crawford Yard,[7] instead of at milepost 6. In *CSX/NS/Conrail* Decision No. 125, 4 S.T.B. 101 (1999), we again denied IP&L's request for further conditions. While IP&L argued that NS could not compete for its traffic at Stout, we concluded that "it is too early to determine whether the new NS-ISRR service that will result from our remedial condition will work as we intended to preserve the competition that Conrail had provided at Stout."

In *CSX/NS/Conrail* Decision No. 89, we imposed a 5-year oversight condition requiring CSX and NS to report annually on their progress in implementing the transaction and carrying out the various conditions that we imposed.[8] CSX and NS filed their first annual oversight reports on June 1, 2000 (CSX-1 and NS-1); IP&L filed a response on July 14, 2000 (and supplemented by letter dated July 27, 2000); ISRR filed comments on July 14, 2000; CSX and NS filed reply comments on August 3, 2000 (CSX-2 and NS-2); IP&L submitted an additional letter comment on August 14, 2000; NS (undesignated) and CSX (CSX-3) responded on August 23, 2000.

THE OVERSIGHT PLEADINGS

NS' First Annual Report (NS-1). NS notes that it has not yet provided service to Stout, because IP&L has committed that traffic under contract to INRD. But NS states that "it will be able to compete head-to-head against CSXT eastern-origin coal for service to Stout from NS coal origins in the east once the IP&L/INRD contract expires."

CSX's First Annual Report (CSX-1). CSX states that it has directed its affiliate INRD to enter a trackage rights agreement with NS to permit service to Stout, and that the fee negotiated is $.35 per car mile. CSX notes that all of the coal to Stout continues to be moving under the pre-transaction INRD contract, while all the coal to Perry K continues to originate on ISRR, with delivery now by CSX instead of Conrail.

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[7] Crawford Yard was the interchange point suggested by IP&L.

[8] We instituted the oversight proceeding in Oversight Dec. No. 1, *CSX Corp. et al. — Control — Conrail Inc. et al. — General Oversight*, 4 S.T.B. 491 (2000), and published at 65 Fed. Reg. 7414 (2000). In Oversight Dec. No. 2 (STB served May 30, 2000), we granted in part IP&L's request relating to our oversight process.

IP&L's Comment.[9] IP&L makes numerous arguments in aid of its renewed request to obtain further conditions. With regard to its Stout plant, IP&L objects that the trackage rights fee for NS' service to Stout over the tracks of INRD is $.35, not the $.29 per car mile that NS and CSX have agreed will be charged when one exercises trackage rights over the other pursuant to the overall CSX/NS/Conrail transaction. IP&L notes that, although the Board found the $.29 fee to be reasonable, it has not ruled on a $.35 fee. Although IP&L fails to provide any detailed analysis to show that the $.35 fee level is unreasonable, it suggests that, if NS has to pay this higher trackage rights fee to INRD, it will be difficult for NS and ISRR to offer a joint rate competitive with INRD's single-line rate for moving Southern Indiana coal to Stout.

IP&L also complains that, if NS uses an INRD switching service to serve Stout, instead of using its trackage rights over INRD, the switching charge will be subject to increase under a (higher) Rail Cost Adjustment Factor[10] that is unadjusted for productivity (RCAF-U) rather than a (lower) RCAF that is adjusted for productivity (RCAF-A). IP&L further argues that, if NS permits its competitor, CSX/INRD, to switch the traffic from the junction with ISRR to Stout, then CSX may impose a second switching charge for its portion of the move. IP&L argues that, if NS operates in this fashion, NS is not really interested in competing with CSX.

IP&L's main argument is that NS has not negotiated aggressively for IP&L's traffic at Stout, allegedly signaling that NS is not in a position to compete effectively for this traffic. IP&L points out that the rates that NS/ISRR has offered so far for moving coal to Stout substantially exceed the rates IP&L is paying for similar service under contract with INRD and rates that it paid Conrail/ISRR when it last used that service. Indeed, IP&L claims that an NS traffic manager, William Clark, has "admitted" that NS is not in a position to compete for this traffic. IP&L alleges that, when its Manager of Fuels, Michael Weaver, sought to "confirm" this understanding by letter, NS did not reply.

