

STB

FD-33388

7-10-98

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ID-189657

• **DENNIS J. KUCINICH**
10TH DISTRICT, OHIO

1730 LONGWORTH OFFICE BUILDING
WASHINGTON, D.C. 20515
(202) 225-5871

14400 DETROIT AVENUE
LAKEWOOD, OHIO 44107
(216) 228-8850
Office of the Secretary

189657



Congress of the United States
House of Representatives

Committees:
Government Oversight
Education
and the
Workforce

JUL 13 1998

Part of
Public Record

July 10, 1998

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Ms. Linda J. Morgan
Chairman
Surface Transportation Board
1925 K St. NW #820
Washington, D.C. 20423

Re: Docket No. 33388

Dear Ms. Morgan:

On June 30, 1998, CSX Corporation expressed its intention to retreat from environmental settlement discussions with the City of Brooklyn, a community in Ohio's 10th Congressional District that I represent in Congress. CSX defended its retreat from negotiations by citing the Surface Transportation Board's June 8, 1998, interim decision in the Conrail merger case.

Because I believe that the Board is committed to seeing that communities such as Brooklyn reach mutually acceptable settlement agreements with railroads seeking approval for mergers, I am filing this brief to ask the Board to intervene on my behalf, and on behalf of the City of Brooklyn, Ohio. Thank you very much for your attention this very important matter for my district.

Sincerely,

Dennis J. Kucinich

Dennis J. Kucinich
Member of Congress

DJK:mg
cc: Parties of Record

[PUBLIC]

BEFORE THE
SURFACE TRANSPORTATION BOARD



FINANCE DOCKET NO. 33388

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

IN RE BROOKLYN, OHIO
FILED BY CONGRESSMAN DENNIS J. KUCINICH

Dated July 10, 1998

[PUBLIC]

BEFORE THE
SURFACE TRANSPORTATION BOARD

FINANCE DOCKET NO. 33388

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

IN RE BROOKLYN, OHIO
FILED BY CONGRESSMAN DENNIS J. KUCINICH

Congressman Dennis J. Kucinich, representing the 10th Congressional District of Ohio which includes the City of Brooklyn, Ohio, hereby submits this brief in response to CSX's unilateral withdrawal from negotiations ordered by the Surface Transportation Board (STB) in Decision No. 71 and Decision No. 73.

I. STATEMENT OF FACTS

As part of the proposed acquisition of Conrail by Norfolk Southern Corporation (NS) and CSX Transportation Corporation (CSX), CSX proposed increasing the freight traffic on the Cleveland Short Line from approximately 16.4 trains per day to approximately 45.8 trains per day. This increase will have a significant impact on the City of Brooklyn, Ohio, a city in Ohio's 10th Congressional District which Congressman Kucinich represents in the U.S. House of Representatives. Congressman Kucinich brought the plight of Brooklyn to the STB's attention

through his environmental comments filed with the Section on Environmental Analysis on February 4, 1998. The SEA included information about Brooklyn in its Final Environmental Impact Statement (FEIS), issued in May 1998.

On March 17, 1998, the STB issued Decision No. 71, which ordered affected communities in the Greater Cleveland area to negotiate with the railroads in an effort to reach mutually acceptable agreements on the mitigation of adverse environmental effects of the Conrail acquisition. On March 18, 1998, Congressman Kucinich's office contacted the STB's Congressional Affairs office with a request for clarification as to the scope of Decision No. 71. Specifically, the request asked: "How long can the parties negotiate an independent settlement? Until the oral decision in June? Until the written decision in July? Or some other date?" (See Electronic Correspondence from Martin Gelfand to Nancy Beiter, Mar. 18, 1998 (Attachment 1)). In response, Nancy Beiter of the STB's Congressional Affairs office replied that

there is no deadline on a negotiated settlement. Until everyone is happy, my suspicion is that these issues will always be in litigation.

For example, in the UP/SP merger the cities of Reno and Wichita had environmental issues similar to those facing the Cleveland area now. All during the environmental review process the cities were negotiating with the carrier and they continued to do so while the various appeals from our decision went through the court of appeals. The court sent the environmental review back to us for further clarification. Still the parties have continued to negotiate.

In short, it ain't over 'til the fat lady sings and we don't know when that is.

(See Electronic Correspondence from Nancy Beiter to Martin Gelfand, Mar. 18, 1998 (Attachment 2)).

On March 20, 1998, the STB issued Decision No. 73, clarifying Decision No. 71. This decision says that Decision No. 71 was meant to be inclusive rather than exclusive. It further stated that nothing in Decision No. 71 was meant "to define who should, or should not, be involved in any specific negotiation [nor] limit the participation of any appropriate party. . . ."

(See Decision No. 73, STB Docket No. 33388, Mar. 20, 1998).

Upon learning about the STB's instruction in Decision No. 71 for the railroads and the affected communities to begin negotiations, Brooklyn Mayor John M. Coyne requested that CSX begin discussions with the City of Brooklyn to resolve environmental problems in that city associated with the increase in freight train traffic along the Cleveland Short Line. (See Letter from Mayor John Coyne to Stephen Watson, Mar. 25, 1998 (Attachment 3)). CSX Regional Vice President Stephen Watson responded that since "the City of Brooklyn was not identified in the [Draft Environmental Impact Statement] as an "affected community", nor was it so identified in the STB's Decision No. 71," CSX would not have discussions with the City of Brooklyn. (See Letter from Stephen Watson to Mayor John Coyne, Apr. 3, 1998 (Attachment 4)).

Upon learning about CSX's refusal to negotiate with Brooklyn, Congressman Kucinich contacted Surface Transportation Board Chairman Linda J. Morgan. In his April 8, 1998, letter to Chairman Morgan, Congressman Kucinich pointed out that CSX's refusal to negotiate with Brooklyn was erroneous on two counts. First, although Brooklyn was not included in the Draft Environmental Impact Statement, the STB was not unaware of the plight of Brooklyn. The STB became aware of the environmental problems associated with increased train traffic through Brooklyn because of the Congressman's February 4, 1998, environmental filing with the Section on Environmental Analysis in response to the Draft Environmental Impact Statement. (See Letter from Congressman Dennis J. Kucinich to Linda J. Morgan, Apr. 8, 1998 (Attachment 5)). Second, the scope of Decision No. 71 was not limited to the Greater Cleveland communities listed in footnote no. 1 of that decision. Rather,

Decision No. 71 was intended to facilitate negotiations among the various interested parties. It was not intended to define who should, or should not, be involved in any specific negotiations, and it was certainly not intended to limit the participation of any appropriate party in any negotiations that may be conducted. Any party that has a legitimate interest in these matters is free and indeed encouraged to participate in negotiations.

(See id.) (See also Decision No. 73, STB Docket No. 33388, Mar. 20, 1998.)

In his letter, Congressman Kucinich pointed out to the STB that the STB ordered CSX to "engage in environmental mitigation discussions with the affected communities." (See Attachment 5, supra.) Congressman Kucinich concluded in his April 8, 1998, letter:

As Congressman from Ohio's 10th Congressional District, I demand that the STB take action to assure representation for the people of Brooklyn, Ohio, in environmental mitigation discussions with CSX Corporation. I am demanding that the STB order CSX to meet with the Mayor and the people of Brooklyn for discussion about how the merger will affect Brooklyn and to order good faith settlement discussions as ordered by Decision No. 71.

(See id.) On April 13, the STB's Congressional Affairs office contacted Congressman Kucinich's staff to inform the Congressman that CSX agreed to contact the City of Brooklyn. (Telephone Correspondence between Nancy Beiter and Martin Gelfand, Apr. 13, 1998).

Between April 13, 1998, and June 30, 1998, the Mayor of Brooklyn believed, based on the foregoing, that the City and CSX were engaged in good faith negotiations. However, on June 30, 1998, CSX Vice President Michael Ruehling wrote to Mayor Coyne informing him that CSX would no longer engage in discussions with Brooklyn because the STB's oral decision of June 8, 1998, would preclude the need for any further discussion. (See Letter from Michael Ruehling to John Coyne, June 30, 1998 (Attachment 6)).

II. NEED FOR FILING

On July 6, 1998, upon receipt of the June 30 letter from CSX to Brooklyn, Congressman Kucinich's office reported CSX's unilateral withdrawal from settlement negotiations to the STB. Congressman Kucinich was informed that because an interim decision was made, the STB would be precluded from any *ex parte* discussions about an applicant's lack of cooperation with earlier decisions and commitments. Therefore, a formal filing would be necessary.

III. REQUEST FOR STB ACTION

The STB, in issuing its oral decision, did not signal an end to on-going settlement

negotiations among the railroads and affected parties. On the contrary, the STB, in correspondence with Congressman Kucinich's office, denied that there are any deadlines to negotiated settlements among railroads and communities. (See Attachment 2, supra.) CSX Corporation made a commitment to negotiate in good faith with the City of Brooklyn after the STB responded to intervention from Congressman Kucinich's office.

However, good faith negotiations must be backed up by good faith. In this case, CSX exploited the opportunity of the STB's oral decision to back out of negotiations. At no time during negotiations did CSX indicate to Brooklyn or to Congressman Kucinich that it intended to end discussions once the STB issued its oral decision.

Congressman Kucinich respectfully requests that the STB honor its commitment to negotiated settlements in the Conrail merger case, as ordered in Decision No. 71 and Decision No. 73, and in its representations regarding deadlines made to his Congressional Office. (See Decision No. 71, Decision No. 73, and Attachment 2, supra). Congressman Kucinich further requests that in honoring its commitments in deciding the Conrail merger, that it order CSX to continue to negotiate in good faith with Brooklyn, either directly or in conjunction with Congressman Kucinich, a Party of Record to the Conrail merger case, to settle their differences on environmental mitigation for that community.

ATTACHMENT 1**Gelfand, Marty**

From: Gelfand, Marty
Sent: Wednesday, March 18, 1998 1:03 PM
To: 'Nancy Beiter'
Subject: RE: FD 33388, Decision No. 71

I just received Decision No. 71. It's pretty self-explanatory, but I did want some clarification on the April 15, 1998, deadline mentioned in the second paragraph.

Intuitively, that deadline makes sense from the perspective of the SEA's planning needs. If an agreement is not reached, SEA needs to know so that it could hire enough staff and consultants to make recommendations to the STB to impose conditions, if necessary.

However, from the perspective of the affected parties, what, if anything, does this deadline mean? How long can the parties negotiate an independent settlement? Until the oral decision in June? Until the written decision in July? Or some other date?

Thank you in advance for your clarification.

Martin D. Gelfand
Staff Attorney
District Office of Congressman Dennis J. Kucinich
Lakewood, Ohio
marty.gelfand@mail.house.gov

ATTACHMENT 2

Gelfand, Marty

From: Nancy Beiter[SMTP:BeiterN@stb.dot.gov]
Sent: Wednesday, March 18, 1998 5:27 PM
To: Gelfand, Marty
Subject: RE: FD 33388, Decision No. 71

We love negotiated settlements here. We know we function in a quasi-judicial capacity and, like judges, our decisions are often unpopular with everyone. Negotiated settlements are much better because the parties live far more happily with the results. My point is that there is no deadline on a negotiated settlement. Until everyone is happy, my suspicion is that these issues will always be in litigation.

For example, in the UP/SP merger the cities of Reno and Wichita had environmental issues similar to those facing the Cleveland area now. All during the environmental review process the cities were negotiating with the carrier and they continued to do so while the various appeals from our decision went through the court of appeals. The court sent the environmental review back to us for further clarification. Still the parties have continued to negotiate.

In short, it ain't over 'til the fat lady sings and we don't know when that is.

The answer to your earlier question is that the ICC and STB decisions that are not in print and not on our WEB site are available on legal research services such as Lexis and Westlaw. Generally only lawyers have access to such services but there is not a large public demand for our decisions in most cases. Interest is usually limited to the parties and the legal community. The decisions are also available for individual purchase from our contractor, DC News and Data, Inc. at 202 289-4357.

Does that help?

John M. Coyne
Mayor

CITY OF

**BROOKLYN
OHIO**

COUNCIL:

John E. Frey
Paula A. Ritter
Kenneth P. Loeri
Thomas E. Coyne
Gregory L. Frey
Rita M. Brown
Regis Barrett

7619 Memphis Avenue, Brooklyn, Ohio 44144-2197 • (216) 351-2133

"Home of the Seatbelt Law"

ATTACHMENT 3

March 25, 1998

Stephen Watson
Regional Vice President
CSX
143 W. Market Street, #700
Indianapolis, IN 46204

Dear Mr. Watson:

It is my understanding that increased freight rail traffic will occur in the City of Brooklyn if the proposed acquisition of Conrail by CSX and Norfolk Southern is approved by the U. S. Surface Transportation Board.

I am strongly opposed to any rail merger which will increase the frequency of freight train traffic through residential areas and fails to take into consideration the safety and environmental ramifications of their actions, specifically, noise, air and traffic pollution, decrease in property values, potential delays in safety forces' emergency response times, and hazardous material incident training and equipment.

Brooklyn may be a small community but nonetheless deserves equal consideration in terms of safety and environmental mitigation measures. It has been reported that one section of the Conrail line to be acquired by CSX, which runs parallel to I-480 and adjacent to homes in Brooklyn's Idlewood neighborhood, will see an increase in train traffic from 7 to 44 trains daily! Residents are concerned for their safety, quality of living and property values!

Stephen Watson**Page Two****March 25, 1998**

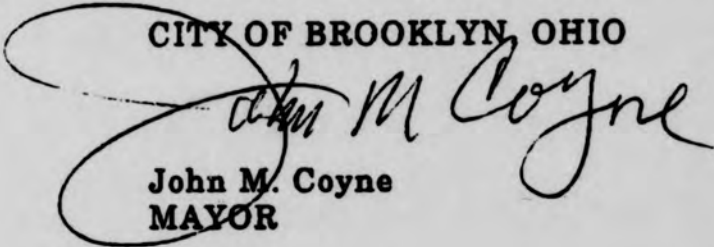
What I find particularly disturbing is that to date no representative of CSX has contacted me to address these concerns and negotiate a mitigation agreement. I understand that the Surface Transportation Board's Section of Environmental Analysis (SEA) in its Draft Environmental Impact Statement requires the railroad proponents of the merger to negotiate a mutually agreeable mitigation settlement with the affected communities, and further, requires the parties to reach a mutually acceptable agreement by April 15, 1998 or live with the SEA's recommendation in its Final Environmental Impact Statement.

Be assured that I stand ready to make myself and our city's legal department available to CSX representatives to discuss these concerns and work out a resolution which will benefit Brooklyn's affected citizens.

You may contact me at 216/351-2133 (telephone) or 216/351-7601 (fax) to schedule an appointment. I look forward to hearing from you soon!

Sincerely,

CITY OF BROOKLYN, OHIO



John M. Coyne
MAYOR

cc: Thomas F. O'Malley, Director of Law
Congressman Dennis Kucinich, Ohio CD10
Elaine Kaiser, U. S. Surface Transportation Board
George Voinovich, Governor, State of Ohio
Tom O'Leary, Ohio Rail Authority
Paul Alsenas, Exec. Director, Cuyahoga Co. Planning Commission



Stephen L. Watson
Regional Vice President - State Relations

04 06 98

700 Harrison Building
143 West Market Street
Indianapolis, IN 46204
(317) 267-3003
FAX (317) 267-3005

ATTACHMENT 4

April 3, 1998

Hon. John M. Coyne, Mayor
City of Brooklyn
7619 Memphis Avenue
Brooklyn, Ohio 44144-2197

Dear Mayor Coyne:

We have received your letter of March 25, 1998 concerning the CSX/NS acquisition of Conrail.

As you correctly note, the Surface Transportation Board's Section of Environmental Analysis (SEA) in its Draft Environmental Impact Statement (DEIS) requires CSX and NS to consult with and attempt to negotiate mutually acceptable mitigation settlements with "affected communities." However, the City of Brooklyn was not identified in the DEIS as an "affected community", nor was it so identified in the STB's Decision No. 71, issued March 17, 1998, which set the April 15, 1998 deadline you cite in your letter.

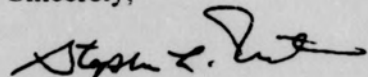
The portion of the Conrail Short Line passing through Brooklyn is expected to experience an increase in train traffic from the current average of 20 Conrail trains per day to approximately 44 trains per day on average. The increase from "7 to 44" you cite in your letter is incorrect for the portion of the line passing through Brooklyn. Also, the Brooklyn portion of the line has no at-grade rail-highway crossings, and is entirely grade separated, so there will be no delays in safety forces' response times. Additionally, the DEIS identified for noise mitigation those areas where the projected train noise exceeded certain noise thresholds established by SEA. Brooklyn had no areas exceeding the thresholds, and therefore requires no noise mitigation. Finally, the SEA has recommended to the STB that CSX and NS develop and implement a comprehensive hazardous materials safety and training program for the communities on our railroads that will experience an increase in hazardous materials traffic, and we have agreed to fully comply with that recommendation. Your public safety forces will be contacted and invited to participate in this program after the acquisition is approved by the STB.

The portion of the current CSX line from Lester, which passes through Brooklyn, is not expected to experience any increase in train traffic as a result of the acquisition. The train traffic on that line is only 5.8 trains per day on average.

Mayor J. Coyne 4/3/98
page 2

I trust that this addresses the issues raised in your letter of March 25, and explains why we have not contacted your community concerning the CSX/NS acquisition of Conrail.

Sincerely,



Stephen L. Watson

cc: Congressman Dennis Kucinich
Ms. Elaine Kaiser, SEA
Mr. Thomas O'Leary, ORDC
Mr. Paul Alsenas, Cuyahoga Planning Comm.
Mr. Thomas F. O'Malley, Brooklyn Law Dir.

DENNIS J. KUCINICH

10TH DISTRICT, OHIO

1730 LONGWORTH OFFICE BUILDING
WASHINGTON, D.C. 20515
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1400 DETROIT AVENUE
LAKEWOOD, OHIO 44107
(216) 228-8850



Congress of the United States
House of Representatives

Committee:
Government Oversight
Education
and the
Workforce

ATTACHMENT 5

April 8, 1998

Ms. Linda J. Morgan
Chairman
Surface Transportation Board
1925 K St. NW #820
Washington, D.C. 20423

Re: Finance Control Docket No. 33388

Dear Ms. Morgan:

On April 3, 1998, Stephen L. Watson, Regional Vice President for State Relations for CSX Corporation, wrote to Brooklyn, Ohio, Mayor John M. Coyne, stating his refusal to discuss environmental mitigation for Brooklyn. Mr. Watson acknowledged that Brooklyn would experience an increase from 20 to 44 trains per day as a result of CSX's acquisition of the Conrail Short Line. However, Mr. Watson cited the Draft Environmental Impact Statement and Decision No. 71 as justification for excluding Brooklyn from environmental mitigation discussions.

On February 4, 1998, this office filed an addendum to our comments on the DEIS that asked the STB to analyze the environmental effects the proposed Conrail merger would have on Brooklyn. Even though Brooklyn was not mentioned in the DEIS, the STB is aware of the environmental problems that the proposed merger will cause in Brooklyn and is working on a mitigation plan to be included in the Final Environmental Impact Statement.

On March 23, 1998, the Surface Transportation Board issued Decision No. 73. That decision interprets Decision No. 71 as follows:

Decision No. 71 was intended to facilitate negotiations among the various interested parties. It was not intended to define who should, or should not, be involved in any specific negotiation, and it was certainly not intended to limit the participation of any appropriate party in any negotiations that may be conducted. Any party that has a legitimate interest in these matters is free and indeed encouraged to participate in negotiations.

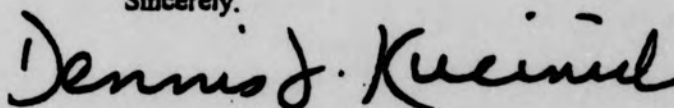
Page 2

The STB ordered Decisions 71 and 73 to encourage inclusion of affected communities in environmental mitigation discussions. CSX Corporation and Mr. Watson have misunderstood Decision No. 71 and applied it in a way that purposely excludes the City of Brooklyn from environmental mitigation discussions.

The STB has ordered CSX and Norfolk Southern railroads to engage in environmental mitigation discussions with the affected communities. The STB has further ordered that if the railroads and affected communities fail to settle their differences by April 15, 1998, then the STB's Section on Environmental Analysis will develop its own environmental mitigation for each of the communities in the Greater Cleveland area.

As Congressman from Ohio's 10th Congressional District, I demand that the STB take action to assure representation for the people of Brooklyn, Ohio, in environmental mitigation discussions with CSX Corporation. I am demanding that the STB order CSX to meet with the Mayor and the people of Brooklyn for discussions about how the merger will affect Brooklyn and to order good faith settlement discussions as ordered by Decision No. 71.

Sincerely,



Dennis J. Kucinich
Member of Congress

DJK:mg

enclosures: Addendum to Comments on the Draft Environmental Impact Statement
Letter from Stephen Watson to Brooklyn Mayor John M. Coyne



ATTACHMENT 6

One James Center
Richmond, Virginia 23219
(804) 782-1444

Michael J. Rushling
Vice President
State Relations

June 30, 1998

The Honorable John M. Coyne
Mayor, City of Brooklyn, Ohio
7619 Memphis Avenue
Brooklyn, Ohio 44144

Dear Mayor Coyne:

As the individual at CSX responsible for coordinating state and local government agreements related to the Conrail transaction, I am responding to your June 17, 1998 letter to Stephen L. Watson.

The Surface Transportation Board voted on June 8, 1998 to approve the CSX/Norfolk Southern acquisition of Conrail. Numerous conditions were imposed in the STB's oral decision addressing various competitive and environmental impacts the agency determined would result from the transaction.

Prior to the June 8 vote, we engaged in extensive consultations with state and local government officials in those areas identified by the STB as potentially experiencing adverse impacts on lines that CSX would acquire as a result of the Conrail transaction. Our efforts focused on negotiating voluntary agreements, when and where possible, with these states and communities to resolve the concerns raised by the STB and preclude the need for imposed conditions.

We were successful in reaching numerous negotiated agreements prior to the June 8 STB voting conference. The STB accepted these agreements as alternatives to mandated conditions and at the June 8 Voting Conference advised that the negotiated agreements would be imposed as conditions.

In those cases where CSX was unable to reach negotiated settlements prior to the Voting Conference, the STB imposed conditions requiring a variety of mitigation measures. These conditions were summarized in the STB's oral decision and included recommendations for certain locations in the Greater Cleveland area. The conditions range from enhanced train defect detection to hazardous materials emergency response coordination and training to noise mitigation. Some of these conditions may be applicable in the case of your community.

Mayor Coyne
June 30, 1998
Page Two

We are now awaiting the STB's issuance of its written decision in the case in order to finalize plans to move forward with implementation of the mitigation measures that are imposed as conditions. You can be assured that we intend to comply fully with the terms of any and all conditions imposed by the STB that may involve the City of Brooklyn. As soon as our plans are complete, we will be in contact with you. In the meantime, if you have any questions, please let me know.

Sincerely,

Michael J. Ruchling

trt

cc: Elaine K. Kaiser, Esquire, Surface Transportation Board
The Honorable Linda Morgan, Chairman, Surface Transportation Board
Mr. Stephen L. Watson, CSX Transportation

STB

FD-33388

5-13-98

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ID-VIDEO

Surface Transportation Board
MEMORANDUM

To:

The file

From:

Edward C. Fernandez

Date:

5/13/98

Subject

FD-33388

On 1/13/98 a "IMPACT ON CLEVELAND" was filed in the above case. There was also a videocassette filed with this document. Anyone wishing to view the video should contact me at 565-1655 to schedule a viewing time and place. This document was assigned a control number of 182900.

STB

FD

33388

3-17-98

E

186479

LAW OFFICES

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888 SEVENTEENTH STREET, N.W.

WASHINGTON, D.C. 20006-3939

TELEPHONE: (202) 298-8660

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(202) 342-1316

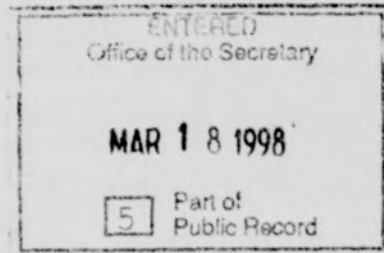
RICHARD A. ALLEN



March 17, 1998

Via Hand Delivery

Vernon A. Williams
Secretary
Surface Transportation Board
1925 K Street, N.W.
Washington, D.C. 20423-0001



Re: 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, Finance Docket No. 33388

Dear Secretary Williams:

Enclosed is an original and twenty-five (25) copies of NS-64, Errata to Brief of Applicants Norfolk Southern Corporation and Norfolk Southern Railway Company in the above-entitled matter. Also enclosed is a 3-1/2" computer disk containing the pleading in WordPerfect 5.1 format, which is capable of being read by WordPerfect 7.0.

Should you have any questions regarding this, please call.

Sincerely,

Richard A. Allen

Counsel for Norfolk Southern Corporation
and Norfolk Southern Railway Company

Enclosures

cc: The Honorable Jacob Leventhal
All Parties of Record

186479

BEFORE THE
SURFACE TRANSPORTATION BOARD

Finance Docket No. 33388

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



ERRATA TO BRIEF OF APPLICANTS NORFOLK SOUTHERN CORPORATION
AND NORFOLK SOUTHERN RAILWAY COMPANY

Norfolk Southern Corporation and Norfolk Southern Railway Company submit the following errata to the brief, NS-62, filed on February 23, 1998:

1. On Page 10, Line 8, the word "relate" should be inserted after "transportation."
2. On Page 33, Line 1, the word "new" should be changed to "no."

Respectfully submitted,

Richard A. Allen
Zuckert, Scoutt & Rasenberger, LLP
888 Seventeenth Street, N.W.
Suite 600
Washington, DC 20006-3939
(202) 298-8660

Counsel for Norfolk Southern Corporation
and Norfolk Southern Railway Company

Dated: March 17, 1998

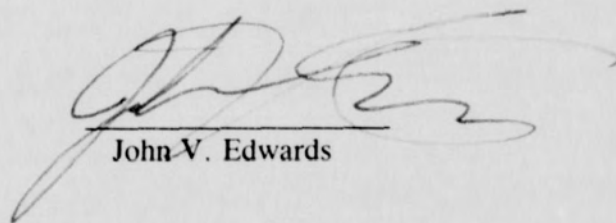


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CERTIFICATE OF SERVICE

I, John V. Edwards, hereby certify that on this 17th day of March, 1998, I have caused to be served a true and correct copy of the foregoing NS-64, Errata to Brief of Applicants Norfolk Southern Corporation and Norfolk Southern Railway by first class mail, postage prepaid, or by more expeditious means, on all parties of record, and by hand delivery on:

The Honorable Jacob Leventhal
Administrative Law Judge
Federal Energy Regulatory Commission
Office of Hearings
825 North Capitol Street, N.W.
Washington, D.C. 20426



John V. Edwards

Dated: March 17, 1998

STB

FD

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3-10-98

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186336
BEFORE THE
SURFACE TRANSPORTATION BOARD

Finance Docket No. 33388

CSX CORPORATION AND CSX TRANSPORTATION, INC.,
NORFOLK SOUTHERN CORPORATION AND
NORFOLK SOUTHERN RAILWAY COMPANY



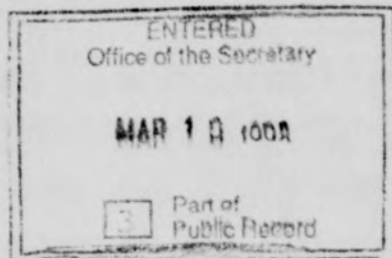
— CONTROL AND OPERATING LEASES/AGREEMENTS —
CONRAIL INC. AND CONSOLIDATED RAIL CORPORATION

ERRATA TO

BRIEF

submitted on behalf of

INSTITUTE OF SCRAP RECYCLING INDUSTRIES, INC.