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[9] In a letter dated July 27, 2000, IP&L supplements its July 14 filing with a copy of CSX's July 24, 2000, letter to the Honorable Karen G. Milton, Clerk, U.S. Court of Appeals for the Second Circuit, in response to IP&L's July 18, 2000, letter to Ms. Milton addressing issues relating to the trackage rights agreement between INRD and NS.

[10] The Rail Cost Adjustment Factor, or RCAF, was established in the Staggers Rail Act of 1980 to track quarterly changes in railroad costs. While its initial purpose was to protect from challenge on rate reasonableness grounds rail tariff rate increases that reflected no more than increased costs, it has come to be used by many railroads and shippers as an aide in setting contractual terms. The Board publishes several RCAF series. RCAF-U measures changes in the cost of railroad inputs, unadjusted for productivity change. RCAF-A is formed by adjusting the RCAF-U index to reflect changes in railroad productivity. *See* 49 U.S.C. 10708.

IP&L states that, even though most of its coal bound for Stout is committed under contract to INRD, that contract will expire "in the relatively near future."

IP&L also repeats claims that it has raised and we have addressed at previous stages of this proceeding that NS cannot compete for this traffic because it has an insufficient presence in the Indianapolis area and will have to dispatch locomotives and crews from Lafayette, IN, which is 60 miles away. IP&L argues that the interchange between NS and ISRR at CSX's Crawford Yard will be inefficient because CSX is permitting ISRR to enter the yard with coal trains bound for Stout only when NS has arrived and is ready to make the interchange. (This arrangement is referred to by the parties as a "headlight-to-headlight" interchange.)

Although we found that the transaction would not impair competition at Perry K and found that no relief was necessary, IP&L now suggests that NS' rates to that plant have risen dramatically. This allegation is based on IP&L's calculation of the initial rate offer of NS (discussed above) for moving coal to Stout, plus the cost of transferring the coal to truck and then trucking the coal from Stout to Perry K. IP&L asks for us to permit ISRR direct access to both the Stout and Perry K plants with a trackage rights fee not to exceed $.29 per car mile.

ISRR Comment. ISRR states that it continues to be interested in handling the non-contract traffic at Stout, and is interested in bidding on all of the traffic in the near future when the contract expires. ISRR repeats its arguments, made and addressed by us in earlier stages of this proceeding, that NS will be operationally handicapped in competing for the Stout traffic in joint line service with ISRR.

NS' Reply (NS-2). NS responds that it has "vigorously pursued" IP&L's business, and that it can provide a competitive service to Stout if given a fair opportunity. NS states that INRD's $.35 per car mile trackage rights fee, which it notes is only $.004 per ton higher than the $.29 per car mile fee that the Board already found reasonable between NS and CSX, will not be any impediment to its provision of competitive service. NS emphasizes that it has consistently advised IP&L that it would need information about IP&L's service requirements and volume commitments to determine the most competitive possible rate for Stout, but that IP&L has never provided that information. NS argues that any rates for service to Stout that it has quoted so far have been on a "worst case" basis, predicated upon low volumes, and sporadic, and unpredictable service requests. NS admits, as it has previously, that the fact that its closest presence is 60 miles away in Lafayette presents a challenge, but it still believes that a

competitive joint service in conjunction with ISRR is entirely feasible.[11] Finally, NS claims that IP&L has been more interested in attempting to prove that NS cannot compete than it has in attempting to work out a competitive alternative.

CSX's Reply (CSX-2). CSX claims that IP&L is not yet seriously negotiating with NS for movements to Stout because substantially all of that coal is under contract to INRD; it suggests that bids for service to Stout have been solicited for "forensic use" only, and that the real test will come when the contract expires and this traffic is rebid.

With regard to the trackage rights fee for NS service over INRD's line, CSX argues that the $.35 per car mile fee is below the out-of-pocket costs of INRD.[12] It also notes that the Board itself developed average trackage rights costs of $.46 and $.40 for Conrail and NS respectively in Decision 89, at 347, which means it would be cheaper for NS to operate over INRD's lines here than it typically is to operate over NS' own lines. CSX also points out that, under Condition No. 23, IP&L, not NS or INRD, has the choice of whether operations over INRD are to be accomplished by trackage rights or by switching. With regard to the switching charge, the Hoback verified statement indicates that NS and INRD have agreed to maintain the same rate that Conrail charged before the transaction.