John K. Maser III
Jeffrey O. Moreno
DONELAN, CLEARY, WOOD & MASER, P.C.
1100 New York Avenue, N.W.
Suite 750
Washington, D.C. 20005-3934
(202) 371-9500

*Attorneys for Institute of Scrap Recycling
Industries, Inc.*

March 10, 1998

BEFORE THE
SURFACE TRANSPORTATION BOARD

Finance Docket No. 33388



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

ERRATA TO

BRIEF

submitted on behalf of

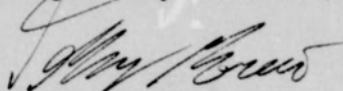
INSTITUTE OF SCRAP RECYCLING INDUSTRIES, INC.

The Institute of Scrap Recycling Industries, Inc. ("ISRI") hereby submits this Errata to the "Brief submitted on behalf of Institute of Scrap Recycling Industries, Inc." (ISRI-11), filed on January 23, 1998 in the above-captioned proceeding. ISRI submits the following errata:

- (1) On page 2 of the Brief, Line 6, strike "membership" and replace with "Board of Directors".
- (2) On page 8 of the Brief, Line 20, strike "a" and replace with "to two".

(3) On page 8 of the Brief, Line 21, strike "haul" and replace with "hauls".

Respectfully submitted,



John K. Maser III

Jeffrey O. Moreno

DONELAN, CLEARY, WOOD & MASER, P.C.

1100 New York Avenue, N.W.

Suite 750

Washington, D.C. 20005-3934

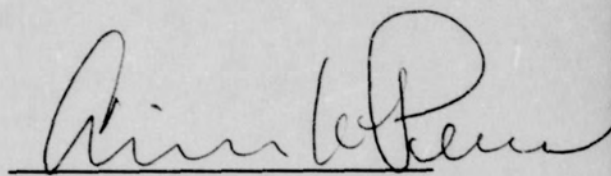
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*Attorneys for Institute of Scrap Recycling
Industries, Inc.*

March 10, 1998

CERTIFICATE OF SERVICE

I hereby certify that a copy of the foregoing ERRATA TO THE BRIEF OF INSTITUTE OF SCRAP RECYCLING INDUSTRIES, INC. has been served by first class mail, postage prepaid, on all parties of record in this proceeding this 10th day of March, 1998.

A handwritten signature in cursive script, appearing to read "Aimee L. DePew", is written over a horizontal line.

Aimee L. DePew

STB

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UNITED STATES DISTRICT COURT
DISTRICT OF NEW JERSEY

CHAMBERS OF
MARY LITTLE PARELL
JUDGE

U.S. COURTHOUSE
402 E. STATE STREET
TRENTON, NJ 08608
(609) 989-2105

February 27, 1998

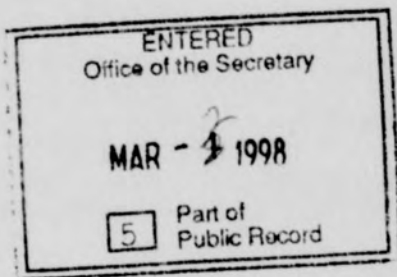
Vernon A. Williams, Secretary
Surface Transportation Board
1925 K. Street, N.W.
Washington, D.C. 20423



Dear Mr. Williams:

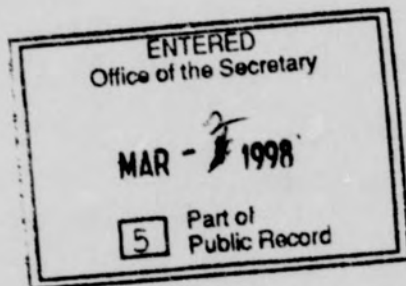
Enclosed please find material from Rutgers Environmental Law Clinic. This material was mis-delivered to Judge Parell's chambers and at the direction of Mr. Lloyd (the sender) we are forwarding this package to your office.

Very truly yours,



Marleen Ann Young
Marleen Ann Young
Secretary to:
MARY LITTLE PARELL
United States District Judge

186085



E

Before the
SURFACE TRANSPORTATION BOARD
Washington, D.C.

Finance Docket No. 33388

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

CERTIFICATE OF SERVICE

I hereby certify that by February 27, 1998 a copy of the foregoing document will be served by first-class mail upon Administrative Law Judge Leventhal and upon all parties of record, as listed on the official service list issued by the Board on August 19, 1997 in Decision No. 21, as well as parties added at a later date.

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February 21, 1998

Vernon A. Williams, Secretary (Via Federal Express)
Surface Transportation Board
1925 K Street, NW
Washington, D.C. 20423

RE: FINANCE DOCKET NO. 33388

Dear Mr. Williams:

This final brief is submitted on behalf of the Tri-State Transportation Campaign (Tri-State) to reaffirm and support its request for conditions that NS and CSX should adopt before STB approves the Conrail Acquisition. Tri-State is a consortium of thirteen environmental, transportation and planning groups working together to create an economically and environmentally sound transportation system for the New York metropolitan area. Improving the region's rail freight system, and thereby reducing truck miles of travel within the region, is an important component of Tri-State's vision for an effective transport system.

Tri-State submitted five conditions to the STB on October 20, 1997 aimed at restoring competitive rail freight service to the East-of-Hudson sector. Based on its review of the supplemental operating plan for the North Jersey Shared Assets Area, Tri-State submitted four additional conditions on November 22, 1987 designed to maintain and expand rail freight, and in particular carload freight, operations in New Jersey, without inhibiting growth in passenger rail services. Tri-State defended these nine conditions in its rebuttal submitted on January 16, 1998. Additional information about the conditions was provided in Tri-State's comments on STB's Draft EIS for the Acquisition submitted on January 12, 1998.

Tri-State's conditions would result in significant reductions in truck traffic across the Harbor and on both sides of the Hudson. The first group would correct a serious shortcoming in the current acquisition plan, namely the preservation of a single carrier monopoly rail service for the 12.5 million residents of the Tri-State Region who live East of the Hudson River, a population larger than the states of Ohio or Pennsylvania. CSX and NS, meeting behind closed doors to shape their acquisition plan, chose to assign all Conrail assets in the East of Hudson sector to a single carrier: CSX. The applicants chose not to assign all Conrail assets in Ohio or Pennsylvania to a single carrier knowing that STB was unlikely to approve such a plan. By the same reasoning, STB must withhold its approval of the current plan until competitive East-of-

Hudson rail access is assured through either the Tri-State conditions or similar conditions suggested in the petition of Congressman Nadler et al. and subsequently endorsed by the Governor of New York and the Mayor of New York City. Leaving East-of-Hudson businesses and residents with the limited single carrier monopoly rail service, described by CSX in its operating plan, will preserve the severe negative impacts brought on by the near total dependence on trucks for freight service in this sector.

The nine conditions submitted by Tri-State are reaffirmed and summarized below:

1. Improved Cross-Harbor Car Float Operation

The key to gaining competitive rail access to the East-of-Hudson sector is to restore a high quality Cross-Harbor car float service on the Greenville-Bay Ridge route. The central argument made by NS and CSX in favor of their acquisition of Conrail is that the plan will revive the competitive balance that once existed in the Eastern part of the U.S. prior to the disastrous merger of the Pennsylvania and New York Central Railroads in 1968. NS would inherit Pennsylvania routes to the west and south while CSX would absorb the New York Central's water level route. But neglected in this plan is the cross-harbor car float, which was an important access route for the Pennsylvania Railroad to New York City and Southern New England. After the merger, Penn Central, later absorbed by Conrail, routed all freight crossing the Hudson on a circuitous route via Selkirk Yard near Albany, NY. The result was a dramatic decline in rail freight activity in the East-of-Hudson sector, shrinking market share to less than 3%.

Tri-State proposes that a high volume car float operation across New York Harbor be required by STB as a condition for the acquisition. This would restore two-carrier service by extending NS to New York City on the car float route to balance CSX's access along the Hudson from the north. The Nadler petition proposes to accomplish a similar result by extending the Conrail North Jersey Shared Assets operation across the Harbor.

Public agencies now recognize the importance of cross-harbor freight alternatives to truck traffic on the region's congested highway crossings. New York City's Intermodal Rail Freight Study completed by Mercer Management in 1996 identified a large market potential for rail freight, some 6 million tons annually, that would use a restored and upgraded car float service. With this volume, costs would be competitive for freight movements that now must face the circuitous land routing via Albany. The NYC Economic Development Corporation plans to invest its resources to restore the once busy car float bridges in Bay Ridge which lead directly to the 65th SYard. New Jersey Dept. of Transportation has invested \$300,000 of state transportation trust funds to repair the Greenville float bridges. Both states, acting through the Port Authority of NY and NJ, have underwritten the capital and operating cost of a demonstration of cross-harbor container-on-barge operations using Federal transportation funds.

The PANYNJ has a long tradition of using excess bridge and tunnel revenues to subsidize rail transit and commuter bus facilities. A well defined plan for similar public funding to help restore the Greenville-Bay Ridge rail car float operation as part of a competitive rail access plan for the East-of-Hudson sector can expect to receive broad public endorsement. STB must lay the groundwork for this plan by including Tri-State's conditions in the acquisition plan.

A key element of these conditions is for NS to lease the city-owned intermodal terminal developed, but unused, at 65th St. Yard. NS could operate double stack intermodal cars to this location with modest modification to the float bridges. NS access to 65th St. Yard would permit NS to establish an interchange point with New York and Atlantic Railway, giving this short line carrier direct access to both major systems.

2. NS trackage rights to Oak Point Yard and Hunts Point Market

A related condition requested by Tri-State would extend NS trackage rights from 65th St. Yard to Oak Point Yard in the Bronx and to the Hunts Point produce market. Access to this market, the nation's busiest, is almost entirely by truck, although rail trackage is in place. Two-carrier rail competition can increase the potential for rail freight service to this market. NS cross-harbor access opens the way for that carrier to reach other new customers in the Bronx. The segment of this route from 65th St. Yard to Fremont is owned by the Metropolitan Transportation Authority and operated by the NY and Atlantic Railway. Allowing NS overhead trackage rights on this segment could benefit both carriers. The alternative plan advanced by Congressman Nadler, and endorsed by the Governor and the Mayor, calls for the extension of Conrail's North Jersey Shared Assets operation across this route.

3. NS trackage rights on the Northeast Corridor to New Haven, CT

NS should share Conrail trackage rights now proposed to go solely to CSX on the Metro-North New Haven Line from New Rochelle Jct. to New Haven, CT and on the Amtrak segment from Oak Point Yard to New Rochelle Jct. This is a logical extension of the Tri-State proposed condition requesting NS service from the Greenville-Bay Ridge car float to Oak Point. Connecticut is poorly served by existing Conrail service and the CSX operating plan shows no increase in service on the New Haven line. NS could develop an important direct route to New England, connecting with short lines in New Haven that reach Hartford, Springfield, Providence and Boston. This would be a less circuitous alternative to its currently planned route through Harrisburg and Albany.

4. NS trackage rights through Pennsylvania Railroad Tunnels

The Pennsylvania Railroad tunnels and associated trackage from Harrison, NJ to Oak Point Yard in the Bronx are currently used exclusively for rail passenger service. Tri-State

requests that any residual Conrail trackage rights for freight service on this line be transferred to NS as part of this acquisition. NS will then be in a position to negotiate with Amtrak to operate road railer-type service and other low profile equipment along the busy I-95 Washington-Boston corridor. Clearly passenger service must be given priority, but for many hours late at night ample capacity is available. Technical details and safety criteria can be part of this negotiation. As mentioned elsewhere in this list of conditions, the speedy resolution of disputes between freight and passenger carriers is important, and the STB should develop arbitration procedures to resolve these disputes.

5. Operation of CSX intermodal trains into Harlem River Yard

At considerable public expense, New York City and State agencies have improved clearances to permit operation of conventional piggyback operation from Selkirk Yard near Albany to Harlem River Yard in the Bronx. Tri-State proposes as a condition to the acquisition that CSX operate regular piggyback service to this terminal.

6. Enhancements at Oak Island Yard

Oak Island Yard in Newark, NJ is the region's sole remaining hump classification yard. Nearly abandoned by Conrail, the yard is back in operation, and CSX and NS plan to increase its throughput. A hump yard greatly enhances the railroads' ability to handle carload freight in the region. Tri-State proposes that the carriers develop a comprehensive plan of specific capital improvements for enhancing this yard's performance, comparable to other NS and CSX yard expansion plans described in the application. An important element of such a plan is the preservation of adjacent vacant tracts of land for future expansion of the yard.

7. Emphasis on carload freight

Delivering carload freight directly to customers located along rail lines is clearly in the public interest, reducing truck travel and using rail lines more efficiently. It is important that existing carload activity be retained and new carload business be solicited. Shifting carload freight to intermodal will create more truck traffic in the most congested parts of the Tri-State Region.

Many of the service improvements cited by NS and CSX as benefits of the acquisition, such as single line service and higher volumes on traffic lanes, could provide new opportunities for increasing carload freight. The restoration of hump service at Oak Island Yard and related improvements can improve the reliability and service levels for carload deliveries. Upgrading the Greenville-Bay Ridge car float operation also enhances carload freight service potential. Yet 80% of the traffic growth NS and CSX expect to gain from the acquisition is intermodal. This diversion of existing truck traffic to intermodal, though important, will have a relatively modest

Vernon Williams
February 21, 1998
Page 5 of 5

benefit in the metropolitan area.

Tri-State proposes that STB require the applicants to conduct an assessment of carload freight potential in the North Jersey Shared Assets Area comparable to the New York Downstate Rail Freight Study carried out by Mercer Management, Inc in 1995. That study indicated that as much as 23 million tons per year of untapped rail freight potential, to a large extent carload freight, exists in the East of Hudson sector. Judging from the results of the New York study, the proposed North Jersey study may identify a substantial potential for carload freight in the North Jersey area.

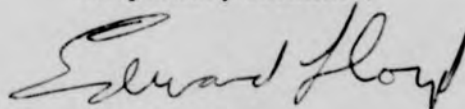
8. Retaining North Jersey rail freight activity in the shared assets area

The NS and CSX plan calls for Conrail to continue to operate the rail freight system in the North Jersey area. Costs would be allocated between the two carriers. Tri-State calls for STB to closely monitor these costs to assure that levels do not rise to the point where NS and CSX would seek to relocate businesses to more remote locations, outside the shared asset area. This dispersion of activities would lead to increased truck miles of travel in the region and would be at odds with the New Jersey State Plan for Development and Redevelopment, which calls for focusing economic activity in existing centers.

9. Speedy arbitration of disputes involving conflicts between freight and passenger service

In the past, proposals for new or increased levels of commuter rail or Amtrak inter-city service have often been stalled by unrealistic demands by the freight carriers. Similarly, commuter rail agencies and Amtrak have often been reluctant to accommodate the needs of rail freight carriers on their trackage. Rail freight and passenger service can generally function efficiently on shared trackage, however, and should be induced to do so. Tri-State requests that STB establish a formal arbitration procedure that permits speedy resolution of disputes between passenger and freight carriers and that encourages the growth of both.

Respectfully submitted,

A handwritten signature in dark ink, appearing to read "Edward Lloyd", is written over a horizontal line.

Edward Lloyd
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Tri-State Transportation Campaign

cc. Parties of Record

STB

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February 25, 1998

VIA HAND DELIVERY

Honorable Vernon A. Williams
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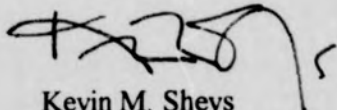
**Re: Finance Docket No. 33398, CSX Corporation and CSX Transportation, Inc.,
Norfolk Southern Corporation and Norfolk Southern Railway Company --
Control and Operating Leases/Agreements -- Conrail Inc. and Consolidated
Rail Corporation -- Transfer of Railroad Line by Norfolk Southern Railway
Company to CSX Transportation, Inc.**

Dear Secretary Williams:

Enclosed you will find the original and 25 copies of the Brief of Northern Virginia Transportation Commission and Potomac and Rappahannock Transportation Commission (VRE-12), Redacted Version. Also enclosed is a 3.5 inch diskette containing the filing in WordPerfect 5.1.

Please stamp the extra copy of the foregoing and return it with our messenger.

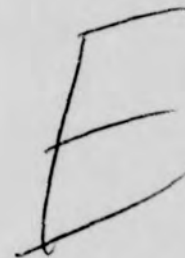
Respectfully submitted,



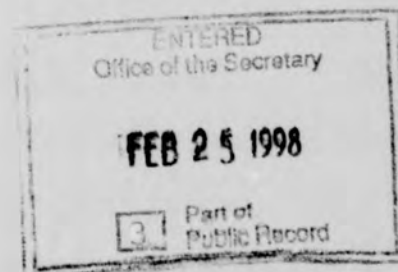
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Enclosures

cc: All Parties Referenced in Certificate of Service



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Redacted Version
VRE-12

186009

BEFORE THE
SURFACE TRANSPORTATION BOARD



Finance Docket No. 33388

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

FINANCE DOCKET NO. 33388 (Sub-No. 37)

NORTHERN VIRGINIA TRANSPORTATION COMMISSION AND POTOMAC
AND RAPPAHANNOCK TRANSPORTATION COMMISSION
-- OPERATING RIGHTS --
LINES OF CSX TRANSPORTATION, INC., NORFOLK SOUTHERN
RAILWAY COMPANY AND CONSOLIDATED RAIL CORPORATION

**BRIEF OF
NORTHERN VIRGINIA TRANSPORTATION COMMISSION
AND
POTOMAC AND RAPPAHANNOCK
TRANSPORTATION COMMISSION**

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Dated: February 23, 1998

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BEFORE THE
SURFACE TRANSPORTATION BOARD

Finance Docket No. 33388

CSX CORPORATION AND CSX TRANSPORTATION, INC., NORFOLK SOUTHERN
CORPORATION AND NORFOLK SOUTHERN RAILWAY COMPANY
-- CONTROL AND OPERATING LEASES/AGREEMENTS --
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NORTHERN VIRGINIA TRANSPORTATION COMMISSION AND POTOMAC
AND RAPPAHANNOCK TRANSPORTATION COMMISSION
-- OPERATING RIGHTS --
LINES OF CSX TRANSPORTATION, INC., NORFOLK SOUTHERN
RAILWAY COMPANY AND CONSOLIDATED RAIL CORPORATION

BRIEF OF
NORTHERN VIRGINIA TRANSPORTATION COMMISSION
AND
POTOMAC AND RAPPAHANNOCK
TRANSPORTATION COMMISSION

I. INTRODUCTION

The acquisition control of Conrail, the division of its assets by CSX and NS, and the changes in operations of NS and CSX arising from the acquisition control and division of assets together constitute the largest and most significant rail consolidation in the history of the United States. The transactions contemplated by the Conrail takeover pose a serious threat to the important commuter rail operations of Virginia Railway Express ("VRE"). The Conrail takeover will substantially increase freight traffic on the Conrail, NS and CSX lines over which VRE

operates.¹ A significant portion of the increased freight traffic will traverse these lines during the morning and evening commuter rush hours in which VRE on-time performance is critical to the viability of this commuter service.

All of VRE's trains traverse the rail line between Alexandria and Virginia Avenue. Of all the rail lines in the combined CSX/Conrail system or the combined NS/Conrail system that are projected to have substantial post-transaction increases in freight traffic, the Alexandria - Virginia Avenue segment has by far the greatest volume of passenger operations. The adverse impact of the Conrail takeover on passenger rail operations (both Amtrak and VRE) is thus nowhere more clearly evident than on this segment.

Although this fact is obvious from even the most cursory review of the Applicants' Operating Plans, the Applicants have not recognized this adverse impact and have done nothing to ameliorate or otherwise address it. Instead, they simply assert that line capacity is adequate and that they will avoid interference with VRE operations through "correct scheduling" of their substantially increased freight operations, with no explanation as to how this will be achieved. This is an inadequate response to the threat to VRE, particularly in light of the history of freight-related delays and interference with VRE operations as documented in VRE's Comments. Indeed, Applicants' sole quantitative effort to refute VRE's detailed and comprehensive

¹ VRE operates over (i) Conrail's line of railroad between RO Interlocking in Arlington, Virginia and Virginia Avenue Interlocking, (ii) CSX's line of railroad between the connection with the Conrail line at RO Interlocking and XR Interlocking in Spotsylvania, Virginia and (iii) NS's line of railroad between the South Manassas turnout and NS's connection with CSX at CSX's AF Interlocking in Alexandria, Virginia. References in the brief to the "Fredericksburg Line" refer to VRE service between Fredericksburg and Union Station on the Conrail and CSX segments; references to the "Manassas Line" refer to VRE service between Broad Run station (south of Manassas) and Union Station.

quantitative analysis of past and projected freight-related delays to VRE service is a distorted string line analysis that isolates only a short, triple-tracked portion of the CSX line.

In order to approve a railroad consolidation, the Board must find that it is in the public interest. The Board is charged by statute to consider the public interest as a whole and, among other things, to consider "the effect of the proposed transaction on the adequacy of transportation to the public." 49 U.S.C. § 11324(b)(1). The Board's authority to impose conditions on approved rail consolidations is broad. In this case, what the Board should do is quite clear. The Conrail takeover offers significant potential benefits to the public generally and therefore should be approved; however, to ameliorate the adverse impact of the transaction specifically on VRE operations, the Board should grant the modest conditions sought by VRE. Approval of the Conrail takeover in its proposed, unconditioned form would not be in the public interest.

In order to protect VRE operations from the adverse effects of the proposed Conrail takeover, the Commissions² have requested imposition of a condition pursuant to which VRE would have operating rights over the lines on which it currently operates, subject to terms and conditions to be negotiated by the parties, or failing a negotiated agreement, set by the Board. In order to ensure that VRE's conditions are narrowly tailored to ameliorate the harms posed by the Conrail takeover without reaching beyond those harms and without undermining the public benefits of the transaction, the Commissions have framed their requested conditions in the form of adjustments to the existing contracts pursuant to which they operate over the relevant Conrail, CSX and NS lines.

² Northern Virginia Transportation Commission and Potomac and Rappahannock Transportation Commission are referred to herein as the "Commissions."

The conditions requested by the Commissions are necessary to avoid the adverse impact of the Conrail takeover on VRE operations. The proposed conditions are operationally feasible and would ameliorate the demonstrated adverse impact without reducing the benefits of the proposed Conrail takeover.

II. FACTUAL BACKGROUND

A. VRE History, Operating Statistics, Public Investment And Benefits

1. VRE's History

The Northern Virginia Transportation Commission ("NVTC") and the Potomac and Rappahannock Transportation Commission ("PRTC") are political subdivisions of the Commonwealth of Virginia organized pursuant to the Transportation District Act of 1964, § 15.2-4500 et seq., VA Code Ann.³ Among NVTC's and PRTC's significant transportation-related planning, construction, operations and funding functions is their joint ownership and operation of the VRE commuter rail service. Verified Statement of Stephen A. MacIsaac and Richard K. Taube ("MacIsaac/Taube VS") (Exhibit A to VRE Comments, at 1.)⁴

³ NVTC is comprised of the counties of Arlington, Fairfax and Loudoun, and the cities of Alexandria, Falls Church and Fairfax. NVTC's territory has a population of 1.3 million and covers approximately 1,000 square miles. MacIsaac/Taube VS at 1. PRTC's member jurisdictions include the counties of Prince William and Stafford and the cities of Manassas, Manassas Park and Fredericksburg. PRTC's territory consists of 630 square miles with a total population of 410,000. Twenty-two percent of PRTC's working population commutes, primarily on the I-95 and I-66 corridors, to employment centers within the District of Columbia and its immediate environs. MacIsaac/Taube VS at 2.

⁴ VRE is a partnership among eight local governments, the Commonwealth and VRE's customers. VRE's Master Agreement requires a fare box recovery of at least 50 percent of its annual operating budget of about \$20 million. VRE's capital budget (including debt service) is over \$10 million annually. Customers have paid about a third, local governments a fifth, the federal government a third, and the Commonwealth the balance of the combined operating and capital budgets. MacIsaac/Taube VS at 6.

VRE began operations in the summer of 1992, having spent close to \$150 million on terminals, stations, track improvements, rolling stock and training, and having obtained federal legislation that authorizes full indemnification by VRE of freight railroad conduct, including gross negligence. MacIsaac/Taube VS at 3-6.

2. VRE's Operating Statistics

VRE's 24 daily trains (12 on the Fredericksburg Line and 12 on the Manassas Line) serve 18 stations. South of Alexandria, Virginia the NS line joins the C3X line, and at the Potomac River both use the Conrail bridge and line to reach Amtrak's Union Station. In addition, VRE customers may use their VRE tickets on several Amtrak trains which to a limited extent expand the hours of service available to VRE customers beyond the restricted periods of operation allowed by the freight railroad track owners. MacIsaac/Taube VS at 5.

VRE ridership grew sharply during the first three years of service and peaked in mid-FY 1996. From about 3,500 average daily passenger trips in the first year to over 8,000 average daily trips in the fall of 1995 and winter of 1996, VRE demonstrated that it could provide a safe, affordable and reliable commuting alternative, carrying the equivalent of a freeway lane of automobile traffic in the heavily congested I-66 and I-95 corridors. Indeed, an analysis by NVTC staff revealed that the \$150 million investment in VRE by the Commonwealth of Virginia and VRE's local governments was less expensive than building the equivalent freeway capacity, when both were operated over a 20-year period. MacIsaac/Taube VS at 5-6.

Ridership since mid-FY 1996, however, has declined significantly as a result of several factors, including ill-advised track maintenance procedures by NS in the summer of 1996, which penalized on-time performance on the Manassas Line, and various delays caused by CSX freight

operations, including most significantly a CSX derailment in July 1997 and subsequent track and signal repairs and upgrades, which severely reduced VRE on-time performance for more than a month.⁵ With frequent late trains, slow trains and annulled trains, VRE's ridership in August 1997 fell to approximately 25 percent below mid-FY 1996 levels. In early October 1997, despite some gains, ridership remained 15 percent below the 1996 levels on the Manassas Line and 20 percent on the Fredericksburg Line. MacIsaac/Taube VS at 6.⁶

3. Public Investment For VRE Service

Approximately one-third of VRE's annual capital budget is devoted to improvements to the Fredericksburg Line. The improvements are funded by the Virginia Department of Rail and Public Transportation ("VDR&PT"), using federal funds. VRE has paid for the Woodbridge crossover (approximately \$1.25 million) north of Quantico Bridge and is predisposed but not committed to pay for the Aquia crossover south of Quantico Bridge. The addition of these crossovers would double the number of crossovers in the area and help both freight and passenger trains avoid delays. Again, VRE is predisposed but not committed to pay for track and signal improvements between a point near the Potomac River (RO) and a point near Telegraph Road (AF), at an expense of approximately \$2,650,000. These track and signal improvements are designed to increase train speeds, decrease travel time and consequently increase VRE ridership.⁷

⁵ It should be noted that ridership declines are rare among U.S. commuter railroads which generally have been experiencing significant ridership growth.

⁶ Freight-related delays to VRE's on-time performance are discussed in greater detail in VRE Comments at 20-28 and the Verified Statement of Stephen T. Roberts ("Roberts VS") (Exhibit B to VRE Comments).

⁷ VRE's capital improvement program also contains a plan to add a new bridge over Quantico Creek, at an expense of approximately \$20 million, which would add an additional track to replace the track that CSX ripped up shortly before VRE began operations. The additional

The increased operating flexibility which would be made possible by the above-described capital improvements would add to line capacity. However, the Woodbridge/Aquia crossovers and the track and signal improvements between the Potomac River and Telegraph Road would be installed only if VRE's service would benefit from them. The Commissions are pleased that there is also a benefit to freight service from these publicly funded improvements, but it should be recognized that the improvements will not be made if they do not enhance VRE service. CSX has simply assumed that additional capital projects which increase capacity are or will be forthcoming. App., Vol. 3A at 227. Unless CSX is prepared to represent that it will make the improvements even if public funding is not forthcoming, the STB should not assume that the improvements will be made or factor the improvements into its consideration of the proposed Conrail acquisition and the adequacy of capacity on the Fredericksburg Line.

4. Public Interest Benefits Of VRE

Several factors point to a sound future for VRE, despite the substantial ridership decline from VRE's mid-FY 1996 peak. First, projections of employment and population in VRE's core markets show steady growth. Automobile ownership and vehicle miles traveled are forecast to outpace new highway capacity, and traffic congestion, already the second worst in the United States, will get worse. If VRE can restore its reputation for on-time performance, its ridership should resume a healthy growth trend.

Second, VRE's ridership is sensitive to the frequency of service. The freight railroads have not allowed VRE to expand service as it wished, citing competition with existing freight traffic for track time. The very substantial growth of freight train traffic predicted by NS and

span of bridge at Quantico Creek would enhance the benefit of the Woodbridge/Aquia crossovers.

CSX in this proceeding indicates that even greater pressure will be placed on VRE's existing schedules, and any capacity enhancements resulting from VRE's investments in CSX and NS rights-of-way could be eroded before VRE is allowed to operate any new service.⁸ But, in conjunction with capacity improvements, if VRE is allowed to expand service frequency, its state-of-the-art ridership forecast model (and the experience of commuter railroads across the country) indicate a healthy ridership response. MacIsaac/Taube VS at 9.

Third, VRE is well positioned to serve the region when special circumstances require a quick and innovative response. A pending 10-year reconstruction of the intersection of I-95/395/495 (Mixing Bowl) at Springfield, Virginia will take a lane of highway capacity out of service. VRE likely will be part of a multi-modal strategy to mitigate traffic congestion during the Mixing Bowl reconstruction, and this will boost VRE ridership. During snow storms and for special events, VRE also is used heavily and has been quite reliable. MacIsaac/Taube VS at 9-10.

VRE data compiled for submission to the U.S. Department of Transportation's ("U.S. DOT") National Transit Database reveal that in FY 1997 VRE provided 57,116,170 passenger miles of service at an average cost of only 32 cents per passenger mile. This compares very favorably with costs of operating single-occupant automobiles. VRE has operated without a passenger fatality or even serious injury since 1992. At VRE's FY 1997 level of ridership (1,758,471 passenger trips) reduced automobile usage by VRE passengers cut consumption of gasoline by approximately 2.9 million gallons. MacIsaac/Taube VS at 10.

⁸ The pressures this increased traffic will place on VRE operations are discussed further at pages 12-15 infra and in the Roberts Verified Statement and the Verified Statement of Charles H. Banks ("Banks VS") (Exhibit C to VRE Comments).

Northern Virginia is designated as a "serious" ozone area by the U.S. Environmental Protection Agency. Accordingly, the region must prepare air quality plans and spend millions of dollars to devise methods to reduce ozone levels to acceptable levels. An emissions analysis performed by NVTC in 1994 shows that each work day VRE service results in 0.06 fewer tons of hydrocarbons, 0.42 fewer tons of carbon monoxide, 0.19 fewer tons of nitrogen oxide and 0.07 fewer tons of volatile organic compounds (the controlling pollutant in smog formation in the Washington, D.C. area). These amounts are net of auto trips by VRE customers to and from VRE stations. MacIsaac/Taube VS at 10.⁹

B. Projected Impact Of Acquisition On VRE Service

1. VRE History Of Significant Freight-Related Service Problems

The Applicants' projections of non-interference with VRE operations must be viewed in the context of the freight-related delay history of VRE. Delays occasioned by CSX accidents and resulting repairs have severely impacted VRE's operations and ridership. For example, a CSX freight derailment in early July 1997 and necessary repairs resulted in delays that in turn contributed to an approximate 25 percent decrease in VRE ridership over the ensuing two-month period. VRE's on-time performance dropped to less than 40 percent (for July 1997), with a year-to-date (January-August) actual on-time performance of only 83 percent. Roberts VS at 3.¹⁰ In

⁹ U.S. DOT and VRE studies and surveys highlight the important public benefits generated by VRE specifically. See VRE Comments at 15-16. Also, commuter rail systems around the United States consistently generate economic activity that yields a substantial return on the investment of public funds. In a September 1997 study for the American Public Transit Association, the Carmen Group, Inc. estimated that commuter rail economic and societal benefits are \$5.2 billion annually. Commuter Rail: Serving America's Emerging Suburban/Urban Economy, Carmen Group, Inc. for APTA (Sept. 1997).

¹⁰ A CSX internal memorandum, CSX 52 CO 000174, dated August 6, 1997, recognized that VRE on-time performance for July 1997 was a "'real' [] percent" as a result of the derailment and subsequent repairs and acknowledges that "VRE is close to falling below its

fact, during the July-early August time period, VRE had the worst on-time performance record of any commuter rail system in the U.S. and Canada. Roberts VS at 3. VRE lost \$300,000 in fare box revenue because of these delays in the immediate aftermath of the derailment and the adverse revenue consequences continue to this day. Roberts VS at 3.

This recent incident demonstrates vividly the extreme sensitivity of VRE's service to freight operations and how unreliable freight operations have threatened the very existence of VRE. Moreover, delays to VRE passenger service as a result of freight train problems are routine occurrences on the CSX line. Data assembled by VRE and included in the Roberts Verified Statement demonstrates that for the period July 1995 through August 1997 (which corresponds to VRE's 1996 and 1997 fiscal years, plus the first two months of fiscal year 1998), VRE's actual on-time performance averaged only 85.9 percent. In the commuter operations industry, this is substantially below desired on-time performance. Roberts VS at 3.¹¹ On-time performance is an absolute priority to most commuter rail passengers, as evidenced by the severe decline in VRE ridership following heavy delay periods and by commuter-passenger survey responses.

MacIsaac/Taube VS at 12.

As explained in detail in the Roberts Verified Statement, much of this delay to VRE operations has been the result of freight train problems, including numerous line-related malfunctions and maintenance-related problems, stemming in large part from CSX's poor

percent revenue coverage...." See also "Officials Say Drop in Riders, Revenue Has VRE Headed for Doom," Washington Post, Aug. 15, 1997, D1, D6, attached as VRE-9 (Vol. II), Exhibit 2.

¹¹ For example, METRA, which serves the Chicago metropolitan area and is a well-regarded commuter operation, has an on-time performance that consistently averages in the 94-98 percent range. Roberts VS at 3.

management and supervision of the rail lines and its failure to properly coordinate operations and communicate with VRE officials. Roberts VS at 2-8. Despite these difficulties, CSX plans to continue its dispatching practice post-acquisition, dispatching the VRE line out of Jacksonville "in the current way that the territory is dispatched today." Orrison Tr. 524.

Since CSX plans to maintain its "current way" of dispatching the line over which VRE operates, there is no reason to expect that the inadequate CSX communication to its dispatchers with respect to this line will improve in any way. Indeed, since CSX will now have the added responsibilities of also dispatching the Conrail line segment from Potomac Yard to Virginia Avenue, D.C. and dispatching a substantially greater number of freight trains on the lines, the resulting CSX dispatching-related problems for VRE undoubtedly will increase. Rather than attempt to address this in its Operating Plan by proposing a metropolitan Washington dispatching district or some other approach designed to address these dispatching-related concerns, the Operating Plan simply fails to address the issue at all.¹²

2. There Will Be Substantial Increases In Freight Traffic On VRE Lines

Both CSX and NS have indicated in their proposed Operating Plans that they plan substantial increases in freight train operations on the rail lines over which VRE provides service. Although Applicants continue to assert the absence of conflict with VRE service, existing congestion is demonstrated by the need to fund improvements by VRE. Increased freight

¹² Similarly, the Operating Plan does not address how train and engine crews districts will be affected by the acquisition or how field supervision will be affected in the territory over which VRE operates. VRE also notes that many of the concerns, including communications and dispatching concerns, raised in the Roberts Verified Statement based on VRE's experience with CSX were contemporaneously echoed in the FRA's Safety Assurance and Compliance Report for CSX Transportation, Inc., Oct. 16, 1997.

operations will cause further congestion on these already busy rail transportation arteries.

In its Operating Plan, NS has indicated that after the acquisition it will operate approximately two more freight trains per day on the line between Manassas and Alexandria, which represents a 23 percent increase in freight train operations over this line shared with VRE. While NS states that there will be "no identifiable adverse effects" on any of VRE's commuter rail operations (Primary Application ("App.") Vol. 3B at 306), VRE is concerned about the impact this 23 percent increase will have on its current operation of twelve commuter trains per weekday on the Manassas Line. Roberts VS at 2.¹³ Moreover, the NS Operating Plan projection of increased freight traffic appears to be understated; the increase in fact will be closer to four trains per day or approximately 45 percent more than current freight traffic. Banks VS at 9. NS has also acknowledged that the Manassas Line is a much more direct and desirable route for NS coal and other traffic to the Baltimore and Wilmington markets than the NS Hagerstown-Harrisburg route, creating the distinct likelihood that greater volumes of this traffic ultimately will be rerouted over the Manassas Line to the detriment of VRE commuter operations. Banks VS at 18-20 (citing McClellan deposition testimony).

The CSX Operating Plan raises far greater concerns. According to the Plan, the CSX Fredericksburg-Alexandria segment currently carries 22 passenger trains per day (twelve of which are VRE trains) and is projected to experience an increase of seven freight trains per day. App., Vol. 3A at 279, 409. This represents a 43 percent increase in freight train operations on this 49-

¹³ Subsequent to the filing of its Comments, VRE has dropped one round trip train on the Manassas Line, reducing the total number of VRE trains on that segment from fourteen to twelve. Since this train continued on to the Alexandria-Virginia Avenue segment, the total number of VRE trains operating between Alexandria and Virginia Avenue has changed from 26 to 24.

mile line segment. The post-acquisition increase in freight operations is even more dramatic on the line segment between Alexandria and Virginia Avenue. This line carries 33 passenger trains per day (24 of which are VRE trains) and will experience an increase of eleven freight trains (CSX and NS) per day (App., Vol. 3A at 280, 412), which represents an increase of 61 percent over the pre-acquisition level.¹⁴

The CSX Operating Plan itself reveals that of all the passenger lines that will undergo moderate to substantial increases in freight activity, the CSX line and current Conrail line -- particularly the Alexandria-Virginia Avenue segment -- are among the most sensitive to freight train increases. Table 13.8-2 of the CSX Operating Plan (App., Vol. 3A at 409-12) lists projected changes in freight trains per day on CSX and current Conrail line segments hosting passenger service. This table includes projected increases of both CSX and NS freight traffic. Orrison Tr. 369-72. Although there are more than 100 lines listed, only six line segments are projected to have an increase of ten or more freight trains per day. With the exception of the Alexandria-Virginia Avenue segment, however, none of these segments carries significant passenger traffic, as all of these lines have only two or fewer passenger trains per day. App., Vol. 3A at 409. In contrast, the Alexandria-Virginia Avenue line segment is erroneously said to carry 35 passenger trains per day. App., Vol. 3A at 412. In fact, it handles many more. (See Footnote 14.)

Thus, of all the CSX/Conrail lines scheduled to undergo substantial post-transaction increases in freight traffic (i.e., ten trains or more per day), the line that has by far the greatest volume of passenger operations is the Alexandria-Virginia Avenue segment. Indeed, with the

¹⁴ CSX apparently has undercounted the number of trains on these lines. There are 28 (not 22) passenger trains on the Fredericksburg-Alexandria segment and 42-44 (not 35) on the Potomac Yard-Virginia Avenue segment. Banks VS at 5.

exception of a handful of lines, primarily in the New Jersey area, all of the CSX/Conrail lines with substantial passenger operations are scheduled to experience a decrease in freight traffic. The potential impact, therefore, of substantial projected increases in freight traffic on lines already carrying substantial passenger traffic -- and the corresponding need to protect such passenger operations -- is nowhere more clearly evident than on the CSX/Conrail Fredericksburg - Washington segment.

CSX itself has expressly recognized the Fredericksburg Line as a heavily constrained one on which passenger operations are extremely sensitive to freight operations. VRE Comments at 19. Yet CSX now proposes a 43 percent to 61 percent increase in freight train operations in this corridor, claiming that this "moderate" increase will not have a significant impact on commuter operations. App., Vol. 3A at 276. CSX bases its position on the conclusory assertion that "these lines have *sufficient capacity* to accommodate the freight increases without adverse impact on commuter service." App., Vol. 3A at 276 (emphasis added). CSX has attempted to support this conclusion with a string line analysis that charted only seven miles of largely triple-track line, conveniently and misleadingly ignoring the approximately 45.7 miles of the double-track (and partially single-track) railroad over which VRE operates.¹⁵ The full string line analyses set forth in the Banks Verified Statement clearly show the delay resulting from CSX's projected increase in freight trains on the Fredericksburg Line. Banks VS at 7-8 and Attachment B; see also DEIS

¹⁵ This partial string line analysis by John Orrison of CSX, which was done at the rebuttal stage, is the only quantitative effort CSX or NS has made to refute the detailed quantitative analyses presented by VRE in its comments. See VRE Comments at 28-31.

Verified Statement of Charles H. Banks, which was filed with the Commissions' Comments on the DEIS ("Banks DEIS VS") at 3-4.¹⁶

3. Applicants Have Proposed No Capacity-Related Improvements

CSX has not identified a single capacity-enhancing improvement on the critical Fredericksburg Line other than publicly funded improvements that will be made by the Commissions only if they enhance or improve VRE service.¹⁷ The only capacity-enhancing improvement that Applicants plan to make in the vicinity of the lines on which VRE trains operate is the proposed speed restoration characterized as an "improvement" of the Virginia Avenue tunnel. VRE does not operate through the Virginia Avenue tunnel. The Applicants have not provided any evidence that improvements of the Virginia Avenue tunnel will improve the movement of VRE trains on the Fredericksburg Line. In fact, it is likely that improvements to the Virginia Avenue tunnel will increase delays to VRE trains or otherwise reduce capacity on the Conrail line (to be acquired by CSX) during the construction of the improvements.

4. Applicants Have Failed To Consider The Impacts On VRE Service

The methodology CSX and NS used to arrive at projected post-acquisition freight train

¹⁶ Applicants have attempted to ignore the impact of the Conrail takeover on VRE service at every step. Applicants have even tried to blame their capacity problems on VRE. The Applicants state that "VRE erroneously assumes that capacity on the line is constrained by freight traffic, when in fact it is constrained by passenger traffic." Verified Statement of Paul H. Reistrup, App. Reb., NS/CSX-177, at 245. Were that true, one would expect to find significantly improved freight train performance during the weekends when VRE trains do not operate. However, as the Banks DEIS Verified Statement demonstrates, CSX freight train operations do not improve on the weekends when VRE trains are not operated on the Fredericksburg Line. Banks DEIS VS at 8-11.

¹⁷ The Verified Statement of Paul Reistrup in CSX's Rebuttal points to various improvements (Verified Statement of Paul H. Reistrup, Applicants' Rebuttal ("App. Reb."), NS/CSX-177, at 248-49) CSX has made, but these are more properly characterized as maintenance-of-way expenditures, rather than capacity-enhancing improvements. Banks DEIS VS at 6-7.

densities resulting from the acquisition was freight-driven and passenger-insensitive. McClellan Tr. 286-87; Orrison Tr. 534, 537. Existing passenger traffic on a line was not factored into the density calculations, nor was any effort made to consider the potential impact of any future increases, however modest, on passenger operations. Orrison Tr. 537; Mohan Tr. 383. In addition, the delay history of a particular line was not quantitatively factored into freight density calculations. Orrison Tr. 539-40; Mohan Tr. 360-61.

In light of these solely freight-driven evaluations, it is not surprising that CSX scheduled substantial increases in freight traffic over the Richmond-Washington line, despite the substantial passenger traffic that exists on that line. Moreover, in scheduling improvements to a line to accommodate freight operations (and specifically with regard to the Alexandria-Virginia Avenue line), CSX made no effort to ascertain possible delays to CSX freight trains or VRE passenger operations as a result of construction of these improvements. Orrison Tr. 543. Yet, as explained in greater detail in the Banks Verified Statement, constructing these freight train-related improvements, which include clearance of the Virginia Avenue tunnel to accommodate automotive vehicle freight and at various other places along the line, will cause substantial additional delays to VRE passenger trains. Banks VS at 15-16.

Consistent with basing their projected changes in freight train line density entirely on freight traffic considerations, Applicants have not attempted to address resulting freight-passenger conflicts through any "structural" undertakings specifically designed to ensure accommodation of passenger operations (e.g., reducing the number of freight trains at peak commuter times because of existing passenger traffic, planning improvements to accommodate passenger traffic). Instead, Applicants will attempt to avoid any negative impact on passenger operations solely by "correct

scheduling" of freight train service. Orrison Tr. 380-81; see also Orrison Tr. 531-32.

CSX's rationale that its scheduling alone will avoid freight-passenger congestion and conflict is clearly deficient. First, it ignores the chronic line-related and maintenance-related delays that have occurred on those lines. Second, it presumes -- and depends wholly upon -- an on-time performance that CSX has not demonstrated on the lines over which VRE operates. CSX trains through Potomac Yard in a very recent, month-long period on average deviated approximately three hours from schedule. Banks VS at 10.

Third, CSX's purported reliance on its scheduling to avoid conflicts with VRE operations is undermined by the proposed scheduling of the substantial additional freight traffic CSX plans to add to the lines over which VRE operates. According to CSX's scheduling information, [] of the seven additional trains CSX will run on the segment between Fredericksburg and Virginia Avenue in Washington, D.C. have been scheduled to operate during the morning and evening hours in which CSX requires that VRE operate all of its service. Banks VS at 7.¹⁸ As a result of the acquisition, therefore, the number of CSX daily freight trains that will share the corridor with VRE trains operating in the same restricted rush hour periods will increase from 43 percent to [] percent of total CSX daily freight trains scheduled (an increase of nearly [] percent). Banks VS at 7. Post-acquisition, the number of CSX and NS trains that will operate within VRE commuter operating hours on either the Fredericksburg or Manassas Lines that will also operate between Alexandria and Virginia Avenue will [], from six to []. Banks VS at 9.

Fourth, as the Banks Verified Statement demonstrates based on actual CSX freight train

¹⁸ This scheduling of new freight trains during VRE operating hours is not limited to CSX. [] of the new trains NS will be adding to the NS line will operate during VRE's peak operating hours. Banks VS at 7-8.

performance, freight train scheduling is an aspiration, not an achievement, of CSX. Banks VS at 10-11.

Even employing conservative projection assumptions, VRE on-time performance after the acquisition will decline from the already unacceptably low 85.9 percent figure (Roberts VS at 3) to about 81 percent. Banks VS at 14.¹⁹ If the hypothetical string line approach proposed in the Orrison Verified Statement is applied, four of twelve Fredericksburg Line VRE trains would be delayed every day. Thus, despite Applicants' repeated assurances that their "correct scheduling" will ensure non-interference with VRE operations, in reality the proposed scheduling of substantially increased freight traffic (particularly CSX's traffic) will only exacerbate the freight-commuter conflicts that already exist.²⁰

VRE is also concerned that the Fredericksburg - Virginia Avenue line ultimately will carry more freight traffic than CSX projects. CSX's Operating Plan states that traffic currently routed through St. Louis or Memphis may alternatively be routed via the New Orleans Service Route, which means that origin-destination pairs such as Houston-Philadelphia will be better served via

¹⁹ CSX's rebuttal allegation that VRE's cumulative average on-time performance ignores "current performance" is unsupported by the actual facts. Had the Banks analysis included all of the most recent months (i.e., the entire "current performance"), the analysis would have produced even lower VRE on-time performance averages because VRE's on-time performance was severely impacted in July and August 1997 as a result of the CSX freight train derailment in July. By excluding July-August 1997 and taking the remaining entirety of the 1996-1997 period for which data were available, the Banks analysis was both representative and fully fair to CSX.

²⁰ Applicants' reliance on "correct scheduling" to prevent interference with VRE operations is reiterated in Applicants' Rebuttal wherein Mr. Orrison asserts that "by adhering to these schedules, train operations will flow more smoothly and freight service will be improved." App. Reb., NS/CSX-176, at 611. This assertion, however, is wholly devoid of any indication as to how such schedule adherence will be accomplished.

this route. App., Vol. 3A at 131-32. This also means, of course, that the combined CSX/Conrail line over which VRE operates will carry much of that traffic since key pairs, such as Houston-Philadelphia, will be served by the New Orleans Service Route via the CSX Richmond-Washington, D.C. corridor. App., Vol. 3A at 130; Banks VS at 17.

III. ARGUMENT

A. If The Commission Approves The Conrail Merger, It Should Impose The Conditions Requested By The Commissions

Public interest considerations require that the Board impose the conditions sought by the Commissions. The conditions are narrowly tailored to address the specific merger-related harms to VRE services. The conditions will not infringe upon the substantial public benefits that the Applicants project if their merger is approved.

1. Applicable Legal Standard

The Board may approve the merger of two railroads only if it finds that the merger "is consistent with the public interest." 49 U.S.C. § 11324(c). In making this determination in a proceeding that involves the merger of two Class I railroads, the Board is required to take into account "the effect of the proposed transaction on the adequacy of transportation to the public." 49 U.S.C. § 11324(b)(1). This factor clearly includes consideration of the impact of the merger on commuter rail operations such as those conducted by VRE.

If the Board finds that a proposed merger will produce harmful effects, it has "broad authority to impose conditions." 49 U.S.C. § 11324(c); *Union Pacific Corp., Union Pacific R.R. Co., and Missouri Pacific R.R. Co. -- Control and Merger -- Southern Pacific Rail Corp., Southern Pacific Transp. Co., St. Louis Southwestern Ry. Co., SPCSL Corp., and The Denver and Rio Grande Western R.R. Co.*, Finance Docket No. 32760 (STB served August 12, 1996)

("UP/SP") at 144; *Burlington Northern, Inc. -- Control and Merger -- Santa Fe Pacific Corp.*, Finance Docket No. 32549 (ICC served August 23, 1995) ("BN/SF") at 55; *Union Pacific -- Control -- Missouri Pacific; Western Pacific*, 366 ICC 459, 562 (ICC 1982), *aff'd sub. nom. Southern Pacific Transp. Co. v. I.C.C.*, 736 F.2d 708 (D.C. Cir. 1984), *cert. denied*, 469 U.S. 1208 (1985) ("UP/MP/WP").

The Board's policy is that it will impose conditions when it finds:

- Absent a condition, the proposed railroad consolidation may produce effects harmful to the public interest;
- An appropriate condition will ameliorate (or eliminate) the harmful effects;
- The condition is operationally feasible; and
- The conditions will yield public benefits outweighing any reduction in the benefits of the railroad consolidation.

Each of the conditions VRE seeks satisfies all elements of the Board's four-part test.

2. Form Of Proposed Conditions

Applicants are highly critical of VRE's proposed conditions because the conditions are in the form of amendments to the existing contracts pursuant to which VRE uses the Conrail, CSX and NS lines. App. Reb., NS/CSX-176, at 264-65. The Board has authority to fashion conditions in any form that it deems appropriate, including imposition of contract changes. See, e.g., BN/SF at 94 (modification of interchange agreement to permit Grainbelt Corporation to interchange with Southern Pacific at one connection and Farmrail System, Inc. at another location); *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 (ICC served February

21, 1995) at 102 (granting Soo Line's request for relief from contractual prohibitions on transfer of interests in certain lines). VRE put its proposed conditions in the form of contract revisions in order to be as specific as possible in tailoring the conditions to the anticipated harms arising from the Conrail takeover. However, it is important to note (as Applicants acknowledge) that VRE is seeking operating rights over all of the lines on which it now operates subject to terms and conditions to be negotiated by the parties or, failing a negotiated agreement, set by the Board. VRE Comments at 31-32. If the Board would prefer to grant VRE's requested relief in the form of free-standing conditions, VRE would have no objection. Of course, doing so would necessitate using broader language than would granting conditions in the form of contract revisions.

3. Overview Of The Proposed Conditions

Before addressing the proposed conditions specifically, it is important to make two general points. First, because they are narrowly tailored, the proposed conditions would work together to protect VRE service from the harms of the Conrail takeover. Granting some, but not all of the proposed conditions could cause those that are granted to be less effective, unless those granted were strengthened or made broader. Second, the proposed conditions would not put VRE service in a better position than it is in today. Even with the conditions, after consummation of the Conrail takeover, CSX and NS through their own actions and level of effort, will have the ability to directly influence the success or failure of VRE. The same is true today. The Commissions do not seek conditions that would constitute a guarantee of VRE on-time performance or even a guarantee of improved VRE service. The Commissions seek only those

protections that would give the VRE service a reasonable chance to not be worsened by the Conrail takeover.

B. Proposed Conditions Regarding CSX Agreement

Attachment 3 to the VRE Comments is the current CSX Access Agreement marked to show changes that the Commissions request the Board impose on CSX as a condition of any approval of the Primary Application.²¹

1. No Further Subordination Of VRE Service Rights

Section 2.6(a) of the current CSX Agreement permits CSX to grant new rights for use of the CSX rail line to third parties. The Commissions want this section to be changed so that any such grants of rights after the most recent amendment of the current CSX Agreement (January 10, 1995) would be subject to the current rights (at the time of such grant) of the Commissions to use the CSX rail line. Attachment 3 at 14-15.

Absent this rather modest condition, CSX could grant operating rights on the line between Spotsylvania, Virginia and Virginia Avenue Interlocking²² to NS or other parties which would be of superior priority to the current rights of VRE. This proposed condition would ameliorate the potential harms of the Conrail takeover by limiting CSX's right to add third-party trains with a higher priority than VRE trains. The proposed condition is clearly feasible. It would not reduce

²¹ VRE Comments, VRE-9 (Vol. II), Attachment 3.