With regard to Perry K, CSX notes that IP&L pays the same rate for rail transport of ISRR/CSX coal that it paid for similar ISRR/Conrail movements before the transaction because CSX has simply adopted Conrail's tariff. (CSX notes that these rates contain no RCAF adjustment.)

IP&L's Letter. In its August 14 letter, IP&L states that it never received two reply letters asking for more information about service requirements and volume commitments that NS claims that it sent during the course of rate negotiations concerning service to Stout. IP&L argues that "circumstantial evidence," including the fact that the copies of the letters included in NS' filing were not signed, supports the inference that these letters were never sent.

NS' Response. NS replies that it did send the letters, and that executed copies were not available when it filed its reply statement because the office of Mr. Clark (who sent the letters) was being relocated. It attached these executed copies to its response.

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[11] NS points out that most of the move would be over ISRR, with a major division of the rate going to that carrier, and that NS must reach agreement with ISRR on these and other issues.

[12] CSX submitted a verified statement of Thomas Hoback, president of INRD, detailing those costs.

CSX's Response (CSX-3). CSX advises that it has no knowledge whatsoever respecting the authenticity of the letters from NS' William E. Clark to IP&L's Michael A. Weaver.

DISCUSSION AND CONCLUSIONS

In approving the *CSX/NS/Conrail* transaction, we gave IP&L two alternative and self-sufficient means of ensuring that rail competition at the Stout plant is preserved. At this juncture, it does not appear to us that IP&L has made a serious enough attempt to take advantage of either of these remedies. Rather, its efforts seem to have been more devoted to attempting to obtain additional conditions. Perhaps it is not surprising that IP&L has not yet made a serious enough effort to use those remedies, because nothing has changed since our approval of the transaction with regard to those competitive factors affecting coal movements to Stout.

IP&L's pre-transaction contract with INRD at Stout is still in effect, and IP&L continues to receive all of its coal at Stout under that contract and under those rates. The threat of a build-out, which IP&L itself said made INRD offer what IP&L described as very attractive switching charges that made possible alternative rail service to Stout, has been preserved by the Board's condition, which means that INRD should have the same incentive to continue to agree to reasonable switching charges as it did before the transaction. Indeed, the record here shows that INRD has agreed to maintain precisely the same switching charge for NS that it had for Conrail.[13]

The only remaining uncertainty in this case is whether NS/ISRR will be able to provide a realistic competitive counterweight to INRD's efficient single-line service at Stout to the extent that Conrail/ISRR did before the transaction. We recognize that there is some dispute on the record about the exact state of negotiations between NS and IP&L, and particularly about certain letters that NS claims it sent to IP&L during the course of their rate negotiations. Because NS' witness has sworn under oath that the letters were sent, and because NS has provided signed copies of these letters for the record, we accept the assertion that they were sent. More importantly, we also know that, whether it received these letters or not, IP&L was keenly aware that any rate NS/ISRR could offer would be dependent upon the volumes that IP&L would commit, and the frequency of service it would require. That information, which every sophisticated shipper knows is crucial to both the competitive and cost factors in ratemaking, was never supplied to NS. In any event, IP&L has those NS letters now, and the ball is clearly in IP&L's court.

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[13] The level of the actual fee is confidential, and was filed under seal.

Other arguments that IP&L raises about why NS will not be able to offer it a competitive rate at Stout are unpersuasive. As a preliminary matter, IP&L's argument — that, if NS chooses to operate using an INRD switching operation, it does not really want to compete — misses the mark. Under our Condition No. 23, applicants "must allow IP&L to choose between having its Stout plant served by NS directly [using trackage rights over INRD] or via switching by INRD * * *." Thus, it is IP&L, not NS, that makes the choice. Moreover, IP&L's criticisms of both the trackage rights fee and the switching charge that NS would pay are not well-founded. As applicants have demonstrated, the difference between the $.29 per car mile trackage rights fee that the Board has already approved as reasonable for NS' operations over CSX and the $.35 per car mile fee that NS has agreed to pay to operate over INRD translates to only $.004 per ton for this very short, less than 3½-mile movement. We do not believe that such a small cost difference would have any real impact upon NS' ability to compete.

INRD has submitted evidence and analysis that supports its position that $.35 is indeed a reasonable charge, and IP&L has submitted no particular evidence to support its supposition that it is not. In particular, INRD argues that its total out-of-pocket maintenance costs on the line ($40,000) will exceed the level of the revenue that it would accrue under this charge ($34,545) if all of the Stout traffic is diverted to NS/ISRR (15,000 carloads). If we were to allocate these maintenance costs evenly on a per car basis over INRD's total traffic (20,000 carloads), maintenance expenses related to the Stout coal movements would account for all but $4,545 of the revenues received by INRD for this traffic. If we were called upon to prescribe a reasonable trackage rights fee here, including pro rata share of a cost of capital rental element, then it is very likely that the fee would exceed $.35 per car mile.[14] Because IP&L has presented no more than a cursory challenge to this fee level, and because INRD and NS have already reached agreement, we will not consider this issue further.

With regard to the switching charge, IP&L suggests that the application of an RCAF-U inflation index could make this cost prohibitively high. We think that this is extremely unlikely given the very low existing level of the charge. A typical yearly RCAF-U adjustment to this charge would only result in a cost increase to NS of 3% - 5% more than an RCAF-A adjustment, and this difference translates to only a few pennies per ton. Moreover, IP&L has presented no evidence to lead us to believe that the RCAF-A would be a more accurate or valid way to gauge the impact of inflationary cost increases on INRD than is the

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[14] *St. Louis Southwestern Ry.Co. Compensation — Trackage Rights*, 4 I.C.C.2d 668 (1987); 5 I.C.C.2d 525 (1989); 8 I.C.C.2d 80 (1991); 8 I.C.C.2d 213 (1991) (*SSW Compensation*) (compensation standard for mandatory trackage rights set to include costs incurred, including a cost of capital rental element).

RCAF-U. Indeed, many of the productivity gains reflected in the RCAF-A are due to new labor agreements and merger synergies achieved by Class I railroads, but such gains are not achieved to anywhere near the same extent by the smaller railroads such as INRD. In sum, IP&L has failed to show that, if IP&L chooses to be served through a switching arrangement, use of the RCAF-U in this context would be unreasonable or would in any way impair NS' ability to compete effectively.

In a prior decision, we suggested that NS might find it more efficient to lease ISRR locomotives to complete the move to Stout rather than supplying its own locomotives. IP&L now argues that toilets are unavailable on ISRR locomotives, and that NS crews will thus refuse to use them to serve Stout. INRD responds that it has serviced ISRR locomotives that do have toilets, but that it has heard that ISRR has recently removed them. We need not be drawn into this dispute now. Engine service is an issue within the carriers' discretion, and we do not believe that it should be an insurmountable problem here. ISRR is a necessary party to any NS/ISRR joint rate; certain issues pertinent to the provision of this joint service are within ISRR's control, and we expect ISRR to work with NS to resolve them. It would be inappropriate to award ISRR direct access to Stout if its recalcitrance in negotiating joint-line service arrangements precluded an efficient service.

Finally, IP&L's arguments about "rate increases" at Perry K are extremely misleading. All of the coal received at Perry K continues to originate on ISRR and move under precisely the same rates that it moved under before the transaction because CSX has merely adopted Conrail's rate. IP&L's argument — based on the level of rates that it would have to pay if it were to pay NS' preliminary, worst case basis rate to Stout, pay to transfer the coal to truck at Stout, and then pay to truck the coal from Stout to Perry K — is without merit, as those charges are not in effect, and IP&L is not using that method of transportation.

In sum, IP&L has not demonstrated that it has experienced any transaction-related harm or that any additional remedies should be imposed. We have given IP&L adequate tools to ensure that competition at Stout is not reduced; it needs to use those tools.

It is ordered:

1. IP&L's request for relief, as discussed in this decision, is denied.
2. This decision is effective November 30, 2000.

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