²² This section discusses the proposed conditions regarding the CSX Agreement. The following section discusses the proposed conditions regarding the Conrail Agreement. The Commissions request that the Board modify the current CSX Agreement to include the Conrail line which is the subject of the current Conrail Agreement. Thus, as appropriate, this section discusses the CSX Agreement including references to the line currently owned by Conrail that will be acquired by CSX between RO Interlocking in Arlington, Virginia and Virginia Avenue Interlocking.

the public benefits of the Conrail takeover, because it would not prohibit or limit CSX's right to grant new rights for use of the Fredericksburg Line.

2. VRE Proposed Changes In VRE Schedules

Section 2.6(a) of the current CSX Agreement also permits CSX to approve or reject any proposed modification of the VRE commuter rail service or of the VRE commuter rail service schedule. The Commissions do not propose that this right be changed. However, the Commissions do want this section to be changed so that CSX would be required to review any proposed modifications with the existing Joint Operations Committee²³ and, if the Joint Operations Committee cannot agree on proposed modifications, the issue would be submitted to the CSX chief operating officer and the Commissions' chairmen for review and recommendations. Attachment 3 at 15-16.

Absent this very modest condition, increased freight traffic on the Fredericksburg Line could motivate CSX to summarily reject any proposed modification in VRE commuter rail service without making a good faith effort to determine whether the proposed modification was feasible. The proposed condition would ameliorate potential harms arising from CSX's failure to fairly consider proposed modifications. The condition is purely procedural and therefore feasible. As noted above, the Commissions do not propose that CSX's existing right to approve or reject any

²³ Under the current CSX Agreement, the parties have established an operating committee (the "Joint Operations Committee") consisting of representatives of CSX and the Commissions, which meets quarterly to discuss issues pertinent to the safe and efficient operation of rail services on the CSX rail line and to review service and performance and make findings, and formulate recommendations for consideration of CSX and the Commissions regarding operation of the service. The findings and recommendations of the Joint Operations Committee are advisory only and CSX reserves the right to make its own determinations with respect to the subjects discussed by the Committee. Section 2.6(a). The Commissions do not propose to change this provision.

proposed modification be changed. Therefore, this proposed condition would not in any way reduce the benefits of the Conrail takeover.

3. Changes In CSX Line Due To Current VRE Operations

Under Section 2.9(a) of the current CSX Agreement, capital improvements may be made to the CSX rail line when, in the judgment of CSX, they are necessary or desirable, or required by law. If CSX deems such capital improvements to be occasioned or required because of the presence of the VRE commuter rail service, the Commissions must pay for them.²⁴ If the Commissions fail to agree to pay for the capital improvements or if CSX is unable to make improvements in the manner and time required for safe and economical operations, CSX is entitled to suspend all or part of VRE commuter rail service. Once made, the costs of maintaining such capital improvements are charged to the Commissions. The Commissions want this provision to be changed so that it governs only capital improvements required by law and not those deemed "desirable" by CSX. Attachment 3 at 18-19.

Given the significant increases in freight traffic on the Fredericksburg Line, CSX will require substantial capital improvements over the course of the next few years. This is true even though CSX has not yet proposed to make any such improvements. The current contract provision, which permits CSX to charge the Commissions for capital improvements that CSX deems desirable was a reasonable obligation on the part of the Commissions in the pre-merger setting. With the Conrail takeover, however, there is substantial chance that CSX will desire

²⁴ Capital improvements required by CSXT are subject to an advisory-only review of the Joint Operations Committee and the Commissions chairmen may make recommendations to the CSX chief operating officer. However, CSXT has the unilateral right to make capital improvements and charge the costs to VRE.

capital improvements that in no way improve VRE's service and that CSX will charge these improvements to the Commissions. This would clearly be unfair and beyond the realm of what was contemplated by either party when the CSX Agreement was negotiated. The proposed condition would eliminate the possibility of this unfair outcome. CSX would still have the right to charge the Commission for capital improvements required by law to accommodate VRE commuter rail service. The parties would be free to negotiate sharing the cost of mutually advantageous improvements. The proposed condition is feasible and would not reduce the benefits of the proposed Conrail takeover because it would only prevent CSX from forcing the Commissions to pay for the capital improvements necessary for expansion of CSX service.

4. Certain Changes In The CSX Line Due To Changed VRE Operations

Certain proposed expansions in the VRE service are governed by Section 2.9(b) of the current CSX Agreement. Attachment 3 at 19-20. The Commissions do not propose any change in Section 2.9(b). However, Section 2.9(c) requires any expansion of VRE commuter rail service (beyond that contemplated in Section 2.9(b)) to be contingent on the Commissions' commitment to undertake, at no cost to CSX, the construction of a third main line parallel to the existing CSX rail line. Thus, the Commissions may request further expansion of VRE commuter rail service only by presenting to CSX evidence of their commitment to implement and fund all or a significant portion of the third main line and such other capital improvements as CSX deems necessary to ensure that commuter operations will not interfere with freight and intercity passenger service on the CSX rail line.

The Commissions want this provision to be changed so that if CSX determines that changes are necessary to accommodate the Commissions' desired expansion of service beyond

that called for in Section 2.9(b), CSX would have an obligation to meet and confer with the Commissions in a cooperative effort to jointly design, construct and fund a "third track" parallel to the CSX rail line. Once built, the rail line would be used by both VRE and CSX, in coordination with the existing lines. The third track would be constructed based upon a Master Service and Capital Improvements Plan (the "Master Plan") jointly developed by a task force comprised of senior officials of CSX, the Commissions and the Commonwealth of Virginia. The Master Plan would identify and address all capacity issues and ensure that capacity created by construction of the third line would be available for VRE commuter rail service. Failing agreement on a Master Plan, with the proposed Board condition the Commissions would have the right to continue running existing VRE trains without any obligation to fund additional capital improvements, but would not be permitted to run any increased number of VRE trains. The specific improvements agreed to under the Master Plan would be implemented pursuant to definitive agreements containing terms and conditions consistent with the Master Plan.

Attachment 3 at 20-22.

The significant increase in freight traffic on the Fredericksburg Line raises for the first time the possibility that CSX would consume all of the expanded capacity that would be created by the construction of a third track. The Commissions are concerned that, after having paid for the construction of a third main line, the increased freight traffic resulting from the Conrail takeover would consume that capacity and there would be no additional capacity for VRE service. Obviously, before they commit public funds for the construction of a third track, the Commissions will need to ensure that this will not occur.

The proposed condition would in two ways reduce the likelihood that the Commissions

would find themselves in this untenable situation. First, CSX would have an obligation to meet and confer with the Commissions in an effort to ensure that, if VRE were to pay for the third track, it would in fact gain capacity as such capacity is created. Second, in the event the parties are unable to agree to a plan for the construction of the third track, the Commissions would have the right to continue running existing VRE trains without any obligation to fund additional capital improvements. It is important to note that under the proposed condition, failure of the parties to reach agreement on a third track would also mean that VRE would not have the right to increase the number of trains it operates on the Fredericksburg Line.

This is a very limited condition and largely a procedural one. Requiring CSX to meet and confer with the Commissions and allowing VRE to continue running trains at present levels in the absence of an agreement to construct a third track is feasible and would not reduce the benefits of the merger.

5. Term Of CSX Agreement

Under Section 4.1 of the current CSX Agreement as extended, the agreement terminates on June 30, 1999. The parties have an obligation to meet during the term of the agreement to discuss its extension and possible modification. The Commissions want this provision changed so that the current CSX Agreement will run through June 30, 2008. Attachment 3 at 27.

6. CSX Revenue Losses

Section 5.1(a) of the current CSX Agreement requires, among other things, that if there is interference with CSX's ability to provide freight operations as a result of VRE commuter rail service, the Commissions will participate fully in costs incurred and revenues lost. The Commissions want this provision to be deleted from the CSX Agreement. Attachment 3 at 28.

Given the dramatic increase in the level of freight activity on the Fredericksburg Line

expected after the Conrail takeover, this provision is fraught with potential for unfair application. Post-merger, VRE will be operating the same number of trains on the same schedule as it was prior to the merger. CSX will be running substantially more freight trains on the Fredericksburg Line. It is quite likely that CSX will have service interruptions that are not due to the presence of VRE. It is possible that CSX will attempt to blame these service interruptions on VRE and charge VRE for increased costs and lost revenues. Deletion of this provision is required to protect the Commissions. Removal of the provision is feasible and would not reduce the benefits of the proposed Conrail takeover.

7. Compensation Paid To CSX

Under the current CSX agreement, Section 5.1(b), the compensation to CSX is based on a combination of a base payment and train-mile fee. In addition, compensation paid to CSX is subject to adjustment pursuant to a schedule, to account for inflation. The Commissions want this provision to be changed so that the base payment is adjusted annually by the greater of (i) four (4) percent or (ii) the CPI Urban Wage Earners and Clerical Workers for Washington, D.C. - Maryland - Virginia. The adjustment to the base payment would be subject to two incentive provisions. First, the base payment would not increase in any year in which the total number of passengers using the VRE commuter rail service decreased from the previous annual period by 15 percent or more. Second, any increase in the base payment would not be earned unless CSX achieved on-time performance targets set forth in the agreement.²⁵ Attachment 3 at 29-30.

As noted above, the Conrail takeover is almost certain to result in a reduction in the on-

²⁵ The proposed on-time performance criteria are set forth in Exhibit C-2 of the proposed CSX Agreement. See Attachment 3.

time performance of VRE trains on the Fredericksburg Line. VRE Comments at 28-31; Banks VS at 16-20. This condition would give CSX a modest incentive to operate VRE service at a higher level of on-time performance. The base payment would be flat in any year when VRE patronage decreased by 15 percent or more. Although VRE patronage could decrease for other reasons, a decrease of 15 percent or more would almost certainly involve a reduction in on-time performance or other service characteristics. Thus, reduction in patronage of 15 percent or more is a reasonable measure upon which to determine whether the base payment should increase. Similarly, any increase in the base payment would not be earned unless CSX achieved the on-time performance targets set forth in the Agreement. The on-time performance targets set forth in the Agreement are reasonable. The proposed condition would not reduce the benefits of the merger because CSX would in all cases earn the base payment and would also earn the increases in the base payment in years where it provided reasonable service to VRE.

C. Proposed Conditions Regarding Conrail Agreement

CSX will acquire the Conrail line between RO Interlocking and Virginia Avenue Interlocking. The Commissions request that the Board modify the current CSX Agreement, as described above, to include this Conrail line. Although adding this line will require adjustment of compensation terms and other changes in descriptions and definitions in the CSX Agreement, it will not itself require any substantive changes in the CSX Agreement (other than the changes described above, as applied to the former Conrail line).

D. Proposed Conditions With Respect To NS Line

Attachment 4 to the VRE Comments is the current NS Agreement marked to show changes that the Commissions request the Board impose on NS as a condition of approving the Primary Application.²⁶

1. No Further Subordination Of VRE Service Rights

Section 2.6(a) of the current NS Agreement provides that NS may elect to grant operating rights to third parties. The Commissions want this provision to be changed so that any such grant of rights after September 1, 1996 would be subject to the Commissions' rights to use the NS line for VRE's then-current commuter rail operations. Attachment 4 at 7-8.

Given the significant increases in freight traffic on this line, Banks VS at 2, 9, and 18-20, the proposed condition would ameliorate the potential harms of the Conrail takeover by limiting NS's right to add third-party trains with a higher priority than VRE trains. The proposed condition is clearly feasible. It would not reduce the public benefits of the Conrail takeover because it would not prohibit or limit NS's right to grant new rights for use of the line.

2. Changes In NS Line Due To Current VRE Operations

Under Section 2.9(a) of the current NS Agreement, NS has the right to make changes in, additions and betterments to, or retirements from the trackage (collectively referred to herein as "changes") as it deems necessary or desirable for the operation of such trackage or as are required by law. To the extent such changes are occasioned or required by operation of the VRE commuter rail service, NS has the right to require the Commissions to pay for them, and to pay for the cost of maintaining them. If the Commissions are unable to appropriate funding to pay for

²⁶ VRE Comments, VRE-9 (Vol. II), Attachment 4.

such changes, NS may suspend all or part of VRE's commuter rail service.

The Commissions want this provision to be changed so that if NS determines that changes are occasioned or required by the operation of the VRE commuter rail service, NS would have an obligation to meet and confer and negotiate in good faith with the Commissions for the purpose of determining whether and to what extent the Commissions and NS should share the cost of such changes to the NS rail line. After such good faith negotiations, if the parties are unable to agree on whether and to what extent the Commissions and NS should share the costs of such changes, the Commissions want the Board to require NS to arbitrate the issue in accordance with a prescribed arbitration provision contained in the current NS Agreement. The Commissions would remain obligated to pursue appropriation of required funds for their share of the cost of such changes to the NS rail line that were determined in the arbitration to be the responsibility of the Commissions. NS would retain the right to suspend all or part of the VRE commuter rail service in the event that the Commissions could not pay for changes that were deemed their responsibility under the arbitration award. Attachment 4 at 9-11.

Absent this condition, increased traffic arising from the Conrail takeover could motivate NS to make unreasonable determinations that changes in the NS line were required to accommodate VRE's current operations. The proposed condition would require NS to meet and confer, and negotiate in good faith with the Commissions to reasonably determine whether and to what extent the Commission and NS should share the cost of any required changes. The condition is operationally feasible, because it involves only an obligation to meet and confer, negotiate in good faith and arbitrate. It would not reduce the public benefits of the Conrail takeover, because it would not force NS to pay for any changes in fact required for

accommodation of current VRE commuter rail operations.

3. Changes In NS Line Due To Changed VRE Operations

Section 2.9(b) of the current NS Agreement explains that changes in the NS rail line (including changes in communication and signal facilities and crossing warning devices) are or may be required to permit the continuation, modification or expansion of the VRE commuter rail service. Upon written notice to the Commissions, NS may make such changes, and the Commissions are obligated to pay NS for the costs of such changes. In addition, the compensation to NS is increased to include the costs of normalized maintenance associated with such changes.

As noted above, the Commissions are proposing that disputes between NS and the Commissions regarding the Commissions' appropriate responsibility for capital improvements necessary in connection with VRE's current commuter rail service be subject to arbitration. Accordingly, the Commissions want Section 2.9(b) to be changed to relate only to modification or expansion of the VRE commuter rail service and to require that NS provide the Commissions with information regarding the estimated costs of such capital improvements and the opportunity to review and comment on such estimated costs.²⁷ Attachment 4 at 10.

This proposed condition is a companion of the proposed condition discussed immediately above. It would conform Section 2.9(b) to match the revised Section 2.9(a). The only additional requirement -- that NS provide the Commissions with information regarding the estimated cost of capital improvements and with the opportunity to review and comment on such estimated costs --

²⁷ The changes marked in Section 2.9(d) of the NS agreement are conforming in nature and do not contain any substantive proposed change.

is purely a procedural matter and therefore operationally feasible. This proposed condition would not in any way reduce the benefits of the Conrail takeover.

4. Term Of NS Agreement

Under Section 4.1 of the current NS Agreement as extended, the agreement terminates on July 15, 1998. The parties have an obligation to meet during the term of the agreement to discuss extension and possible modification of it. The Commissions want this provision to be changed so that the current NS agreement will run through July 31, 2006. Furthermore, the parties would have an obligation to meet during the last twelve months of the extended term. Attachment 4 at 15.

A substantial increase in freight traffic on the line could motivate NS to terminate the NS Agreement. Extending the Agreement for a period of approximately eight years after consummation of the Conrail takeover would prevent NS from terminating the NS Agreement as a result of the Conrail takeover. This condition is operationally feasible and would not reduce the benefits of the Conrail takeover because it would simply extend the existing contract (as modified by the other conditions, which also do not reduce the benefits of the proposed takeover).

5. VRE Acquisition Of NS Line

Under Section 4.2(a) of the current NS Agreement, the right of the Commissions to seek the continuation or expansion of commuter rail service beyond the current term is conditioned upon the Commissions' assurance that they will work in good faith to develop a plan to purchase the NS rail line.

The Commissions want this section to be changed so that their obligation with respect to the NS rail line would be to work in good faith to develop a plan to purchase, lease or acquire an interest in the NS rail line. The Commissions want to extend the timetable for its obligation to

purchase, lease or acquire an interest in the NS rail line. Under the Commissions' requested change, representatives of the Commissions and NS would meet during the last twelve months of the term of the proposed NS Agreement (July 31, 2005 would be the start of such period) to negotiate terms and conditions for the Commissions' purchase, lease or other acquisition of an interest in the NS rail line. If the parties were unable to reach agreement during a nine-month negotiation period, either party would have the right to submit unresolved issues to arbitration under an arbitration provision contained in the current NS Agreement.

In the event that neither party sought arbitration, NS would have the right to decline to renew the Agreement. In the event that arbitration was sought by one of the parties, the arbitrator's final decision would be binding on NS. The Commissions would have thirty (30) days to accept the terms and conditions set by the arbitrator. If the Commissions did not accept the terms and conditions set by the arbitrator, any continuation of their operations on the NS rail line would include a provision permitting NS to receive compensation reflecting the fair market value for the Commissions' use of the NS rail line. NS and the Commissions would have an obligation to meet and confer and negotiate in good faith for the purpose of determining the revised compensation terms. If, after attempting such negotiations, the parties were unable to agree to revised compensation terms, that issue could be submitted for resolution by arbitration. If neither party sought arbitration, the Commissions' right to use the NS rail line would terminate. The arbitrator's decision on the compensation award would be binding on NS. If the Commissions did not accept the terms and conditions set by the arbitrator, the right to continued use of the NS line would end ninety 90 days thereafter. Attachment 4 at 16-17.

This proposed condition is a companion of the proposed condition discussed immediately

above. It would conform Section 4.2(a) to Section 4.1. In addition, it would establish the process pursuant to which the parties would negotiate (or failing that, arbitrate) the terms and conditions for the Commissions' acquisition of the NS rail line. This condition is operationally feasible and would not reduce the benefits of the Conrail takeover. Importantly, NS would retain the right to decline to renew the extended Agreement in the event that (i) the parties were unable to reach agreement as to terms and neither party sought arbitration or (ii) the Commissions declined to accept the terms and conditions set by an arbitrator and declined to accept the fair market value compensation awarded by an arbitrator.

6. Compensation Paid To NS/Performance Incentive

Under the current NS Agreement, Section 5.1(c), the compensation the Commissions pay to NS is based on a combination of a base payment and a train-mile fee. In addition, the compensation paid to NS is subject to adjustment pursuant to a schedule, to account for inflation. The Commissions propose a new provision that would adjust the base payment on an annual basis by the greater of (i) four (4) percent or (ii) the CPI Urban Wage Earners and Clerical Workers for Washington, D.C. - Maryland - Virginia. The adjustment to the base payment would be subject to two provisions. First, the base payment would not increase in any year in which the total number of passengers using the VRE commuter rail service decreased from the previous annual period by fifteen (15) percent or more. Second, any increase in the base payment would not be earned unless NS achieved on-time performance targets in the agreement. Attachment 4 at 18-19.²⁸

As noted above, the Conrail takeover is almost certain to result in increased traffic on the NS line. Roberts VS at 2, 9 and 18-20. The proposed condition would give NS a modest

²⁸ The proposed on-time performance criteria are set forth in Exhibit C-2 of the proposed NS Agreement.

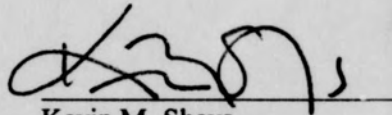
incentive to operate VRE service at a higher level of on-time performance. The base payment would be flat in any year where VRE patronage decreased by 15 percent or more. Although VRE patronage could decrease for other reasons, a decrease of 15 percent or more would almost certainly result from a reduction in on-time performance or other service characteristics. Thus, reduction in patronage of 15 percent or more is a reasonable measure upon which to determine whether the base payment should increase. Similarly, any increase in the base payment would not be earned unless NS achieved the on-time performance targets set forth in the Agreement. The on-time performance targets set forth in the Agreement are reasonable. The proposed condition would not reduce the benefits of the merger, because NS would in all cases earn the base payment and would also earn the increase in the base payment in years where it provided reasonable service to VRE.

IV. CONCLUSION

For the foregoing reasons, the Commissions respectfully request that the Board grant the conditions requested in the VRE Comments if it approves, in whole or in part, the transactions contemplated by the Primary Application.

Respectfully submitted,

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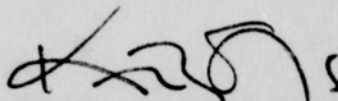
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Dated: February 23, 1998

CERTIFICATE OF SERVICE

I hereby certify that on this 25th day of February, 1998, a copy of the foregoing **Brief of Northern Virginia Transportation Commission and Potomac and Rappahannock Transportation Commission (VRE-12), Redacted Version** was served by first class mail, postage prepaid, upon the entities listed in 49 C.F.R. § 1105.7(b), Administrative Law Judge Jacob Leventhal and all Parties of Record on the Service List.

A handwritten signature in black ink, appearing to read 'K. Sheys', is written over a horizontal line.

Kevin M. Sheys

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FD33388

Re: 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

Dear Secretary Williams:

Yesterday we filed the Brief of Providence and Worcester Railroad Company in the above referenced matter. Attached to the brief as Exhibit A is a black and white map depicting the P&W Railroad Company's Operated Controlled Lines. Because the black and white map is difficult to read, we have obtained a clearer color version.

We would very much appreciate it if you would substitute the enclosed colored maps (25 copies) that we received this morning in place of the black and white copies that were filed with the brief.

Thank you for your cooperation in this matter.

Very truly yours,

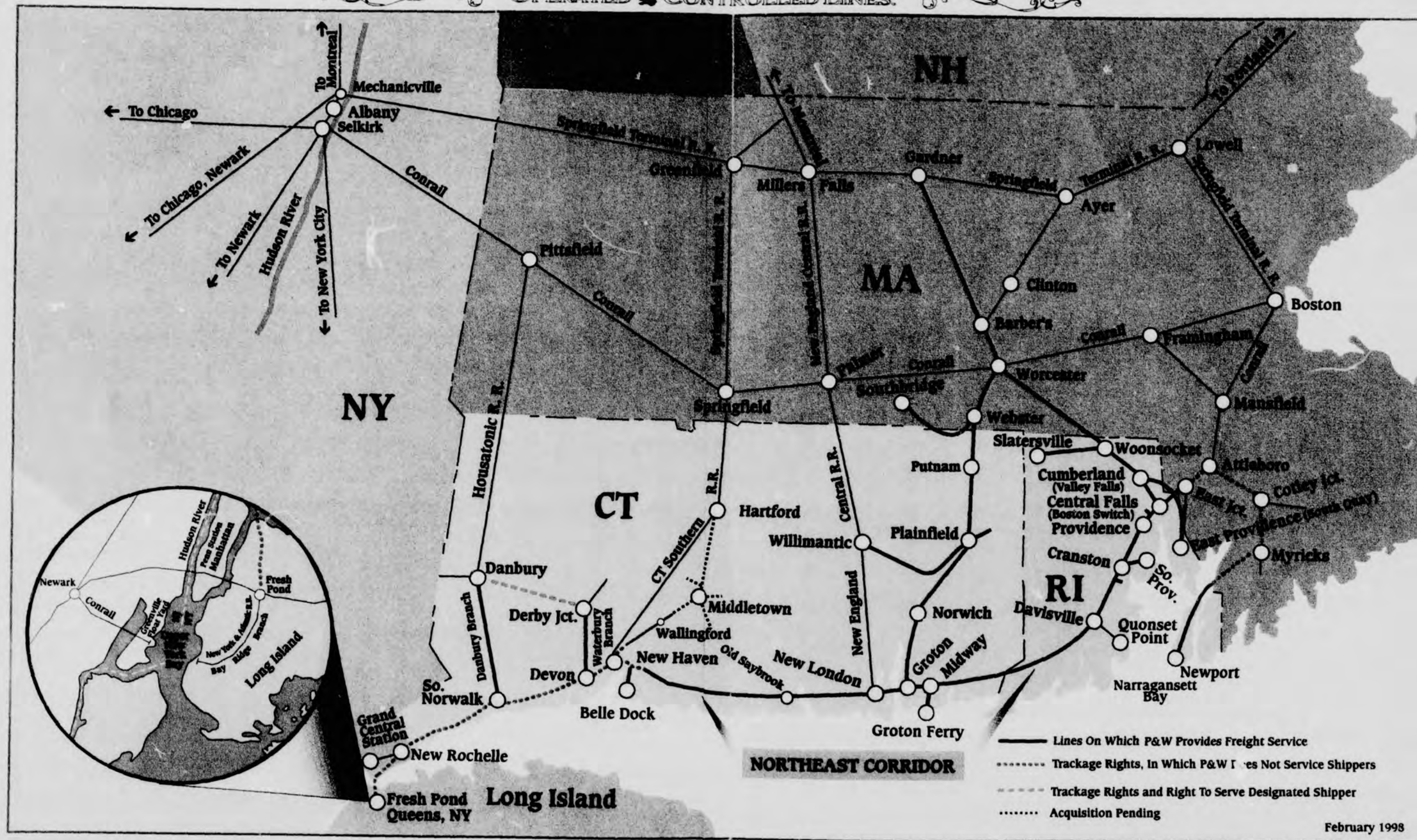
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Enclosures

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HAND DELIVERY

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RE: STB Finance Docket No. 33388, 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

Dear Secretary Williams:

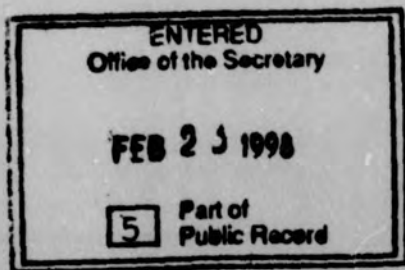
Enclosed for filing please find the original and 25 copies of the Brief of Indiana Southern Railroad, Inc. Also enclosed is a 3.5 inch diskette containing the filing in WordPerfect 5.2.

Please time and date stamp the extra copy of the filing and return it with our messenger.

If you have any questions, please contact me.

Respectfully,

Karl Morell
Attorney for:
INDIANA SOUTHERN RAILROAD, INC.



ORIGINAL

ISRR-10

**BEFORE THE
SURFACE TRANSPORTATION BOARD**

STB FINANCE DOCKET NO. 33388

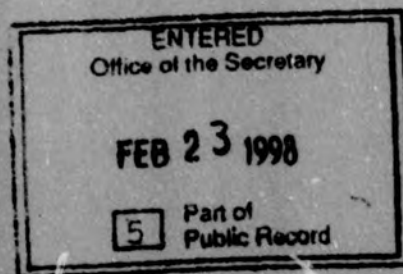


**CSX CORPORATION AND CSX TRANSPORTATION, INC.
NORFOLK SOUTHERN CORPORATION AND
NORFOLK SOUTHERN RAILWAY COMPANY
--CONTROL AND OPERATING LEASES/AGREEMENTS--
CONRAIL INC. AND CONSOLIDATED RAIL CORPORATION**

STB FINANCE DOCKET NO. 33388 (SUB-NO. 76)

**INDIANA SOUTHERN RAILROAD, INC.
--TRACKAGE RIGHTS--
CSX TRANSPORTATION, INC. AND INDIANA RAIL ROAD COMPANY**

**BRIEF OF
INDIANA SOUTHERN RAILROAD, INC.**



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Dated: February 23, 1998

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BEFORE THE
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STB FINANCE DOCKET NO. 33388

CSX CORPORATION AND CSX TRANSPORTATION, INC.
NORFOLK SOUTHERN CORPORATION AND
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BRIEF OF
INDIANA SOUTHERN RAILROAD, INC.

Indiana Southern Railroad, Inc. ("ISRR"), pursuant to Decision No. 12 in these proceedings and the Surface Transportation Board's ("STB" or "Board") Railroad Consolidation Procedures at 49 C.F.R. Part 1180, hereby submits its brief in support of ISRR's Responsive Application. ISRR respectfully submits that the Railroad Control Application ("Control Application") filed by CSX Corporation ("CSXC"), CSX Transportation, Inc. ("CSXT"), Norfolk Southern Corporation ("NSC"), Norfolk Southern Railway Company ("NSR"), Conrail Inc. ("CRR"), and Consolidated Rail Corporation ("CRC")¹ (collectively referred to as the "Primary Applicants") should be denied unless the conditions requested by ISRR are approved.

¹ CSXC and CSXT are referred to collectively as CSX. NSC and NSR are referred to collectively as NS. CRR and CRC are referred to collectively as Conrail. In their Control Application filed on June 23, 1997, Primary Applicants

SUMMARY OF ARGUMENTS

Indianapolis and the surrounding area presents the Board with the most serious and pervasive competitive issues in these proceedings. Nearly 88 percent of all the 2-to-1 shippers identified by Primary Applicants are located in the Indianapolis area. Indianapolis and the surrounding area will lose all meaningful rail competition and are vastly more susceptible to rail rate increases and service deterioration than any other community affected by the Primary Transaction. In their private agreement to carve up CRC, Primary Applicants have relegated the Indianapolis area to the complete and exclusive domain of CSXT.

Indianapolis Power & Light ("IPL") operates two coal burning facilities in Indianapolis that currently enjoy the benefits of head-to-head rail competition. Post-Transaction both of these plants will become captive to CSXT. The Perry K Plant is located on the CRC line in Indianapolis and has been designed as a 2-to-1 destination by Primary Applicants. IPL currently has at least five routing options for coal deliveries to Perry K. ISRR and a CSXT subsidiary, the Indiana Rail Road Company ("INRD"), vigorously compete for coal movements to that plant via a CRC switch. IPL is also able to deliver coal to Perry K by truck from the nearby E.W. Stout Plant and a terminal on CSXT's subsidiary.

Post-Transaction, all options for moving coal to Perry K will be controlled by CSXT. CSXT, which will replace CRC as the switch carrier, will economically or operationally disadvantage coal movements over the ISRR in order to favor the routings over its subsidiary. The short truck movements to Perry K will no longer serve as a competitive constraint on CSXT,

seek Board approval for: (1) the acquisition by CSX and NS of control of Conrail; and (2) the division of the assets of Conrail by and between CSX and NS (hereinafter referred to as the "Primary Transaction").

as they do today on CRC, because CSXT will control the prior rail movements to both transloading facilities.

IPL's second facility, the Stout Power Plant, is located on CSXT's subsidiary a short distance from CRC's Indianapolis line. IPL currently has at least six routing options for coal movements to Stout. Again, ISRR and CSXT's subsidiary have vigorously competed for coal traffic to that plant. ISRR has delivered coal to Stout via a CRC and INRD switch in Indianapolis. CRC has the potential to serve Stout via an INRD switch or directly via a build-in from its nearby line. Post-Transaction, all options for moving coal to the Stout Plant will be controlled by CSXT. CSXT will competitively disadvantage the ISRR routings in order to favor its subsidiary. Once CSXT replaces CRC, all CRC routings will be taken over by CSXT and the build-in option -- which now disciplines INRD rates -- will become meaningless.

NSR will not be a competitive factor for coal movements to Indianapolis. NSR will have no direct access to the nearby Indiana coal fields; its shortest direct route is almost five times longer than the INRD route. Eastern coal sources are not competitive in Indianapolis because they must move vastly greater distances than coal shipments from Indiana mines. NSR will also not gain access to ISRR and its direct coal sources, and NSR will be precluded from serving Stout via the build-in options. Also, NSR coal movements to Indianapolis would not be operationally feasible because of NSR's circuitous route to that city and the requirement that NSR interchange all traffic with CSXT in CSXT's Hawthorne Yard.

By Primary Applicants' own admission, at least 66 shippers in Indianapolis will lose competitive rail service if the Primary Transaction is approved without conditions. In the nearby community of Crawfordsville, at least seven shippers face a similar fate. There is deep and

widespread concern over the significant loss of rail competition in Indianapolis and the surrounding area. Primary Applicants' answer to these concerns -- granting NSR overhead trackage rights to Hawthorne Yard and overhead trackage rights or haulage rights to Crawfordsville -- falls woefully short of remedying the competitive harm in this area.

ISRR and other parties have demonstrated that NSR's ability to compete in the Indianapolis area is illusory and that the private arrangement between CSXT and NSR cedes this area to CSXT's exclusive dominion and control. Primary Applicants are not trading places or replicating the status quo, as they would lead the Board to believe. CSXT is largely retaining its current position in the area as well as assuming the position of CRC. CSXT will retain all of its assets and acquire all of CRC assets in the Indianapolis area. CSXT will retain direct access to its current customers and acquire the exclusive right to serve directly all but one of CRC's customers. NSR, on the other hand, will own no physical assets in the area, will have direct access to only one shipper and will be forced to operate over highly circuitous routes. Faced with numerous operating and access disadvantages, NSR will most likely be discouraged from providing any meaningful service to the Indianapolis area. Additionally, the CSXT-NSR arrangement provides CSXT no incentive to reduce costs or improve efficiencies in the Indianapolis area since NSR cannot provide service competition and is dependent on CSXT service to reach all but one customer.

Unlike the contrived CSXT-NSR solution, the trackage rights ISRR seeks are designed to provide meaningful rail competition and eliminate the competitive harm the Primary Transaction would otherwise produce in the Indianapolis area. By gaining direct access to IPL's two plants, ISRR would be able to preserve the two carrier competition those plants currently enjoy. The

requested conditions would also enable ISRR to offer the shipping public in the Indianapolis area a competitive alternative to CSXT, which will be lost when CRC exits this market.

The Primary Transaction will also produce harm to essential services on the ISRR rail system. ISRR will lose over \$1.5 million in annual revenues as a result of traffic diversions to CSXT and its subsidiary. The loss of this traffic will render the northern most section of ISRR's rail line unprofitable and force ISRR to abandon that segment. At least seven of ISRR's customers would be adversely affected by the abandonment through the loss of essential rail service. If ISRR's conditions are granted, ISRR would be able to continue serving its customers, as well as provide meaningful rail competition to the Indianapolis area.

BACKGROUND

ISRR is a Class III rail carrier operating over approximately 176 miles of track between Indianapolis and Evansville, Indiana. ISRR currently connects with CRC at Indianapolis; NSR and the Algiers, Winslow & Western Railway (an NSR subsidiary) at Oakland City, Indiana; Indiana Rail Road Company ("INRD") at Switz City, Indiana; the CP Rail System ("CP Rail") at Bee Hunter, Indiana; and CSXT at Evansville, Indiana. Neumann V.S. at 2, ISRR-4.

ISRR began operations in April 1992, and has been able to consistently increase its traffic base. ISRR currently has 36 employees and operates a fleet of 14 locomotives. Its headquarters are located in Petersburg, Indiana, where it maintains a locomotive and car repair shop, a rail yard and service tracks. ISRR also maintains a facility at Worthington, Indiana, for its transportation employees and one at Spencer, Indiana, for its maintenance of way employees. The major commodity handled by ISRR is coal, which comprises 95 percent of its total carloads.

ISRR's gross revenues in 1996 were approximately \$9 million and its major customers currently are IPL, Black Beauty Coal Company, Ferro and Whirlpool. *Id.* at 2-3.

ISRR has worked hard at reducing its costs to a bare minimum in order to provide economical service to its customers. ISRR operates with limited overhead. Its employees are cross-trained to perform multiple duties thereby eliminating the need for extra employees to handle separate functions. ISRR has reached the point where it cannot afford to further reduce its costs without adversely impacting the quality of service and the maintenance of its physical plant. *Id.* at 3.

TRACKAGE RIGHTS REQUESTED BY ISRR

In its Responsive Application, ISRR requested the Board to condition the approval of the Primary Transaction by granting ISRR trackage rights in Indianapolis and the area surrounding Indianapolis as follows:

1. Indianapolis

Overhead trackage rights between MP 6.0 on ISRR's Petersburg Subdivision and IPL's Perry K facility in Indianapolis over the rail line currently owned by CRC and to be acquired by CSXT.

Overhead trackage rights between MP 6.0 on ISRR's Petersburg Subdivision and IPL's Stout facility located on the INRD rail line over a segment of the rail line currently owned by CRC and to be acquired by CSXT and a segment of INRD's rail line.

Local trackage rights over CRC's rail lines in Indianapolis, including the Indianapolis Belt Line, to be acquired by CSXT.²

2. Between Indianapolis and Surrounding Communities

Local trackage rights between Indianapolis and Shelbyville, Indiana, over the rail line currently owned by CRC and to be acquired by CSXT.

² ISRR seeks trackage rights over all CRC rail lines in Indianapolis needed to access the 2-to-1 shippers located in Indianapolis and the other shortlines operating to Indianapolis.

Local trackage rights between Indianapolis and Crawfordsville, Indiana, over the rail line currently owned by CRC and to be acquired by CSXT.

Local trackage rights between Indianapolis and Muncie,³ Indiana, over the rail line currently owned by CRC and to be acquired by CSXT.

GOVERNING LEGAL STANDARD

Under 49 U.S.C. § 11324 (c), the Board shall approve a transaction when it finds the transaction consistent with the public interest.⁴ In applying the statutory "public interest" standard, the Board must balance the benefits applicants and the public will derive from the transaction against the potential competitive harm. Finance Docket No. 32760, *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*, Decision No. 44 (slip op. at 98-99, served August 12, 1996) (UP/SP).⁵

In determining whether a proposed transaction involving two or more Class I railroads is consistent with the public interest, the Board is directed to consider, at a minimum, the following five factors:

- (1) the effect of the proposed transaction on the adequacy of transportation to the public;

³ On rebuttal, ISRR clarified that it is not seeking to serve local shippers in Muncie because the competitive status quo will be maintained in that community. Neumann R.V.S. at 14, ISRR-9.

⁴ The "single and essential standard of approval is that the (Board) find the (transaction) to be consistent with the public interest." *Missouri-Kansas-Texas R. Co. v. United States*, 632 F. 2d 392, 395 (5th Cir. 1980), *cert denied*, 451 U.S. 1017 (1981).

⁵ The Board's general policy statement on rail consolidations provides, in pertinent part, that:

In determining whether a transaction is in the public interest, the (Board) performs a balancing test. It weighs the potential benefits to applicants and the public against the potential harm to the public.

49 C. F. R. § 1180.1 (c).

- (2) the effect on the public interest of including, or failing to include, other rail carriers in the area involved in the proposed transaction;
- (3) the total fixed charges that result from the proposed transaction;
- (4) the interest of rail carrier employees affected by the proposed transaction; and
- (5) whether the proposed transaction would have an adverse effect on competition among rail carriers in the affected region or in the national rail system."⁶

49 U.S.C. § 11324 (b).

⁶ Subsection (5) was added by the Staggers Rail Act of 1980 (Public Law 96-448) and was amended by the ICC Termination Act of 1995 (Public Law 104-88) to require the Board to consider adverse impacts upon competition "in the national rail system". This subsection was originally enacted to statutorily obligate the Board's predecessor to analyze the loss of rail competition in relevant regional markets. As explained by the sponsor of the subsection:

I am offering an amendment...to specifically direct the Interstate Commerce Commission to consider the question of rail competition whenever making a determination of a railroad merger transaction.

The escalation of rail mergers now taking place in the industry is causing concern among our Nation's farmers and ranchers as well as other shippers. The Interstate Commerce Commission is facing decision on several mergers that would have the effect of eliminating or nearly eliminating rail competition within entire sections of the country. I think it is important, therefore, that the ICC consider the question of competition as a regular part of the process of evaluating whether to allow mergers.

126 Cong. Rec. H8604 (September 9, 1980); Remarks of Congressman Panetta.

The first and last of these factors are relevant to ISRR's Responsive Application.

Section 11324 (b)(1) requires the Board to examine the public benefits that will result from the transaction. The Board has defined public benefits "as efficiency gains such as cost reductions, cost savings, and service improvements...(that) in varying degrees...are passed on to most shippers as reduced rates and/or improved services." *UP/SP* at 99. Benefits that accrue to the applicants as a result of increased market power, however, "are exclusively private benefits that detract from any public benefits associated with a control transaction." *Id.*

Section 11324 (b)(5) requires the Board to assess the effects of the transaction on competition. The Staggers Act increased the need for more careful scrutiny of anticompetitive effects of merger transactions. As the Board's predecessor noted:

The new (Rail Transportation Policy) favoring increased reliance on competition to regulate activities will govern the environment in which the new system will operate. The ability of the railroads to take various actions free of regulatory restraints will make it easier to exert or abuse market power gained as a result of consolidation. For these reasons we must take even greater care to identify harmful competitive effects and to mitigate those effects where possible.

Union Pacific - Control - Missouri Pacific; Western Pacific, 366 I.C.C. 459, 502 (1982) ("UP/MP/WP").

The Board considers two types of potential harm that may result from a proposed consolidation transaction: reduction of competition and harm to essential services. 49 C.F.R. § 1180.1 (c) (2).

The Board is concerned not only with the possible "elimination" of competition by consolidations, but also with any significant "lessening" or "reduction" in competition. *Railroad Consolidation Procedures*, 363 I.C.C. 784, 786-87 (1981). "Competitive harm results from a

merger to the extent the merging parties gain sufficient market power to raise rates or reduce service (or both), and to do so profitably, relative to premerger levels." *UP/SP* at 100.

Whenever possible, the Board attempts to ameliorate competitive harms with conditions. *Id.*

In determining whether a proposed transaction will result in competitive harm, the Board looks to the affected market. The affected market has two dimensions: product and geographic.

Rio Grand Industries, et al. - Control - SPT Co., et al., 4 I. C. C. 2d 834, 885 (1988)

("RGI/SPT"). The product sold by railroads is the transportation of freight. *Id.* at 886; *Rio Grande Ind., Inc. -- Pur. & Track. -- Soo Line R. Co.*, 6 I. C. C. 2d 854, 878 (1990)

("RGI/SOO"). The Board generally considers alternative rail service and, where relevant, intermodal options. *RGI/SOO* at 886-87; *Union Pacific Corp. et al. - Cont. - MO-KS-TX CO. et al.*, 4 I. C. C. 2d 409, 433-35 (1988) ("*UP/MKT*"). In past merger cases, the Board and its predecessor have not applied a fixed definition of the relevant market. Instead, they have examined the specific circumstances in each case to determine if the relevant market should be confined to rail transportation or enlarged to include other transportation modes. See Finance Docket No. 32133, *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*, Decision No. 25 (slip op. 57, served March 7, 1995); *UP/MKT* at 433-34..

The area in which providers of a particular product operate is the relevant geographic market. The area may be as small as a city or as large as the entire country. *RGI/SPT* at 887. The Board's predecessor noted that "the distinctions between product and geographic markets are not as clear in transportation as they are in other industries, for carriers, in particular railroads,

effectively sell their geography." *UP/MP/WP* at 505, n 28. Accordingly, the determinations of the relevant product market and the relevant geographic market in a particular case will necessarily be interrelated. The Board's predecessor analyzed traffic flows between city pairs, as well as traffic flows in rail corridors, and at specific points in the area in which the merging rail carriers operate. *UP/MKT* at 437.

The Board also considers whether a proposed transaction affects essential services. The Board's focus is on the preservation of essential services and not on the survival of any particular carrier. 49 C.F.R. § 1180.1 (c) (2) (ii). *See also, UP/MKT* at 431. The Board uses a two-step analysis in determining whether a proposed transaction will harm essential services. *UP/MP/WP* at 546. First, the Board considers whether any affected carrier faces financial losses on a particular line that would reduce its operational viability. *See Guilford Transportation - Control - B&M, et al.*, 5 I. C. C. 2d 202, 215 (1988). Second, the Board considers whether the rail line suffering the losses provides essential service. *UP/MP/WP* at 546. A service is considered essential "if there is a sufficient public need for the service and adequate alternative transportation is not available." 49 C.F.R. § 1180.1 (c) (2) (ii).

The Board has broad authority to impose conditions on its approval of a consolidation transaction in order to ensure that the public interest standard is met. 49 U.S.C. § 11324 (c); *UP/MP/WP* at 562. In determining whether conditions are warranted, the Board's "overriding concern is the public interest." *Id.* The Board can impose conditions to remedy new problems created by the transaction or preexisting problems that will be exacerbated by the transaction.

Public interest conditions will be imposed to ameliorate anticompetitive consequences of a proposed transaction if the conditions: (i) are operationally feasible; (ii) ameliorate or eliminate

the harm threatened by the transaction; and (iii) are of greater benefit to the public than they are detrimental to the transaction. *UP/MP/WP* at 564.

A condition to protect a carrier when the transaction affects essential service on the carrier's rail lines is imposed upon a showing that the condition: (i) is related to the impact of the consolidation; (ii) is designed to enable shippers to receive adequate service; (iii) would not pose unreasonable operating or other problems for the consolidated carrier; and (iv) would not frustrate the ability of the consolidated carrier to obtain the anticipated public benefits. 49 C.F.R. § 1180.1 (d) (1).

THE TRACKAGE RIGHTS REQUESTED BY ISRR SHOULD BE GRANTED

Approval of the Primary Transaction, without appropriate conditions, will significantly reduce competition for rail shippers in Indianapolis and the surrounding area and will cause a loss of essential services on the ISRR rail system. The conditions requested by ISRR are uniquely designed to ameliorate both of these competitive harms. If the conditions are granted, ISRR will be able to preserve competitive rail service for shippers in Indianapolis and the surrounding area and maintain service to its rail dependent on-line customers. As demonstrated below, the trackage rights ISRR seeks fully meet the Board's criteria for imposing conditions.

RAIL COMPETITION IN INDIANAPOLIS AND THE SURROUNDING AREA WILL BE SIGNIFICANTLY REDUCED AS A RESULT OF THE PRIMARY TRANSACTION

According to Primary Applicants' own testimony, Indianapolis is by far the largest 2-to-1 area created by the Primary Transaction. *See CSX/NS-18* at 548. They concede that there are at

least 66 shippers on CRC lines in Indianapolis that currently have two carrier rail service through reciprocal switching. *See CSX/NS-19* at 147. The nearby community of Crawfordsville, according to Primary Applicants, is the second largest 2-to-1 area, with seven shippers facing a loss of competitive rail service. *Id.* at 148. In addition, CRC currently serves as a neutral gateway carrier to shippers on the Indianapolis to Shelbyville, Indianapolis to Crawfordsville, and Indianapolis to Muncie rail lines for traffic moving to nearby CSXT and NSR junctions. The proposed solution -- granting NSR overhead trackage rights to Hawthorne Yard in Indianapolis and overhead trackage or haulage rights to Crawfordsville -- falls woefully short of remedying the anticompetitive effects of the Primary Transaction in Indianapolis and the surrounding area. The conditions requested by ISRR, on the other hand, would enable ISRR to compete directly with CSXT from a rate and service standpoint and to provide the affected shippers a meaningful competitive alternative.

Perry K Plant

IPL's Perry K Plant is located on a CRC line in Indianapolis. IPL currently has five routing options for coal deliveries to the Perry K Plant: (1) CRC direct; (2) ISRR via CRC switch at Indianapolis; (3) INRD via CRC switch at Indianapolis; (4) INRD to the E. W. Stout Plant and truck to Perry K; and (5) INRD to its switching yard in Indianapolis and truck to Perry K. ISRR has transported coal to Perry K via a CRC switch since it began operations in 1992. ISRR's primary competitor for coal movements to Perry K has been the INRD. The source of coal currently moving to Perry K is the Triad Mine located on the INRD at Switz City, Indiana. ISRR has trackage rights over the INRD to serve that mine for coal movements to all IPL plants other than Stout. Consequently, INRD can serve Perry K via a CRC switch from the Triad Mine,

as well as from the various other mines INRD serves directly in Indiana. Neumann R.V.S. at 2-3, ISRR-9. In addition, IPL has shipped coal over the INRD to IPL's Stout Plant and INRD's Senate Avenue Terminal in Indianapolis for movements to Perry K by truck. CSX/NS-177 at 195-96. *See also*, Crowley R.V.S. at 3 and 9, ISRR-9.

Post-Transaction, the Perry K Plant will become captive to CSXT and its 89 percent owned subsidiary, the INRD. Once CRC exits the Indianapolis market, the options of CRC handling coal direct or as a switch carrier for ISRR or INRD will be lost. While ISRR currently has a slight operational advantage over INRD because it interchanges the coal movements with CRC within one to two miles of the Perry K facility, CRC is largely indifferent and neutral in switching the traffic to Perry K from either ISRR or INRD. CSXT, which will replace CRC, will have the means and a strong economic motive to favor its subsidiary and economically or operationally disadvantage coal movements over the ISRR. The short truck movements to Perry K from Stout or the INRD terminal will not serve as a competitive constraint on CSXT, as they do on CRC today, since the prior rail movements will be controlled by CSXT's subsidiary. Accordingly, post-Transaction, all options of moving coal to Perry K will be controlled by CSXT.

Primary Applicants suggest that Perry K will benefit from the Primary Transaction by gaining access to NSR via a CSXT switch through Hawthorne Yard. CSX/NS-176 at 55. What they conveniently fail to note, however, is that NSR has no direct access to nearby coal sources from which NSR could economically transport coal to Perry K. NSR will not gain access to ISRR in Indianapolis and the only NSR route from nearby Indiana coal mines is highly circuitous. In order to transport Indiana coal to Perry K, NSR would be forced to utilize a 491-

mile route via Louisville and Danville, Kentucky, Cincinnati, Ohio, and Muncie, Indiana, which is nearly five times longer than INRD's direct route. Because of the significantly further distances and NSR's highly circuitous route to Indianapolis, Eastern coal would not be competitive with the nearby Indiana coal. Neumann R.V.S. at 3-4, ISRR-9. Primary Applicants' own witness has confirmed NSR's inability to be competitive for coal movements to Indianapolis by demonstrating that IPL is economically committed to using Indiana coal. CSX/NS-177 Vol. 2B at 514-19. Even if NSR had access to economical sources of coal -- which it does not -- NSR would be restricted to interchanging the traffic with CSXT at Hawthorne Yard. The movement of unit coal trains through Hawthorne Yard is operationally inefficient and would further disadvantage movements to Perry K via the NSR.

CSXT witnesses attempt to downplay the loss of rail competition at Perry K by erroneously alleging that the plant has been partially converted to natural gas. CSXT/NS-177 Vol. 2A at 201 and Vol. 2B 510. According to Mr. Neumann, however, the conversion has been delayed and may never occur. Even if the conversion does occur, Perry K would still need to receive about one-half of its current coal volumes and would still be dependent on rail to meet its coal transportation needs. Neumann R.V.S. at 11-12, ISRR-9.

Primary Applicants have designated Perry K as a 2-to-1 facility. CSX/NS-37 at 12; CSX/NS-51 at 8; and CSX/NS-178 Vol. 3B at 638-39. As demonstrated by ISRR and others, Primary Applicants' contrived solution of preserving competition at that plant is not economically feasible and operationally efficient. Primary Applicants alternative argument -- that there will be no loss of competition at Perry K because CSXT will simply replace CRC (CSX/NS-177 Vol. 2A at 635)-- is equally unavailing. As already explained, ISRR coal

movements to Perry K now compete with INRD routings, and CSXT, which controls INRD, will have the means and the motive to disadvantage ISRR routings. Indeed, CSXT Witness Hoback, the President of INRD, admitted that INRD competes with ISRR for coal movements to Perry K. CSX/NS-177 Vol. 2A at 198. Accordingly, the Primary Transaction will significantly reduce competition at Perry K and not, as Primary Applicants allege, maintain the status quo or improve competition.

Stout Plant

IPL's second power plant in Indianapolis is located on the INRD approximately three miles from CRC's Indianapolis Belt Running Track. IPL currently has six routing options for coal shipments to the Stout Plant: (1) INRD direct; (2) CP Rail-Linton-INRD; (3) ISRR-Switz City-INRD; (4) ISRR-Indianapolis-CRC-INRD; (5) CRC-INRD; and (6) CRC direct or ISRR-CRC via a build-in to the Stout Plant. INRD is able to serve the Stout Plant direct from several Indiana coal mines and in interline movements with CP Rail from the Farmersburg Mine. ISRR has provided service to Stout via the INRD at Switz City and via a CRC and INRD switch at Indianapolis. CRC has the potential to serve Stout via an INRD switch or directly via a build-in from its nearby Belt Line. Neumann R.V.S. at 5, ISRR-9.

Post-Transaction, the Stout Plant, like the Perry K Plant, will become captive to CSXT and its subsidiary the INRD. CSXT will have the means and the motive to competitively disadvantage ISRR routings via Indianapolis. Once ISRR's service via Indianapolis is no longer competitive, INRD will have no incentive to jointly market ISRR-INRD movements via Switz City. ISRR, therefore, will be foreclosed from competing for Stout traffic. Once CRC exits the Indianapolis market, the option of CRC linehauling coal to Stout via an INRD switch will be

lost. In addition, IPL is currently able to discipline INRD rail rates to Stout by threatening the use of the build-out option, which, if constructed, would provide CRC or ISRR-CRC routings direct access to Stout. The build-in/build-out option, however, will also become meaningless with the replacement of CRC by CSXT on the Belt Line.⁷ It would make no sense whatsoever to build a connecting line to the parent of the company to which you have just become captive. Accordingly, post-Transaction, all options of moving coal to the Stout Plant will be controlled by CSXT.

For reasons previously discussed, NSR will not be a competitive factor for coal movements to Indianapolis. NSR's direct route from the nearby Indiana coal fields is over a highly-circuitous route, the eastern mines are located at too great a distance to be competitive, NSR will not gain access to ISRR, and NSR's overhead trackage rights on the Belt Line will specifically preclude NSR from serving Stout via a build-in. Moreover, NSR will be operationally constrained by the requirement that it only interchange traffic in Indianapolis with CSXT at the Hawthorne Yard.

On rebuttal, CSXT witnesses attempt to deflect the demonstrated loss of competition at the Stout Plant with illogical and transparently erroneous contentions. First, CSXT Witness Orrison acknowledges that ISRR is currently able to serve Stout via an interchange with CRC. CSX/NS-177 Vol. 2A at 655. He goes on to suggest, however, that there is no "operating" reason why ISRR could not continue hauling coal to Stout because CSXT will simply assume

⁷ The Board and its predecessor have consistently acknowledged that a build-out option constitutes potential competition that effectively constrains rail rates. See Finance Docket No. 32549, *Burlington Northern Inc. and Burlington Northern Railroad Company -- Control and Merger -- Santa Fe Pacific Corporation and The Atchison, Topeka and Santa Fe Railway Company*, Decision No. 38 (slip op. 67-8, served August 23, 1995) ("the merger will reduce OG&E's competitive options at Red Rock by negating its ability to 'build out' to a neutral carrier"); *UP/SP* slip op. 185.

CRC's role for ISRR coal movements to Stout. Mr. Orrison's contention, however, conveniently ignores the fact that ISRR's competitor, the INRD, is controlled by CSXT. He seems to suggest, as CSXT has done on other occasions in these proceedings, that CSXT will compete with its subsidiary, a notion that is counterintuitive and has been rejected by other CSXT witnesses.⁸ See CSX/NS-177 Vol. 2A at 269-70 ("In most instances, economists consider complete ownership sufficient to provide the incentive to control the types of decisions, such as pricing, service quality, and interchanges, that control vertical rail relationships.").

Second, CSXT Witness Vaninetti alleges that ISRR is not a competitive factor for coal movements to Stout because last year ISRR lost the traffic to a two-line haul via CP Rail-INRD. CSX/NS-177 Vol. 2B at 513. Mr. Vaninetti's notion of competition is nonsensical and contrary to his testimony in this proceeding and in *UP/SP*.⁹ Mr. Vaninetti is at a loss to explain why ISRR handled traffic to Stout in prior years via CRC if its routing is not competitive. As explained by Mr. Neumann, the fact that ISRR lost traffic to INRD last year "does not mean that ISRR is not a competitor for the traffic; it simply means that ISRR was outcompeted for the traffic originating on the CP Rail. *** ISRR can compete for spot purchases of coal to Stout today and, if IPL decides to source its Stout coal from a different origin in the future, ISRR would be able to compete for the movements." Neumann R.V.S. at 7, ISRR-9. In reality, ISRR's

⁸On Rebuttal, CSXT offers to temporarily preserve competition at Stout by extending the contract governing ISRR's movements to Stout. CSX/NS-176 at 365. As explained in ISRR's Rebuttal, CSXT's offer is virtually meaningless and, at best, would only delay the anticompetitive consequences of the Primary Transaction in Indianapolis.

⁹In these proceedings, Mr. Vaninetti claims that trucks are competitive for coal movements to Stout, even though he readily admits that he has no knowledge of any coal ever being trucked to Stout. More importantly, Mr. Vaninetti's testimony in *UP/SP* is directly at odds with his testimony here. In *UP/SP*, he criticized UP Witness Sharp by stating:

Mr. Sharp does not differentiate between competition and successful competition, since his assessment that "competition between Union Pacific origins and Southern Pacific Origins was quite modest (or) rare" is apparently based on which carrier was successful in gaining the business -- not that the carriers competed for the business.

See Crowley R.V.S. at 13, ISRR-9.

routings to Stout via CRC are currently competitive with alternative routings over the INRD, but will be rendered noncompetitive with the replacement of CRC by CSXT in Indianapolis.¹⁰

Third, CSXT Witnesses Hoback and Vaninetti would have the Board accept the loss of rail competition at Stout on the theory that truck competition constrains rail rates for coal movements to that plant. Their unsubstantiated allegations are, however, soundly refuted by Messrs. Neumann, Weaver and Crowley.

Mr. Neumann concedes that it is theoretically possible to truck some coal to Stout. In his view, however, it would be neither economical nor politically practicable to truck large volumes of coal to Stout given the distances involved and the fact that Stout is located in a major metropolitan area. Mr. Neumann points out that, in his six years at ISRR, IPL never raised the threat of truck competition for coal movements to Stout and that ISRR always considered alternative rail routings as its sole competition for Stout traffic. Neumann R.V.S. at 10-11, ISRR-9.

Mr. Weaver explains that, in negotiating the current INRD contract for the transportation of coal to Stout, IPL used the ISRR-CRC competitive rail routings as leverage and not, as Messrs. Hoback and Vaninetti allege, truck competition. Mr. Weaver compares the costs of moving coal to Stout by truck and rail and conclusively demonstrates that rail has a large rate advantage. He also points out that IPL has made a significant investment in rail cars, an

¹⁰Mr. Vaninetti, citing to a document produced by ISRR in discovery, alleges that CRC service problems in Indianapolis rendered ISRR routings to Stout noncompetitive. CSX/NS-177 Vol. 2B at 513. As explained by Mr. Neumann, however, the document addressed service problems ISRR was experiencing in 1994 for coal movements to Perry K, and not Stout, and that any past operational problems ISRR may have experienced with CRC will pale in comparison to the ones ISRR will undoubtedly experience with CSXT in competing with CSXT's subsidiary. Neumann R.V.S. at 7-8, ISRR-9.

Citing to an internal ISRR memorandum, Mr. Vaninetti claims that ISRR previously concluded that the Primary Transaction will have no effect on ISRR. CSX/NS-177 Vol. 2B at 514. The document Mr. Vaninetti relies on, however, was prepared well before the details of the Primary Transaction were made public and addresses a topic different than that alleged by Mr. Vaninetti. See Neuman R.V.S. at 8-9, ISRR-9.

investment that would have been imprudent if trucks are competitive with rail. Mr. Weaver considers CSXT's new-found theory of truck competition as merely an attempt by CSXT to divert the Board's attention from the real issue -- which is the loss of rail competition at Stout. Weaver R.V.S. at 8-12, ISRR-9. Mr. Weaver also refutes CSXT's contention that CRC is a limited player in the Indiana coal industry by demonstrating that CRC's role remains integral to the competitive balance IPL currently enjoys at the Stout and Perry K Plants. He goes on to explain that ISRR is a major factor in the Indiana coal market and CRC's current neutrality between ISRR- and INRD- originated coal movements provides IPL rail competition in Indianapolis. *Id.* at 11-14.

Mr. Crowley refutes CSXT's truck-to-rail comparison by demonstrating that CSXT's witnesses have no knowledge of actual truck rates to Stout. He also disputes Mr. Vaninetti's contention that trucks have an apparent \$1 per ton advantage over rail because of the differential in loading and unloading costs. Based on Mr. Crowley's experience, rail loading and unloading costs are usually lower than truck loading and unloading costs. In any event, based on the unloading facilities that currently exist at Stout, Mr. Crowley demonstrates that rail has a cost advantage over trucks. Crowley R.V.S. at 14-17, ISRR-9.

Moreover, the Board recently discounted evidence of alleged truck competition for distances comparable to those to the Stout Plant. STB No. 41185, *Arizona Public Service Company and PacifiCorp v. The Atchison, Topeka and Santa Fe Railway Company*, served July 29, 1997. The Board concluded that the suggested truck movements would present significant environmental and operational problems. The Board further determined that, even if these

problems could be surmounted, truck rates would not "place an effective competitive constraint on Santa Fe's rail rates." *Id.*, slip op. at 6-7.

Fourth, CSXT Witness Vaninetti speculates that IPL could discipline rail rates to Stout by generating additional power at IPL's Petersburg or Pritchard Plants.¹¹ CSX/NS-177 at 507-9. Mr. Weaver explains that, because Petersburg is IPL's lowest-cost Plant, IPL always utilizes power from Petersburg first when it is available. IPL has programmed its computers to sequentially generate power at its lowest cost plants not to discipline rail rates but to meet IPL's obligations to its rate payers. Weaver R.V.S. at 15-17, ISRR-9. *See also* Crowley R.V.S. at 17-18, ISRR-9. Accordingly, IPL is already doing precisely what Mr. Vaninetti suggests.

Fifth, CSXT Witnesses Kuhn and Vaninetti criticize IPL's cost estimates of the build-out/build-in option. CSX/NS-177, Vol. 2A at 306-11; CSX/NS-177, Vol. 2B at 511. Mr. Kuhn claims that IPL omitted some expenses in its build-out analysis. Even if the Board were to accept all of Mr. Kuhn's alleged additional costs, the build-out option would still be economically feasible, a fact which neither CSXT witness disputes. *See* Weaver R.V.S. at 19-21, ISRR-9; Crowley R.V.S. at 28-9, ISRR-9. Interestingly, CSXT's own witnesses confirm the economic feasibility of the build-out.

Indianapolis and the Surrounding Area

Primary Applicants readily admit that shippers in Indianapolis and the surrounding area will be competitively harmed if the Primary Transaction is approved without conditions. Aside from IPL's two plants, at least 65 other shippers in Indianapolis would suffer a loss of rail

¹¹ Mr. Vaninetti's suggestion that other power sources could discipline rail rates to Perry K (CSX/NS-177 at 503) is nonsense. Perry K is a steam generating plant and not, as Mr. Vaninetti assumes, a power plant. *See* Neumann R.V.S. at 12, ISRR-9.

competition. *See* CSX/NS-19 at 147. In the nearby community of Crawfordsville, at least seven shippers face the same loss of competition. *Id.* at 148. Similarly, shippers located on the rail lines extending from Indianapolis to the nearby communities of Shelbyville, Crawfordsville and Muncie will lose CRC's neutral service to the CSXT and NSR junctions. By Primary Applicants' own admission, at least 73 of the 83 designated 2-to-1 shippers, or 88 percent, are located in the Indianapolis area. Consequently, Indianapolis and the surrounding area are vastly more susceptible to rail rate increases and inefficient routings than any other community affected by the Primary Transaction and, therefore, deserve the Board's closest attention.

Primary Applicants blithely respond to the competitive concerns in the Indianapolis area by contending that the Primary Transaction simply replicates the existing competitive scenario. They unabashedly claim that CSXT is merely assuming the role of CRC and NSR is assuming CSXT's current position. *See* CSX/NS-176 at 52. If Primary Applicants had truly intended to maintain the competitive status quo in the Indianapolis area, the solution would have been simple: NSR would simply have stepped into the shoes of CRC in this area. This solution would insure that competition to the two IPL plants is preserved and no 2-to-1 shippers are created in Indianapolis and Crawfordsville. Primary Applicants' failure to adopt this simple solution is powerful evidence of their intention to cede all meaningful rail operations in the Indianapolis area to CSXT.

NSR's ability to compete in the Indianapolis area is illusory. NSR is not assuming CSXT's current position, as Primary Applicants allege. Rather, CSXT is largely retaining its current position as well as assuming the position of CRC. NSR is merely being granted overhead trackage rights without the right to connect with any carrier other than CSXT and without the

right to directly serve any shipper other than one facility in Indianapolis. Both CRC and CSXT currently have a substantial physical presence in Indianapolis. CSXT owns its own rail lines into Indianapolis, has employees stationed in Indianapolis, owns its own Indianapolis rail yard and directly serves certain Indianapolis shippers. Once the Primary Transaction is consummated, CSXT will acquire all of CRC's rail lines, presumably hire all or most of CRC's employees, acquire all of CRC's yard facilities and gain direct access to all CRC customers. NSR, on the other hand, apparently will own no physical assets in Indianapolis or Crawfordsville.¹² It will own no rail lines or yard facilities, have direct access to only one customer and will apparently have no employees stationed in either community. NSR is simply being given the right to pass through these two communities when picking up whatever freight may be available at Hawthorne Yard.

In addition to having no physical presence in these communities and having direct access to only one shipper, NSR would be forced to operate over a highly circuitous route. For example, CSXT currently competes for traffic moving between the Indianapolis area and Chicago via Crawfordsville. Post-Transaction CSXT will continue to have that same direct route. NSR, however, will be forced to operate from Muncie to Hawthorne Yard to await CSXT's switch, then backtrack to Muncie and proceed north and west to Chicago. CSXT will have similar routing advantages for traffic moving between the Indianapolis area and the southeast, the midwest and the southwest. NSR's ability to serve Crawfordsville is even more circumscribed. It appears that NSR will have little, if any, traffic moving over the rail line between Indianapolis and Lafayette. Also, Crawfordsville traffic moving to or from Chicago, the

¹² NSR Chairman of the Board, President and Chief Executive Officer, Mr. David R. Goode, testified that he is unaware of any planned NSR investment for Indianapolis. See I&PL-3, Exhibit 5 (Goode Dep'n Tr. at 45.)

northeast and southeast would be routed through Muncie. Consequently, in order to serve Crawfordsville, NSR would have to make an almost 200-mile round trip from Muncie simply to bring the traffic onto the NSR system. NSR's ability economically to serve that community is highly suspect.

Faced with these numerous disadvantages, NSR will most likely be discouraged from providing any meaningful service to the Indianapolis area. CSXT, therefore, will be able to significantly raise its rates to the point where NSR's disadvantaged service becomes competitive. In addition, NSR must rely on CSXT service to reach all but one shipper in the Indianapolis area. CSXT, therefore, has no incentive to reduce costs or improve its efficiencies in this area because NSR cannot provide service competition.

CSXT will clearly have a strangle hold on Indianapolis and the surrounding area. NSR will not be able to provide any meaningful competition to CSXT, given NSR's lack of facilities and shipper access and the inefficient and circuitous NSR routings in this area. NSR's inability effectively to compete in the Indianapolis market is largely confirmed by Primary Applicants' own filings to date in these proceedings. NSR's operating plan contains a mere 10-line discussion of NSR's proposed operations in Indianapolis and simply states that NSR will receive overhead trackage rights to serve the 2-to-1 shippers via a CSXT switch in Hawthorne Yard. CSX/NS-20 at 231. One searches NSR's filings in vain for any indication of NSR's intentions or ability to provide meaningful competition in the Indianapolis area. There is no evidence of how NSR intends to serve shippers, the routes it would use for particular traffic patterns, the volume and type of traffic it expects to generate, and the physical presence it will have in these

communities, much less any assurances that its limited access and circuitous routings will not impede NSR's ability effectively to compete.

CSXT and NSR apparently have agreed among themselves, for their own private reasons and without regard to the public interest, that there shall be no effective rail competition in the Indianapolis area. The Board's predecessor rejected such contrived solutions where the applicants select among themselves the remedy to a competitive problem. *Santa Fe Southern Pacific Corp. - Control - SPT Co.*, 2 I.C.C.2d 709, 815-17 (1986). In so doing, the ICC noted that "applicants might be inclined to propose conditions that would create the least effective competition....(and that) applicants might...find it worthwhile to offer a proposal that addresses some but not all of the anticompetitive problems, in the hope that the (ICC) would be satisfied." *Id.* at 816. *See also, Santa Fe Southern Pacific Corp - Control - SPT Co.*, 3 I.C.C.2d 926, 935 (1987) ("We are disinclined to risk the possibility of collusion and market splitting that might result from such an artificial, settlement induced rationalization of the western rail system.").

The loss of meaningful rail competition in the Indianapolis area is further confirmed by other parties to these proceedings. For example, the United States Department of Agriculture ("USDA") points out that the greater Indianapolis region, "located in the heart of the Eastern Cornbelt, is one of the Nation's largest and most dynamic metropolitan areas." Comments of USDA, dated December 15, 1997 at 3. USDA supports ISRR's Responsive Application because it is concerned that "the overhead trackage rights (NSR) will receive may not enable (NSR) to provide effective competition in this market." *Id.* The United States Department of Justice ("DOJ") points out that INRD and ISRR-CRC routings currently compete for coal traffic moving to the Stout Plant and that this competition will vanish when CSXT takes over the CRC

rail lines in Indianapolis. In concluding that NSR will not effectively replace the lost CRC competition, DOJ explains that:

First, (NSR) does not have (CRC's) convenient access to the nearby Indiana coal, which means its delivered costs are higher, which means (NSR) likely could not offer competitive rates on coal shipments to Stout. Second, (NSR) likely would suffer operational problems (slowdowns and the like) in using (CSXT's) congested Indianapolis switching facilities. (CRC) too must depend on a competitor for switching services, but its threat to receive a build-out (a threat that [NSR] cannot use as a lever) helps to ensure effective cooperation.

DOJ-1 at 8-9.

The City of Indianapolis ("CI") seeks the imposition of conditions to remedy the public harm posed to Indianapolis if the Primary Transaction is unconditionally approved. CI describes Indianapolis' predicament as follows:

Whatever public benefits the Proposed Transaction might yield for the rest of the northeast and the midwest, these benefits will not be realized for the City of Indianapolis.... Rather than increased competition for Indianapolis, the Proposed Transaction will mean a decrease in competition. Rather than single-line efficiency for Indianapolis, the Proposed Transaction will mean inefficient and costly trackage and switching arrangements. Rather than fresh opportunities for improved transportation options and resulting economic growth for Indianapolis, the Proposed Transaction will mean lost opportunities for improved transportation options and resulting economic harm.

CI-6 at 2.

CI claims that Indianapolis will become a "one railroad town" because NSR will not be able to effectively compete in Indianapolis. *Id.* at 3. The arrangement between CSXT and NSR precludes NSR from providing direct service to the 2-to-1 shippers, does not give NSR "any contractual rights regarding access to specific trackage" in Hawthorne Yard, gives CSXT the

"exclusive control of the management, operation and maintenance of the trackage from Muncie and Lafayette, as well as the trackage at Hawthorne Yard, *** [d]oes not require (CSXT) to dispatch (NSR) trains equally and without prejudice" and significantly circumscribes the "number and scope of Indianapolis customers (NSR) will actually be allowed to serve...." *Id.* at 4-5.

IPL expresses similar concerns over the serious loss of competition in Indianapolis in general and for its two plants in that city in particular. *See* I&PL-3. IPL demonstrates that both Perry K and Stout are 2-to-1 destinations. In so doing, IPL explains that the Primary

Transaction:

will not improve the competitive environment for railroad service to IPL in Indianapolis. On the contrary, it will diminish IPL's competitive options. (NSR) will enter the Indianapolis market at a significant disadvantage. It cannot realistically expect to compete with (CSXT) on equal terms. With only overhead trackage rights, (NSR) will not be able to offer IPL service comparable to that available today from (CRC). Even worse, (NSR) has not even considered what service it will be able to offer IPL in Indianapolis....

I&PL-3 at 5.

IPL is supporting ISRR's Responsive Application because the trackage rights ISRR seeks offer the only effective solution for preserving IPL's current two rail carrier competition at the Perry K and Stout Plants. *See* Weaver R.V.S. at 2 and 16, ISRR-9; Crowley R.V.S. at 1, ISRR-9.

Citizens Gas & Coke Utility ("Citizens") points out that Indianapolis is the twelfth largest metropolitan area in the Nation and the largest not having any direct access to navigable waters. It is deeply concerned over the further loss of rail competition in Indianapolis. Citizens notes that the arrangement between NSR and CSXT "offers not even the appearance of true

competition but is in any objective sense, an illusion." Comments and Supporting Evidence of Citizens, dated October 21, 1997, at 3.

Shell Oil Company and Shell Chemical Company ("Shell") oppose the Primary Transaction because of their concerns over "service deterioration, acceleration of rate increases, and a continued decrease in railroad competition." SOC-3 at 2. Because the arrangement between CSXT and NSR in Indianapolis is inadequate, Shell seeks to have Indianapolis declared an "open" area. Hall V.S. at 16, SOC-3.

Other shippers in the Indianapolis area are equally concerned over various anticompetitive effects of the Primary Transaction. For example, Savage Industries Inc., ("Savage") supports ISRR's requested trackage rights between Indianapolis and Crawfordsville because rail transportation is vital to its success. Savage explains that ISRR's requested conditions will maintain current rail competition and guarantee service in the event of problems such as those currently experienced in the west. (A copy of Savage's letter to the Board is attached as Exhibit 1.) Grain Processing Corporation ("GPC") is currently constructing a new plant on the ISRR south of Indianapolis. One of the primary reasons it selected this site was to gain access to Class I railroads, particularly CRC, for movements to the east and northeast. GPC maintains that ISRR's requested conditions are necessary to preserve rail competition in the Indianapolis area and avert potential service problems such as those experienced in the west. (A copy of GPC's letter to the Board is attached as Exhibit 2.) Indy Railway Service Corporation also supports ISRR's requested trackage rights to preserve rail competition for itself and the other shippers in the Indianapolis area that will become captive to a single rail carrier. (A copy of Indy Railway's letter to the Board is attached as Exhibit 3.)

As the above summary of evidence demonstrates, there is deep and widespread concern over the significant reduction of rail service in Indianapolis and the surrounding area. This area by far contains the most 2-to-1 shippers and presents the Board with the most serious and pervasive competitive issues. The arrangement between CSXT and NSR will not by any stretch of the imagination maintain the competitive status quo in the Indianapolis area, as Primary Applicants would lead the Board to believe. It is painfully obvious that, in carving up CRC, CSXT and NSR have relegated Indianapolis and the surrounding area to the complete and exclusive domain of CSXT.

**THE PRIMARY TRANSACTION WILL FINANCIALLY
HARM ISRR AND IMPAIR ITS ABILITY
TO PROVIDE ESSENTIAL SERVICES**

ISRR will lose approximately \$1.5 million in annual gross revenues if the Primary Transaction is approved without the conditions requested by ISRR. The loss of about 17 percent of its revenues would have a devastating effect on ISRR. ISRR would immediately have to reduce costs by terminating service on the marginal segment of its rail system and possibly increasing rates for its remaining shippers. These cost-saving measures will undoubtedly lead to further traffic losses.

In 1996, ISRR generated gross revenues of over \$1.5 million from traffic handled to IPL's Perry K and Stout Plants. That same year ISRR's total gross revenues were approximately \$9 million. Neumann V.S. at 3-4, ISRR-4. Since its inception, ISRR has been competitive for coal movements to Perry K and Stout. Post-Transaction, Perry K and Stout will become captive to CSXT and its subsidiary, the INRD, and ISRR will be foreclosed from serving either of these

plants. Consequently, all revenues ISRR has enjoyed from coal movements to Indianapolis will be diverted to CSXT and its subsidiary.

These traffic diversions will force ISRR to cover its fixed costs from a declining traffic base thereby increasing its per unit cost which would have to be passed on to its remaining customers. These increased unit costs will have a downward spiraling trend. As the per unit cost for ISRR's service increases, some of ISRR's remaining customers would be forced to switch to other transportation modes or go out of business, which, in turn, would only further increase ISRR's per unit cost and drive away additional customers.

ISRR's concern over the downward spiraling effect of the projected traffic losses is confirmed extensively in economic literature and was recognized by the Board's predecessor. It is almost universally accepted that the rail industry exhibits substantial economies of density.¹³ Consequently, as a railroad's traffic volume declines, its unit cost increases. Economies of density arise, in part, from the fact that railroads have relatively high fixed costs. As these costs are spread over a declining amount of traffic, the unit cost of providing service increases. While unit variable costs generally vary inversely with traffic volumes, the changes are not necessarily immediate or proportional with the changes in traffic volume. ISRR is essentially a single north-south rail line. ISRR, therefore, cannot abandon any discrete section of its mainline without jeopardizing the loss of additional traffic. The major cost savings ISRR could immediately achieve, such as significantly reducing maintenance expenditures, would ultimately be

¹³ *Coal Rate Guidelines - Nationwide*, 1 I.C.C. 2d 520, 531 (1985); Ernst R. Berndt, Ann F. Friedlaender, Judy-Er Wang Chiang, and Christopher A. Velturo, *Cost Effects of Mergers and Deregulation in the U.S. Rail Industry*, 4 *The Journal of Productivity Analysis* 127 (1993); A. Barbera, C.M. Grimm, K.A. Phillips, and L.J. Selzer, *Railroad Cost Structure-Revisited*, *Journal of the Transportation Research Forum*, Vol. 28, No. 1 237 (1987).

counterproductive. Moreover, ISRR's major expense, paying principal and interest on the acquisition cost of the rail system in 1992, cannot be avoided.

With the permanent loss of the IPL coal traffic to Indianapolis, the northern most section of ISRR's rail system -- between milepost 17, near Mooresville, Indiana, and milepost 6, at Indianapolis -- would be rendered unprofitable. The IPL's Indianapolis coal traffic has enabled ISRR profitably to operate this 11-mile segment. There is not sufficient local and other overhead traffic on that segment, however, to economically justify ISRR's continued operation of that segment. Therefore, with the loss of the Indianapolis coal traffic, the most immediate cost savings ISRR could achieve with the least disruptive effect on its overall financial situation would be to abandon the 11-mile segment. *See* Neumann V.S. at 4, ISRR-4. The abandonment of that segment, however, would sever ISRR's ties to Indianapolis, which would further reduce rail service to that city and leave shippers located on that segment without rail service.

The \$1.5 million revenue losses projected by ISRR are a direct result of traffic diversions to CSXT and its subsidiary. The abandonment of the 11-mile segment would result in further revenue losses from the local and other overhead traffic currently handled over that line.

On rebuttal, Primary Applicants raise three cursory arguments in response to ISRR's essential service case. First, they claim that ISRR will be able to continue moving coal to Indianapolis under existing contracts. CSX/NS-176 at 369. Primary Applicants' own citations to those contracts confirms the absurdity of their argument. *See Id.* at 54-55. As ISRR and other parties have demonstrated, post-Transaction, ISRR will be competitively foreclosed from serving IPL's plants in Indianapolis. Second, Primary Applicants claim that the use of 1996 revenue data is misleading because ISRR lost the Stout traffic to INRD in 1997. CSX/NS-176 at 370. While

ISRR lost the Stout traffic to its competitor, the INRD, last year through market place competition, under current competitive conditions ISRR is able to recapture all or part of that traffic. Once CSXT replaces CRC in Indianapolis, however, ISRR will be permanently foreclosed from handling any future Stout traffic.

Third, Primary Applicants allege that ISRR does not provide any essential rail service because six of the seven shippers on the segment ISRR would be forced to abandon can use trucks. *Id.* Their argument, however, is based totally on the mischaracterization of ISRR's discovery responses. In response to CSXT and NSR interrogatories, ISRR identified seven shippers that would lose rail service if ISRR is forced to abandon its rail line north of milepost 17. (Relevant portions of ISRR's discovery responses are attached as Exhibit 4.) In response to their subsequent question whether to ISRR's knowledge any of these "shipper's shipments...ever moved by truck", ISRR responded in the affirmative for six of the seven shippers. The question CSXT and NSR asked and the one ISRR answered was whether these shippers ever used trucks for any shipments and not whether the traffic ISRR handles for these shippers could move by truck. In any event, Mr. Neumann explains that only one of the shippers identified could substitute trucks to move the traffic now handled by ISRR. Neumann R.V.S. at 16, ISRR-9.

The essential services provided by ISRR are further confirmed in the letters attached as Exhibits 2 and 3. Indy Railway, which is located on the line segment ISRR would be forced to abandon, is a heavy railcar repair facility. It ships and receives railcars nationwide and portrays ISRR as its "umbilical cord" to the markets that it serves. GPC is constructing a new plant on the ISRR and is not one of the seven shippers identified by ISRR. Nevertheless, GPC demonstrates that trucks are not a viable alternative for long distance transportation. If ISRR is forced to

abandon the northern segment of its line, GPC will lose essential rail service for routings through Indianapolis, which will greatly reduce, if not eliminate, its ability to compete in the market.

ISRR is aware that in the past decade and a half the Board and its predecessor have focused on the preservation of essential services and not on the survival of carriers. Even though ISRR believes that it has fully met the Board's "essential service" standard, ISRR nevertheless urges the Board to give heightened attention to the plight of small railroads in the current environment. Given the ever diminishing number of Class I railroads and the concentration of market power, ISRR believes that it is incumbent on the Board to broaden its analytical perspective to consider the survival and financial viability of small carriers, as well as the survival of the shippers that rely on their service. It is well established that an agency "faced with new developments or in reconsideration of the relevant facts and its mandate, may alter its past interpretation and overturn past administrative rulings and practice." *American Trucking Ass'ns v. Atchison Topeka & Santa Fe Ry*, 387 U.S. 397, 416 (1967).

THE TRACKAGE RIGHTS ISRR SEEKS MEET ALL OF THE BOARD'S CONDITIONING CRITERIA

The trackage rights ISRR seeks are designed to ameliorate the anticompetitive consequences of the Primary Transaction in the Indianapolis area. If granted, the trackage rights would enable ISRR to preserve rail competition at IPL's Perry K and Stout Plants and for other affected shippers in Indianapolis and the surrounding area. At the same time, the revenues ISRR would derive from the trackage rights operations would allow ISRR to continue providing shippers on its system essential rail services.

As previously noted, the Board has broad authority to impose conditions on its approval of transactions. The Board has an affirmative duty to impose such conditions as are necessary to insure that a transaction before it is in the public interest. See *Atlantic Coast Line R. Co. v. United States*, 48 F.2d 239, 244 (W.D.S.C. 4th Cir. 1931), *aff'd*, 284 U.S. 288 (1932). The Board "is not intended to be a passive arbiter but the 'guardian of the general public interest,' with a duty to see that this interest is at all times effectively protected." *Lamoille Valley R.R. v. ICC*, 711 F.2d 295, 322 n. 55 (D.C. Cir. 1983).

ISRR's requested trackage rights satisfy each of the criteria for imposing a public interest condition and a condition designed to preserve essential services. ISRR has demonstrated that the Primary Transaction will have anticompetitive consequences and threatens harm to the public interest in Indianapolis and the surrounding area. Consequently, the imposition of public interest conditions is warranted.

In its Responsive Application, ISRR demonstrated that the requested trackage rights are operationally feasible. On rebuttal, Primary Applicants raise no operational challenges to ISRR's proposal to serve the Perry K and Stout Plants. CSX/NS-177 at 518-21. Their lack of criticism is not surprising, since ISRR's proposed service to the two IPL plants is more efficient and operationally far superior to the CSXT-NSR proposal. See *Weaver R.V.S.* at 19, ISRR-9.

CSXT Witness Orrison raises a few inconsequential operational concerns about the other conditions ISRR seeks. Because coal is the primary commodity ISRR moves over its rail line, Mr. Orrison expresses a concern over ISRR's ability to handle other commodities. As explained by Mr. Neumann, ISRR handles a diverse range of commodities, including steel, corn, soybeans, fuel oil, potash, fertilizer, plastic products, brick, ammonia, rail cars, lumber products, sugar,

LPG, sunflower, aluminum scrap, methanol, and canned vegetables. Neumann R.V.S. at 14, ISRR-9. With respect to the requested trackage rights between Indianapolis and Shelbyville, Mr. Orrison is concerned that ISRR's operations would add an interchange and delay traffic by at least one day. ISRR would be able to serve shippers on that line on a one-day round trip basis because Shelbyville is only 30 miles from Indianapolis. Given the limited volume of traffic on that line, ISRR operations would not cause any delays or interference. With respect to the proposed operations to Crawfordsville, Mr. Orrison is concerned that the addition of ISRR would cause interference and unnecessary complications for traffic on the Crawfordsville line. There are currently two freight carriers operating over the line to Crawfordsville, and because ISRR is simply seeking to replace the purported NSR operations, there will continue to be only two carriers on the line post-Transaction. Mr. Orrison generally complains about additional complexities of adding a trackage rights carrier. These concerns, however, are generic and would apply to any grant of trackage rights. As Mr. Orrison well knows, trackage rights are ubiquitous, with railroads operating over one another daily. His concerns apply to all trackage rights operations and are surmounted daily by CSXT and other railroads.

ISRR's requested trackage rights are specifically designed to eliminate the competitive harm threatened by the Primary Transaction in Indianapolis and the surrounding area. By gaining direct access to IPL's two Indianapolis plants, ISRR would be able to preserve the two rail carrier competition those plants currently enjoy. The remainder of the requested conditions would enable ISRR to offer the general shipping public in the Indianapolis area a competitive option to CSXT, which will be lost when CRC exits this market. As previously shown, NSR's ability to compete in this market is illusory. If granted, the trackage rights ISRR seeks would

enable ISRR to provide the shipping public in this area meaningful and effective rate and service competition.

Finally, ISRR's requested trackage rights are in the public interest and would not be detrimental to the Primary Transaction. Insofar as Indianapolis and the surrounding area are concerned, the Board's balancing test is quite simple. Primary Applicants have demonstrated few, if any, public benefits in this area. Not only are there no public benefits to speak of, the Primary Transaction, if unconditionally approved, would result in substantial public detriments to shippers in the Indianapolis area in the form of increased transportation costs and less efficient routings. On the other hand, the general public in the Indianapolis area would derive significant benefits from the conditions ISRR seeks through improved service and the preservation of rail competition in the area. At the same time, the conditions would not detract in any material respect from the public benefits CSXT and NSR expect to achieve from the Primary Transaction. CSXT and NSR claim collective public benefits of nearly \$1 billion a year. *See CSX/NS-18 at 2.* The requested conditions would simply enable ISRR to continue competing for the IPL traffic and possibly attract some additional traffic from service to shippers otherwise losing competitive rail service in the Indianapolis area.

The criteria for imposing "essential service" conditions, as set forth at 49 C.F.R. § 1180.1 (d) (1), have already largely been covered. First, the requested trackage rights to serve the Perry K and Stout Plants are directly related to ISRR's projected financial losses and the resulting loss of essential services on the ISRR rail system. If those conditions are granted, ISRR would be able to continue competing for that traffic and provide ISRR the opportunity to earn sufficient

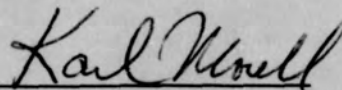
revenues so that it can continue providing efficient and economical service to its on-line shippers.

Second, the requested trackage rights are designed to enable ISRR's rail-dependent shippers to receive adequate service. If ISRR is able to retain the IPL traffic or gain new traffic in the Indianapolis area, ISRR will remain a viable carrier and will be able to continue serving its customers. Third, as explained above, the requested trackage rights are operationally feasible and would not pose any operating or other problems for CSXT and NSR. Fourth, as already demonstrated, the requested rights would not frustrate the ability of Primary Applicants to achieve their anticipated public benefits.

CONCLUSION

For the foregoing reasons, ISRR respectfully urges the Board to condition the Primary Transaction by imposing the trackage rights sought by ISRR.

Respectfully submitted,



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Dated: February 23, 1998

EXHIBITS

EXHIBIT 1

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December 18, 1997

Mr. Vernon A. Williams
Secretary
Surface Transportation Board
1925 K Street, N. W.
Washington, D. C. 20423-0001

STB FINANCE DOCKET NO. 33388

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 (SUB-NO.76)

INDIANA SOUTHERN RAILWAY COMPANY
--TRACKAGE RIGHTS--
CSX TRANSPORTATION, INC. AND INDIANA RAILROAD COMPANY

VERIFIED STATEMENT
OF
KEVIN A. HALL

My name is Kevin A. Hall, Senior Vice President for Savage Industries Inc. My business address is 5250 South Commerce Drive, Suite 200, Salt Lake City, Utah 84107. My responsibilities include general management of rail operations, which include rail property leases and rail equipment leases, as well as arranging for carload shipment.

Savage Industries Inc. is a multimodal transportation company with over 40 million tons of products managed annually with a facility located on CONRAIL in Indianapolis. Rail transportation is a vital factor to the success of our business as we ship and receive over 200,000 carloads annually.

Mr. Vernon A. Williams
Page 2
December 18, 1997

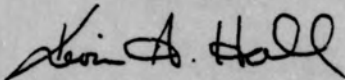
The multimodal transportation business is highly competitive and economic survival is directly related to availability of responsive transportation service at competitive rates.

In summation, we request the Surface Transportation Board to grant the trackage rights requested by the Indiana Southern Railroad (ISRR) to, from and between Indianapolis and Crawfordsville, IN. We believe the ISRR trackage rights will maintain competition, provide my company with long-term economic security, and guarantee rail transportation in the event of service problems such as those experienced recently in the west.

I, Kevin A. Hall, declare under penalty of perjury that the foregoing is true and correct. Further, I certify that I am qualified and authorized to file this verified statement.

Executed on December 18, 1997.

Sincerely,

A handwritten signature in dark ink, appearing to read "Kevin A. Hall". The signature is fluid and cursive, with the first name "Kevin" and last name "Hall" clearly distinguishable.

Kevin A. Hall
Senior Vice President
and General Manager

EXHIBIT 2



Grain Processing Corporation
1600 Oregon Street
Muscatine, Iowa 52761-1494 USA
Phone 319-264-4211

January 6, 1998

Mr. Vernon A. Williams
Secretary
Surface Transportation Board
1925 K Street, N.W.
Washington, DC 20423-0001

STB FINANCE DOCKET NO. 33388

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 (SUB-NO.76)

INDIANA SOUTHERN RAILWAY COMPANY
-TRackage RIGHTS-
CSX TRANSPORTATION, INC. AND INDIANA RAILROAD COMPANY

VERIFIED STATEMENT
OF
ROBERT J. WILLIS

My name is Robert J. Willis, Vice President of Transportation for Grain Processing Corporation. My business address is 1600 Oregon Street; Muscatine, IA 52761. I have held my position for six (6) years and my responsibilities include negotiation of rail contracts, rail property leases and rail equipment leases, as well as arranging for carload shipments.

Grain Processing Corporation is a corn wet milling company located in Muscatine, Iowa. We are currently constructing a new plant near Washington, Indiana, on the Indiana Southern Railroad. One of the primary reasons for selecting this site was the rail transportation alternatives offered by connections the Indiana Southern had with Class I railroads. One of these was Conrail in Indianapolis for our customers in the east and northeast. By allowing the Indiana Southern's request for trackage rights you will assure competition for the future through this large 2 to 1 shipping community of Indianapolis and its surrounding area.

The grain business is highly competitive and economic survival is directly related to availability of responsive transportation service at competitive rates. Long distance truck transportation is not a viable alternative due to volume shipment requirements.



Grain Processing Corporation

1600 Oregon Street
Muncatine, Iowa 52751-1494 USA
Phone 319-264-4211

Page 2

The loss of rail service options would be detrimental to our business as we are dependent on the cost effectiveness of rail shipments, especially over long distances where trucks cannot compete. Without these options, our ability to compete in the current market would be greatly reduced if not eliminated.

Furthermore, we have seen the manner in which customers throughout the country have been affected by service problems resulting from recent railroad mergers in the western United States. Given this scenario, we feel the value of a viable alternative after the Conrail acquisition is evident.

In summation, we request the Surface Transportation Board to grant the trackage rights requested by the Indiana Southern Railroad (ISRR). We believe the ISRR trackage rights will help maintain competition, protect my company and others from potential post-merger rate increases, and guarantee rail transportation in the event of service problems such as those experienced recently in the west.

I, Robert J. Willis, declare under penalty of perjury that the foregoing is true and correct. Further, I certify that I am qualified and authorized to file this verified statement.

Executed on January 6, 1998.

Sincerely,

GRAIN PROCESSING CORPORATION

Robert J. Willis
Vice President Transportation

RJW/bc

bcc Mr. Phil Wilzbacher, Director of Marketing; Indiana Southern Railroad;
PO Box 158; Petersburg, IN 47567

EXHIBIT 3

INDY RAILWAY SERVICE CORPORATION
Mailing Address: P.O. Box 42331 Office/Shop: 6111 W. Hanna Ave.
INDIANAPOLIS, INDIANA 46242-0331
Telephone: 317-388-3708

February 3, 1998

Mr. Vernon A. Williams, Secretary
Surface Transportation Board
1925 K. Street, N.W.
Washington, D.C. 20423-0001

Subject: STB FINANCE DOCKET NO. 33388

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 (SUB-NO. 76)

INDIANA SOUTHERN RAILROAD, INC.
- TRACKAGE RIGHTS-
CSX TRANSPORTATION, INC. AND INDIANA RAILROAD COMPANY

Dear Mr. Williams:

My name is Calvin T. Morris, President and owner of Indy Railway Service Corporation located at 6111 West Hanna Avenue, Indianapolis, Indiana, 46241. The mail address is P.O. Box 42331, Indianapolis, Indiana, 46242-0331.

Indy Railway Service Corporation is a heavy railcar repair facility, specializing in open top coal hopper cars and covered hopper cars. We have been in business since 1974 and at the present location since 1977. We are served by The Indiana Southern Railroad at mile post eight (8) on the southwest side of Indianapolis.

The customer base of Indy Railway Service Corporation is nationwide with cars moving to and from Conrail at Indianapolis on the north end and from Norfolk Southern Railway at Oakland City, Indiana, and CSX at Evansville, Indiana, on the south end. We also receive considerable traffic from The Indiana Southern Railroad, originating at Petersburg, Indiana, and coal mines in the immediate area. In fact, The Indiana Southern Railroad is

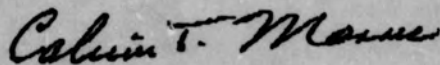
our umbilical cord to the market we serve. Without them we are dead at the present location.

Other local industries now served by Conrail will also be in peril if they are captive to single line rail service. I am well aware of the competitive nature and operating excellence of the Norfolk Southern Railway, where I have twelve years service and CSX, where I have fifteen years service. Neither of these companies will suffer from competition of a short line railroad such as The Indiana Southern Railroad.

As a result of the dire need for competition to control rates and insure survival of captive local industries, I request the Surface Transportation Board to grant the trackage rights requested by The Indiana Southern Railroad as outlined in the STB Finance Docket No. 33388 (Sub-No. 76).

Thank you for your consideration.

Sincerely,



Calvin T. Morris
President

CTM/srt

cc: Mr. Dick Neumann, General Manager
Indiana Southern Railroad Company
P.O. Box 158
Petersburg, IN 45967

EXHIBIT 4

ISRR-6

**BEFORE THE
SURFACE TRANSPORTATION BOARD**

STB FINANCE DOCKET NO. 33388

**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 (SUB-NO. 76)

**INDIANA SOUTHERN RAILROAD, INC.
--TRACKAGE RIGHTS--
CSX TRANSPORTATION, INC. AND INDIANA RAIL ROAD COMPANY**

**RESPONSE OF INDIANA SOUTHERN RAILROAD, INC.,
TO THE FIRST SET OF INTERROGATORIES AND REQUESTS FOR DOCUMENTS OF
CSX AND NORFOLK SOUTHERN**

Indiana Southern Railroad, Inc. ("ISRR"), hereby responds to the First Set of Interrogatories and Requests for Production of Documents of CSX and NS¹ (CSX/NS-133), served November 6, 1997.

¹ "CSX" refers collectively to CSX Corporation and CSX Transportation, Inc., and "NS" refers collectively to Norfolk Southern Corporation and Norfolk Southern Railway Company.

3. Describe in detail the basis for ISRR's "estimates that it will lose approximately \$1.5 million in revenues annually to CSXT and INRD," as alleged on page 5 of ISRR's Responsive Application.

Response: ISRR projects that it will lose all revenues earned from traffic handled for Indianapolis Power and Light Company ("IPL"). Documents responsive to this interrogatory will be placed in ISRR's depository.

4. Describe in detail the basis for ISRR's contention that "[t]he loss of these revenues will impair ISRR's ability to perform essential services on its rail line," as alleged on page 5 of ISRR's Responsive Application.

Response: The loss of the projected revenues will force ISRR to reduce costs. The most immediate cost savings ISRR would be able to achieve would be to abandon its line north of milepost 17, which would sever ISRR's connection to Indianapolis. This northern line segment would not be profitable without the IPL traffic that currently moves over that segment. If ISRR is forced to abandon that segment, all rail shippers on that segment as well as shippers on other parts of the ISRR system that ship by rail to or over Indianapolis would lose rail service.

5. Identify all shippers currently served by ISRR that ISRR contends would lose rail service as a result of the Proposed Transaction.

Response: ISRR is continuing to analyze the actions ISRR would need to take as a result of the projected revenue losses. As explained in the Responsive Application, one option ISRR has considered is to abandon its line north of milepost 17. If ISRR were to take this action the following shippers would lose rail service:

Trans-City Terminal Warehouse, Inc.
P.O. Box 42069 4750 Kentucky Ave.
Indianapolis, IN 46242

Newcomer Lumber
149 East High
Mooresville, IN 46158

Ambassador Steel
149 Sycamore Lane
Mooresville, IN 46158

Star Metals
Illinois Street
Petersburg, IN 47567

Indy Railway Service Corporation
6111 W. Hanna Ave.
Indianapolis, IN 46241

Ameriplex Industrial Park
251 N. Illinois Street
Indianapolis, IN 46204

General Shale
P.O. Box 96
Sycamore Lane
Mooresville, IN 46158

6. For each shipper identified in response to the preceding interrogatory, identify:
- a. The specific physical location, including street address, of each of that shippers facilities served by ISRR;
 - b. The annual volume of traffic, by car, that ISRR has transported for that shipper (separately for each facility) from 1995 to the present; and
 - c. The routes, by origin and destination, over which ISRR has transported traffic for that shipper from each facility from 1995 to the present.

Response:

- a. See response to Interrogatory No. 5.
- b. Documents responsive to this interrogatory will be placed in ISRR's depository.
- c. For Trans-City Terminal Warehouse, inbound traffic is handled from interchange with CRC at Indianapolis, CP Rail at Bee Hunter, and CSX at Evansville. For Newcomer Lumber, inbound traffic is handled from interchange with CRC at Indianapolis. For Ambassador Steel, inbound traffic is handled from interchange with CRC at Indianapolis, NS at Oakland City and CSX at Evansville. For Indy Railway Service Corporation, inbound and outbound traffic is handled to and from the interchange with CRC at Indianapolis, CSX at Evansville, and INRD at

Switz City. For General Shale, inbound traffic is handled from interchange with NS at Oakland City and CSX at Evansville. Outbound traffic is handled to interchange with CRC at Indianapolis. Ameriplex Industrial Park is currently under development on the ISRR with the intention that companies locating in the Park will have rail service. For Star Metals, inbound traffic is handled from interchange with CRC at Indianapolis and CSX at Evansville. Outbound traffic is handled to interchange with CRC at Indianapolis.

7. Identify the amount of revenue received by ISRR from each of the shippers identified in response to the preceding interrogatory for the years 1995, 1996, 1997 or any part thereof.

Response: Documents responsive to this interrogatory will be placed in ISRR's depository.

8. For each shipper identified in response to Interrogatory No. 5,
- a. To ISRR's knowledge, have any of that shipper's shipments from any facility served by ISRR ever moved by truck or any other mode of transportation not involving ISRR at any time from 1995 to the present?
 - b. If the answer to the preceding subpart is "yes," identify separately with respect to each such facility the alternate transportation mode or modes by which such shipments moved.

Response:

- a. Yes, except for Indy Railway Service Corporation.
- b. The alternate mode for each shipper other than Indy Railway is truck. To the best of ISRR's knowledge, Indy Railway's only mode of transportation has been rail.

9. State the volume of traffic that ISRR contends it will lose if the Application is approved without the conditions ISRR requests:

- a. In total; and

Response: According to Applicants, Indianapolis is by far the largest 2-to-1 point created by the Proposed Transaction. CSX/NS-18 at 548. In addition, the Indianapolis area today is a major traffic origination point for CRC. CSX/NS-20 at 209. Unlike CRC today, which has a major presence in Indianapolis and direct routes to and from Indianapolis over which it can provide local service, NS will have only a limited presence in Indianapolis, its routings to and from Indianapolis are highly circuitous in relation to the rest of the NS system, and NS will not be able directly to serve any shipper in Indianapolis or on the rail lines it will use to access Indianapolis. NS's limited and unduly circumscribed access to Indianapolis is hardly an appropriate substitute for CRC's current presence in the area.

12. Describe in detail the basis for ISRR's contention that "ISRR's customers would have no option other than to divert to (sic) their shipments to trucks" if ISRR reduces rail service as a result of traffic diversions to CSX and INRD, as ISRR contends on pages 6-7 of the Responsive Application.

Response: Shippers on the ISRR today have two transportation options: they can ship by rail over the ISRR or they can ship by truck. If ISRR is forced to reduce or stop service altogether, these shippers will either have to ship by truck or not ship at all and go out of business. The basis for ISRR's contention is that there is no barge service nearby, air freight service is impracticable and these shippers' traffic is not conducive to being hauled by wheelbarrow.

13 Define the term "neutral and indifferent gateway service" as that term is used on page 9 of the Responsive Application.

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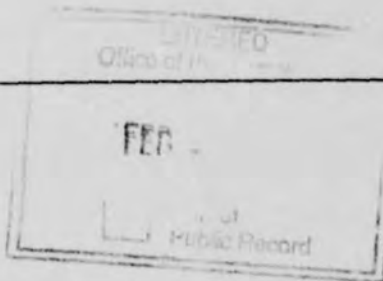


U. S. Department of Justice

Antitrust Division

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325 Th Street, N.W., Suite 500

Washington, DC 20530

February 23, 1998

E



Mr. Vernon A. Williams, Secretary
Surface Transportation Board
1925 K Street, N.W., Seventh Floor
Washington, D.C. 20423-0001

Re: Conrail Control Case -- STB Finance Docket No. 33388

Dear Secretary Williams:

I am enclosing for filing an original and 25 copies of the Brief of the United States Department of Justice (DOJ-2). Our Brief contains highly confidential material and so it should be filed under seal. I am also enclosing 25 copies of a public (redacted) version of our Brief. Finally, I am enclosing two 3.5 inch disks containing the highly confidential and public versions of our Brief in Word Perfect 6.1 format.

We are serving the highly confidential and public versions of this filing on the Applicants and all other Parties of Record known by the Department to be entitled to access to highly confidential material under the protective order in this proceeding. All other Parties of Record who are not on the highly confidential restricted service list will receive the public version of this filing.

Thank you for your assistance in this matter. If you have any question please feel free to call me at 202-307-6357.

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to working office. Original copy is in the
Office of the Secretary
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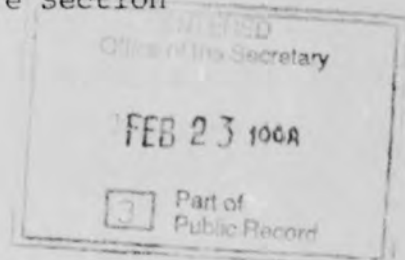
Sincerely yours,

Michael P. Harmonis

Michael P. Harmonis
Attorney
Transportation, Energy and
Agriculture Section

Enclosures

cc: The Honorable Jacob Leventhal
Parties of Record





U. S. Department of Justice

Antitrust Division

185874

325 Th Street, N.W., Suite 500
Washington, DC 20530

February 23, 1998



Mr. Vernon A. Williams, Secretary
Surface Transportation Board
1925 K Street, N.W., Seventh Floor
Washington, D.C. 20423-0001

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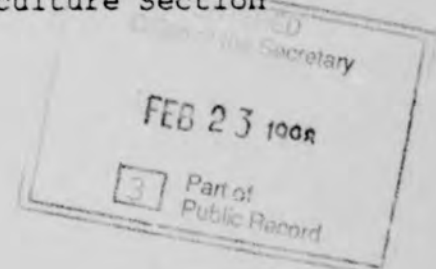
Sincerely yours

Michael P. Harmonis
Michael P. Harmonis
Attorney
Transportation, Energy and
Agriculture Section

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Not Available for Public Inspection
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to working office. Original copies in the
office of the Secretary
UNDER SEAL

Enclosures

cc: The Honorable Jacob Leventhal
Parties of Record

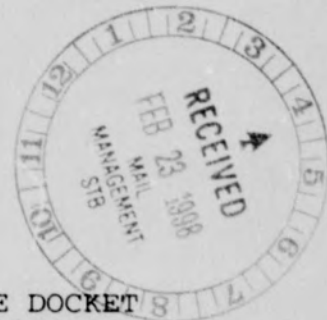


185874

PUBLIC (REDACTED) VERSION

DOJ-2

BEFORE THE
SURFACE TRANSPORTATION BOARD
WASHINGTON, D.C.



CSX CORPORATION AND CSX TRANSPORTATION,)
INC., NORFOLK SOUTHERN CORPORATION)
AND NORFOLK SOUTHERN RAILWAY COMPANY) FINANCE DOCKET
--CONTROL AND OPERATING LEASES/) NO. 33388
AGREEMENTS--CONRAIL INC. AND)
CONSOLIDATED RAIL CORPORATION)

BRIEF OF THE UNITED STATES DEPARTMENT OF JUSTICE

Communications with respect to this document should be addressed to:

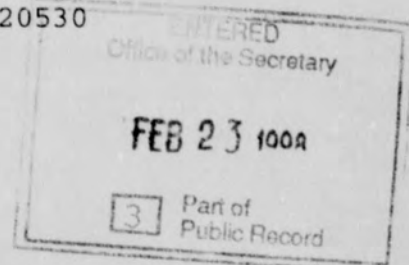
Roger W. Fones, Chief
Donna N. Kooperstein, Assistant Chief

Michael P. Harmonis
Attorney

*original
Public Version
Brief*

Transportation, Energy &
Agriculture Section
Antitrust Division
U.S. Department of Justice
325 Seventh Street, N.W.
Washington, D.C. 20530

(202) 307-6357



February 23, 1998

BEFORE THE
SURFACE TRANSPORTATION BOARD
WASHINGTON, D.C.

CSX CORPORATION AND CSX TRANSPORTATION,)
INC., NORFOLK SOUTHERN CORPORATION)
AND NORFOLK SOUTHERN RAILWAY COMPANY) FINANCE DOCKET
--CONTROL AND OPERATING LEASES/) NO. 33388
AGREEMENTS--CONRAIL INC. AND)
CONSOLIDATED RAIL CORPORATION)

BRIEF OF THE UNITED STATES DEPARTMENT OF JUSTICE

Public Version

INTRODUCTION

On June 23, 1997, CSX Corporation ("CSX"), Norfolk Southern Railway Company ("NS"), and Conrail Inc., collectively the "Applicants," filed their primary application in this matter pursuant to 49 U.S.C. 11321-25. The primary application seeks Board approval and authorization for the acquisition of control by CSX and NS of Conrail, and the division of Conrail's assets by and between CSX and NS. The United States Department of Justice filed comments and submitted the testimony of Dr. Peter A. Woodward, an economist, on October 21, 1997. The Department now submits its final brief.

I. POSITION OF THE UNITED STATES DEPARTMENT OF JUSTICE

The record evidence in this matter demonstrates that the proposed transaction raises significant competitive problems in two markets, and perhaps a third, depending on the validity of an

agreement between NS and Conrail to terminate a trackage rights agreement. These markets involve coal shipments to electric utility plants in Indiana and Maryland, and, in each of them, the number of competitors effectively would decline from two to one after the transaction. The total volume of traffic in these two-to-one markets is well over \$80 million.

The Board should impose conditions that resolve the competitive problems in these markets before approving the proposed transaction. Although conditions in the form of trackage rights do not always provide effective remedies, they appear to be appropriate in this case. The Department therefore recommends that the Board restore the competition that otherwise would be lost by imposing short segments of trackage, connection, and build-out rights in the affected markets as specified in detail later in this brief. The conditions recommended by the Department are narrowly tailored, and so they would maintain two-carrier competition in the affected markets without interfering with any efficiencies that CSX or NS may seek to achieve from the transaction.

II. DESCRIPTION OF THE PROPOSED TRANSACTION

CSX and NS plan to purchase Conrail for \$10.2 billion. Together these three railroads accounted for \$13.3 billion in sales in 1996. Conrail operates 10,701 miles of track in the East and Midwest. CSX and NS, respectively, operate 18,500 and 14,300 miles of track in the Southeast and Midwest. After the breakup, CSX and NS each would operate more than 20,000 route

miles in the eastern United States.

NS and CSX plan to divide Conrail's principal routes, which form an "X" crossing in Ohio, with each railroad operating two of the four legs of the "X". CSX will acquire most of Conrail's main rail line from St. Louis through Indianapolis and Cleveland to New York, Boston, and Montreal. CSX also will acquire most of Conrail's routes in Ohio, Indiana, and Illinois. NS will acquire Conrail's main line from Chicago to Pittsburgh and Philadelphia as well as two lines connecting New York to the current NS line at Buffalo and most lines in Michigan, Maryland, Delaware, and Pennsylvania. NS and CSX each will gain a route connecting its lines in the Southeast with New York, North America's largest consumer market. CSX and NS jointly will operate tracks and terminals in the New York metropolitan area, New Jersey, and Detroit, as well as in parts of Philadelphia.

While the proposed transaction would create new rail competition, most notably in major markets in New York, New Jersey, and Philadelphia, CSX and NS acknowledge that there also would be markets where shippers would see their options decline from two rail carriers to one. See CSX/NS-18, Volume 1 at 4. In an attempt to remedy the acknowledged competitive concerns in these markets, CSX and NS have agreed to provide one another with trackage and/or haulage rights, which they contend would permit the continuation of two-rail carrier service wherever possible. See id.

III. LEGAL STANDARD

The ICC Termination Act of 1995 ("the Act") sets out the framework under which the Board must review and analyze this merger. See 49 U.S.C. §§ 11321-27. In proceedings involving rail consolidations, mergers, and acquisitions of control, the Act requires the Board to consider a number of elements in making its essential finding of whether the transaction is consistent with the public interest. 49 U.S.C. § 11324. One element of the public interest finding is whether the proposed transaction would have an adverse effect on competition among rail carriers in the affected region or in the national rail system. 49 U.S.C. § 11324(b)(5).

The Board is also guided by the rail transportation policy, 49 U.S.C. 10101, added by the Staggers Rail Act of 1980. Union Pacific Corp., et al. -- Control and Merger -- Southern Pacific Corp., et al., Finance Docket No. 32760 ("UP/SP"), Decision No. 44 (served August 12, 1996) at 99. That policy emphasizes "reliance on competitive forces . . . to modernize railroad operations and to promote efficiency." Id. at 100.

It is therefore necessary for the Board to determine whether a proposed merger or acquisition of control will produce anticompetitive effects in any defined market. Although the Board does not sit as an antitrust court in determining compliance with the antitrust laws, the Board must define economic markets and then evaluate competitive effects in those markets in order to reach its ultimate public interest

determination. This is as it should be, for antitrust policy "gives understandable content to the broad statutory concept of 'the public interest.'" FMC v. Aktiebolaget Svenska Amerika Linien, 390 U.S. 238, 244 (1968); see also Northern Lines Merger Cases, 396 U.S. 491, 511-13 (1970).

IV. FRAMEWORK FOR COMPETITIVE ANALYSIS

The core issue in competition analysis is whether the proposed transaction likely would create or enhance market power or facilitate its exercise. Market power is the ability of a seller profitably to maintain prices above competitive levels (or reduce quality or service below competitive levels) for a significant period of time. The result of the exercise of market power is a transfer of wealth from buyers to sellers and misallocation of resources. A merger can facilitate the exercise of market power by increasing the likelihood of coordinated interaction among competing firms, or by creating a market structure in which firms find it profitable to unilaterally raise prices or reduce output.

To determine whether the proposed transaction would create, enhance, or facilitate the exercise of market power, the Board should define the markets within which the merging parties compete. Under the Horizontal Merger Guidelines, which outline the enforcement policy of the Department of Justice concerning horizontal acquisitions and mergers subject to section 7 of the Clayton Act, 15 U.S.C. 18, a market is defined as a set of products or services within a geographic area such that a

hypothetical monopolist could profitably impose a "small but significant and nontransitory" price increase. See Horizontal Merger Guidelines, issued in 1992, revised in 1997 § 1.11.

If the evidence shows that a hypothetical monopolist of any given product or service profitably could impose such a price increase, that product or service is defined as the market. Id. If, on the other hand, the evidence shows that a sufficient number of consumers would substitute other products or services, which would make such a price increase unprofitable, those products or services are also included in the market. Id. This process continues until a group of products or services is identified for which a small but significant and nontransitory price increase would be profitable. Id.

In this case, the definition of a market begins with the basic service provided by the railroad -- the transportation of a particular commodity from a particular origin to a particular destination. Conrail, CSX, and NS compete for significant amounts of traffic in a large number of markets, and in some of the markets where they compete, they are the only rail carriers who are or potentially could be providing service.

The market, however, may not be limited to rail carriers. Intermodal competition in the form of truck, barge, or sometimes pipeline movements may allow shippers to substitute another mode of transportation for the shipment of a commodity from a particular origin to a particular destination. If another mode of transportation is a close substitute for rail, a single rail

carrier alone likely would not possess market power in the movement of that commodity; that is, the rail carrier's ability to raise rates would be constrained by the shippers' ability to use another mode.

For some commodities, however, transportation by truck cannot compete with rail because the distance the commodity is shipped is great, the volume of the commodity shipped is large, or the value of the commodity as compared to its weight is small. Water competition is often limited by the geographic location of the shipper or receiver, and sometimes by seasonal factors.

Source competition is also a potential factor in market definition. Source competition could allow a shipper to avoid a supra competitive rail rate between two points by using alternative rail carriers to ship a commodity from a different source or to a different destination.

Thus, in defining markets, the Board should address such issues as whether rail carriers not currently transporting the commodity are economically substitutable for rail carriers currently transporting the commodity, whether truck transportation or barge transportation is economically substitutable for rail transportation, and whether commodities originating or consumed at one location are economically substitutable for commodities originating or consumed at another location.

Once the markets are defined, the Board must evaluate the competitive impact of the proposed merger. Generally, a rail

merger would not have an adverse competitive impact on a market where there are sufficient intermodal alternatives that would prevent the exercise of market power by the merged carrier alone or in concert with others. Hence a rail merger likely would not adversely impact a market where shippers economically can ship the same commodity to other destinations, or where receivers can economically receive the same commodity from other origins or consume it at other locations, or receive a substitute commodity from the same or other origins via transportation alternatives not involving the merged carrier. Absent sufficient competitive alternatives, however, a reduction in the number of rail competitors to a small number causes a substantial loss of competition. The smaller the number of rail competitors remaining after a merger, the worse the competitive problem would be, with a rail monopoly creating the worst competitive problem. See UP/SP at 100; see also, e.g., Santa Fe Southern Pacific Corp. -- Control -- Southern Pacific Transportation Co., 2 I.C.C. 2d 709, 791-792 (1986).

V. The Competitive Analysis

The Department of Justice has relied on the testimony of its economic witness, Dr. Woodward, and on evidence submitted by other parties in reaching its conclusions regarding the competitive effects of the proposed transaction. After focusing on movements where it appears that the number of rail competitors would be reduced from two to one as a result of the transaction, Dr. Woodward analyzed whether other forms of competition, such as

intermodal competition or competition resulting from other origins and to other destinations, would constrain the merged carrier from raising rates or reducing service. In conducting his analysis, Dr. Woodward relied on 1995 waybill data, interviews with shippers and receivers, documents submitted by the Applicants and other parties to this proceeding, and deposition testimony.

Based on Dr. Woodward's testimony and on evidence submitted by other parties, the Department has concluded that the unconditioned acquisition and division of Conrail by the Applicants would substantially lessen competition in at least two, and perhaps three relevant markets.

A. Indianapolis Power & Light Company

The proposed transaction likely will reduce transportation competition for coal shipments to the Stout plant of Indianapolis Power & Light Company ("IPL"). Stout, situated in the city of Indianapolis, burns Indiana coals, all transported by rail from mines within 110 miles to the south of the plant.¹

Stout is served directly by Indiana Railroad ("INRD"), a wholly owned subsidiary of Midland United Corporation, which is

¹ Hoback RVS at 195 (CSX/NS-177, Volume 2A); Woodward VS at 8 (DOJ-1). All citations of fact refer to the verified statements, depositions, rebuttal verified statements, and other papers that constitute the record in this proceeding. For the Board's convenience, the Department has appended cited portions of the record to this brief as it is filed with the Board. Upon request, the Department will provide cited portions of the record to persons on the highly confidential restricted service list.

89% owned by CSX.² Stout is also served by Conrail in joint movement with Indiana Southern Railroad ("ISRR"), with Conrail using INRD switch services into Stout.³ Conrail could serve Stout directly if Stout were to construct a build-out line to the nearby Conrail branch line, or to Conrail's Indianapolis Belt Running Track, both of which are within 3 miles of Stout.⁴ If Stout built out, Conrail could serve the plant in joint movement with ISRR without using INRD's switching services.⁵

INRD (CSX) and Conrail thus compete for coal shipments to Stout.⁶ Pursuant to the terms of the proposed transaction, however, CSX would acquire Conrail's lines into Indianapolis, and eliminate the CSX-Conrail competition for coal shipments that IPL now enjoys.⁷

² Hoback RVS at 195; Hoback dep. at 8-9. As befitting its 89% stock ownership, CSX may elect three of five members of the board of directors at Midland and INRD. Hoback dep. at 14. This degree of control forecloses any competition between CSX and INRD, and so CSX and INRD should be viewed as one entity for purposes of competition analysis. See United States v. Penn-Olin Co., 378 U.S. 158, 168 (1964) ("realistically, the parents would not compete with their progeny"); Yamaha Motor Co. v. Federal Trade Commission, 657 F.2d 971, 982 (8th Cir. 1981), cert. denied 456 U.S. 915 (1982); Northern Natural Gas Company v. Federal Power Commission, 399 F.2d 953, 967 (D.C. Cir. 1968).

³ See, e.g., Weaver RVS at 2 (ISRR-9).

⁴ Crowley RVS 28-29 (ISRR-9); Neuman RVS 9 (ISRR-9); Weaver RVS 19-22; Woodward VS 8, 17-18 (DOJ-1).

⁵ Weaver RVS at 20-21; Woodward VS at 17-18.

⁶ Neuman RVS at 5; Weaver VS at 9 (IP&L-3, Exhibit 1); Woodward VS at 8, 16; see also Weaver RVS at 11-12.

⁷ CSX/NS-18, Volume 1 at 34-36. Stout is so efficient a plant that IPL cannot constrain INRD's rates by producing less

Applicants argue that Conrail is not an effective competitor at Stout,⁸ but the record demonstrates that competition between Conrail and INRD has significantly reduced IPL's coal transportation costs. In 1996, when Conrail, INRD, and trucks sought Stout's business, INRD matched Conrail's offer to win 90% of Stout's business, with the competition between them reducing prices to Stout 20% below the then-current truck rate.⁹ And while Conrail may not have delivered coal to Stout in 1997, it delivered more than 10% of Stout's requirements in 1995 and 1996, an amount in the range of 160,000 tons of coal per year.¹⁰ IPL's current coal transportation agreement with INRD, [[

]].¹¹ This [[]], demonstrates that IPL continues to regard Conrail as an effective competitor.¹²

Conrail therefore does provide significant competition at Stout. If the Board does not impose conditions to replicate this

power at Stout and shifting that generation to other IPL plants or to other plants in its East Central Area Reliability Interconnection Network ("ECAR"). Woodward VS at 19.

⁸ See CSX/NS-176, Volume 1 at 55 Hoback RVS at 199; Vaninetti RVS at 103 (CSX/NS-177, Volume 2B).

⁹ Woodward VS at 18.

¹⁰ See Vaninetti RVS at 510HC; Weaver RVS at 9, 12; Woodward VS at 8-9.

¹¹ See Hoback dep. 59; Vaninetti RVS at 510HC.

¹² Hoback dep. at 228-29; Weaver RVS at 12.

lost competition, then the prices Stout pays for its coal transportation are likely to rise.¹³

Applicants additionally argue that truck movements provide substantial competition at Stout,¹⁴ but this argument also is at odds with the facts. In recent years, Stout has not received a single pound of coal by truck.¹⁵ This is hardly surprising,

[[

]].¹⁶ Of course

higher truck costs are reflected in higher truck transportation rates. Rail rates for movements of Indiana coals to Stout are in the [[]],

except for movements from the mine closest to Stout, the Farmersburg mine, from which the differential [[]] per ton.¹⁷

¹³ See Woodward VS at 18-19.

¹⁴ CSX/NS-176, Volume 1 at 55-56

¹⁵ See Weaver RVS 3, 9-10; CSX/NS-178 Volume 3D at 109-111 (answer 1m); Hoback dep. at 131-32.

¹⁶ See Neuman RVS at 10; Vaninetti RVS at 528; Weaver RVS at 10.

¹⁷ See Hoback dep. at 60-61; Vaninetti RVS at 506HC; Weaver RVS at 3, 10. CSX witness Gerald Vaninetti testified that trucks are competitive with rail on coal shipments of 100 miles or less, Vaninetti RVS at 504-507, assuming that rail rates to Stout are \$2 per ton less than corresponding truck rates, and that it costs \$2 per ton more to load and unload coal from rail than from trucks. See Vaninetti RVS at 500; Vaninetti dep. at 43-44, 164, 174-76. The error in Mr. Vaninetti's position is that he focused on coal movements from Farmersburg to Stout, Vaninetti dep. 134, 180-81, and even on those movements he had not determined going truck rates, or the relative costs of loading or unloading coal by rail versus truck. Id. at 19, 23, 128-29, 133, 167-68, 174-

INRD claims once to have adjusted its rates to meet the threat of truck competition at Stout in connection with movements of coal from the Farmersburg mine.¹⁸ But IPL's isolated threat to meet some of its coal needs by trucks does not prove that truck movements are competitive with rail movements at Stout.

The Farmersburg mine supplies Stout with one-third of its coal requirements.¹⁹ Farmersburg is served by one railroad, CP Rail System ("CPRS").²⁰ All-rail movements of coal from Farmersburg originate at the mine on CPRS, with a connection to INRD at Linton, and then on INRD directly into Stout.²¹

Trucks may compete for Stout's coal movements from Farmersburg, but only in the sense that [[

]].²² In negotiations with INRD, IPL threatened to take

76, 180-81. Mr. Vaninetti's testimony thus pertains only to competition at Farmersburg, from which Stout receives one-third of its coal. Id. at 181; Weaver RVS at 9. Worse yet, Mr. Vaninetti's critical assumptions are no more than guesswork. Under the circumstances, Mr. Vaninetti's testimony is entitled to no weight.

¹⁸ Hoback dep. at 220-21; but see Weaver RVS at 8-9 (suggesting that [[

]]).

¹⁹ Hoback RVS 197HC; Vaninetti dep. 114-17, 181, 208 (78 truck miles); Weaver RVS at 9.

²⁰ See Weaver RVS at 10; Knight dep. at 13-15; Vaninetti dep. at 235-236.

²¹ See Hoback RVS at 196.

²² See Knight dep. 13-15; cf. Weaver RVS at 10; Crowley RVS at 16 ([[

coal deliveries from Farmersburg to Stout by truck, but that threat simply meant that rail rates from Farmersburg were so high that trucks had become a viable alternative, and that IPL would turn to trucks for coal deliveries on the Farmersburg-Stout route if the CPRS/INRD rate was not reduced below the prevailing truck rate.²³ IPL's threat worked, the current situation being that Stout takes its coal deliveries from Farmersburg by rail,²⁴ which means that even on this relatively short route truck rates are higher than rail rates.

In sum, the proposed transaction will eliminate INRD's only competition at Stout. As Conrail disappears, Stout will become a 2-1 plant. INRD (CSX) then will have incentives to raise its rates to near monopoly levels, up to the point where truck competition just begins to constrain these rates. Applicants propose to remedy this situation by granting trackage rights to NS. As explained in detail below, Applicants' proposal is deficient because the trackage rights they propose do not remedy the adverse competitive effects from the transaction; i.e., they do not grant to NS the means to assume Conrail's position as an effective competitor with CSX at Stout.

B. Potomac Electric Power Company

PEPCO operates four coal-fired plants, each served by a

]]).

²³ See Knight dep. 12-15.

²⁴ See CSX/NS-178 at 111; Hoback dep. 131-32.

single railroad that supplies that plant's full supply of coal. None of these plants receive any coal deliveries by barge or by truck. The proposed transaction likely will reduce competition for coal shipments to PEPCO's two most efficient plants at Dickerson and Morgantown, Maryland.

The Dickerson plant is served by CSX from CSX-served origins in northern West Virginia.²⁵ It consumed 1.2 million tons of coal in 1996.²⁶ Morgantown is on the Potomac River in Charles County, Maryland.²⁷ It consumes some 2.5 million tons of coal annually, which PEPCO purchases from CSX-served origins in northern West Virginia and Conrail-served origins in west-central Pennsylvania.²⁸

Dickerson and Morgantown are by far PEPCO's two most efficient and heavily utilized plants.²⁹ Dickerson operated at a capacity factor of 67.7% in 1996, while Morgantown operated at 70% that same year, and of the four PEPCO plants, these two had the lowest fuel costs and total expenditures per KWH.³⁰

²⁵ Felton VS at 6 (PEPC-4).

²⁶ Felton VS at 6; Woodward VS at 9.

²⁷ Felton VS at 5.

²⁸ Felton VS at 5-6, 8-9; Woodward VS at 9. Since movements of coal by truck would involve transloading from rail, and then a long haul through congested urban areas, truck movements are not likely to provide competition at PEPCO's plants. Woodward VS at 20.

²⁹ Woodward VS at 9.

³⁰ Woodward VS at 9, 23.

Dickerson's and Morgantown's relatively high efficiencies mean that these two plants are each other's closest substitutes, which means that PEPCO readily can substitute power from Conrail-served Morgantown for power from CSX-served Dickerson, and vice versa.³¹ As a consequence, PEPCO likely could defeat an anticompetitive rate increase by CSX at Dickerson if it were to threaten to alter its dispatch priorities; i.e., PEPCO could insist that if CSX does not reduce its rates at Dickerson, PEPCO will produce less power at Dickerson, and shift that generation to Morgantown. Similarly, PEPCO could defeat an anticompetitive rate increase by Conrail at Morgantown if it threatened to alter Dickerson's dispatch priorities in favor of Dickerson. In this way, PEPCO can prompt CSX and Conrail to constrain each other from imposing significant price increases in the future on coal shipments to Dickerson and Morgantown.³²

Pursuant to the proposed transaction, however, CSX is to acquire the Conrail line to the PEPCO Morgantown and Chalk Point plants. At the utility level, PEPCO will face a 3-2 situation, but PEPCO will not really become a 3-2 shipper. CSX will become sole provider of transportation services at Dickerson and

³¹ See Woodward VS at 22-23.

³² See Woodward VS at 22-23. This theory of anticompetitive effect is not inconsistent with PEPCO's contentions. It is PEPCO's stated view that Conrail's ability to provide service to the Morgantown and Chalk Point plants "constrains (and has constrained)" CSX's pricing at Dickerson. PEPCO Response to CSX Interrogatory No. 29 (First Set). That is precisely our point.

Morgantown, and so after the transaction PEPCO will not be able to constrain increases in CSX rail charges by substituting generation between these plants.³³ PEPCO, in essence, will become a 2-1 shipper, and CSX, as the monopoly railroad, would then be able to substantially increase its rail rates to PEPCO.³⁴

Applicants argue that PEPCO is not a 2-1 shipper, on the theory that the relevant market for PEPCO's purposes is the entire PJM Interconnection Association ("PJM") power pool.³⁵ Applicants also argue that PEPCO could constrain CSX's pricing after the transaction by installing facilities to receive and unload coal by barge at Morgantown.³⁶ On both these points, Applicants are incorrect.

PEPCO is a member of PJM, but PJM does not provide competition at PEPCO's plants sufficient to constrain CSX's rates. PJM's peak prices for power, and even its on-peak average, and overall average prices are considerably higher than PEPCO's variable costs for generating power at its own stations, and so it costs PEPCO much less to produce power than to purchase it from the interconnection network.³⁷ Transmission constraints and the unavailability of power during periods of peak demand

³³ See Woodward VS at 22-23.

³⁴ See Woodward VS at 22-23.

³⁵ See CSX/NS-176, Volume 1 at 424-425.

³⁶ See CSX/NS-176, Volume 1 at 428.

³⁷ Woodward VS 10, 13.

also restrict competition that might otherwise be available from the network.³⁸ Evidence in this record of particular sole-served generating stations paying significant premiums to the monopoly railroad further demonstrates that network competition cannot effectively constrain a railroad with market power.³⁹ Indeed, the Board has acknowledged as much in its numerous decisions granting relief to utilities faced with railroad market power. See, e.g., UP/SP at 185 (Entergy); Burlington Northern Inc., et al. -- Control and Merger -- Santa Fe Pacific Corporation, et al., Finance Docket No. 32549 (served August 23, 1995) at 68.

As to PEPCO's barge option, the Morgantown plant is situated on the Potomac such that PEPCO in theory could build a barge unloading facility at that plant. Were such a facility in place, NS-origin Central Appalachian coals could move via rail to NS' coal transloading terminal at Lambert's Point near Norfolk and then to Morgantown via barge.⁴⁰

That PEPCO could build a barge unloading facility at Morgantown is a necessary but not sufficient condition for constraining CSX's prices after the transaction. The ultimate question is whether PEPCO would build a facility that would be timely, likely, and sufficient in its magnitude, character, and scope to deter or counteract the competitive effects of concern

³⁸ Woodward VS at 12-13.

³⁹ Woodward VS at 10.

⁴⁰ Felton VS at 19.

in the post-transaction environment. See Horizontal Merger Guidelines § 3.0.

Using barges to deliver coals at Morgantown would entail building a barge unloading facility, and [

]].⁴¹ The barge unloading facility itself would cost [[
]].⁴² [[

]].⁴³ Dredging of the Potomac may also be required, especially to accommodate larger barges.⁴⁴ Independent of capital costs, loading costs associated with such a transload would increase the variable cost of supplying coal to PEPCO by about [[]] per ton.⁴⁵

It would take at least three years to build the facility, and the necessary permits might be difficult if not impossible to obtain from the Corps of Engineers.⁴⁶ Perhaps most important, investing in the barge option would not necessarily produce competitive rates. Last year, for example, NS' quoted rate for delivering coals to Lambert's Point simply was not low enough to

⁴¹ Woodward VS at 20; [[
]]).

⁴² Woodward VS at 20; [[
]]).

⁴³ [[

]].

⁴⁴ See Woodward VS at 20.

⁴⁵ Woodward VS at 20-21.

⁴⁶ Woodward VS at 20-22.

make the barge option worthwhile for PEPCO.⁴⁷

These facts demonstrate that PEPCO is not likely to be building a barge unloading facility at Morgantown any time soon after the transaction. That being the case, the barge option is not likely to serve as effective a constraint on CSX's pricing as does the current Conrail all-rail option to Morgantown.⁴⁸

Applicants rely on CSX witness Robert Sansom for their argument that PEPCO has a credible barge option at Morgantown. Sansom's reasoning, however, is seriously flawed. [[

⁴⁷ Woodward VS 21-22; see also [[]].

⁴⁸ See [[]]; Kaplan VS at 15-16 (PEPC-4); Woodward VS at 20-22. PEPCO threatened to construct a barge unloader during negotiations with Conrail in late 1993, Felton VS at 20, but that threat does not establish the feasibility of a barge option for PEPCO after the proposed transaction. [[

]]. In 1993, PEPCO could have moved NS-origin coals via barge to Morgantown as described above. PEPCO also could have moved CSX-origin Central Appalachian coals by rail to Newport News or Baltimore, and then to Morgantown via barge. Felton VS at 19. Indeed, CSX appeared more interested than NS in participating in a joint movement via barge. In addition, CSX has better access to coals that PEPCO may need in order to comply with Phase 2 of the Clean Air Act. See Felton VS at 9-10, 19-21; [[

]]. Based on these facts, [[

]].

]] does not take into account the substantial costs that PEPCO would incur in moving coals from Baltimore to Morgantown, in unloading the coals at Morgantown, or the amortized costs of the barge unloading facility and the barges. Moreover, NS and CSX are the only two railroads that can deliver coal to Baltimore, and [[]].⁴⁹

At bottom, CSX's acquisition of Conrail's line to the PEPCO plant at Morgantown will eliminate entirely the competition that PEPCO now enjoys at Morgantown and Dickerson, a competitive problem that PEPCO cannot ameliorate or constrain by turning to the PJM power pool or to its barge option. Under the circumstances, the Board should impose appropriate conditions to remedy this situation, as described in more detail below.

C. PSI Energy, Inc.

PSI Energy, Inc. ("PSI"), a subsidiary of Cinergy Corporation, is an electrical utility company serving customers in Indiana, Ohio, and Kentucky. PSI operates a number of coal-fired power plants, including its Gibson plant at Carol, Indiana.

⁴⁹[[]]. Sansom also refers to a PEPCO "Shore Erosion Project," recently approved by the Corps of Engineers, as if that tends to establish the feasibility of the PEPCO barge option. See Sansom RVS at 414 (CSX/NS-177, Volume 2B). PEPCO efforts to breathe new life into the Potomac bear no resemblance to the building of a barge unloading facility, and provide no support for the notion that the two projects would be similarly acceptable to the Corps of Engineers.

Much of Gibson's coal comes from the Cyprus-Amax mine in nearby Keensburg, just across the Illinois border. NS originates and delivers the Cyprus-Amax coal to Gibson over the only active rail line to Carol.⁵⁰ According to the Applicants' primary application, Conrail has trackage rights over this line, and so it competes with NS in delivering coal from Keensburg to Gibson. Pursuant to the terms of the proposed transaction, however, Conrail would transfer its Keensburg-Gibson rights to NS, thus eliminating the Conrail-NS competition that PSI now enjoys at Gibson.

Applicants argue that the fundamental premise in the Department's analysis of the Gibson situation is wrong because the trackage rights that permitted Conrail to deliver coal from the Cyprus-Amax mine to Gibson were "contractually canceled" on October 24, 1996, when NS accepted Conrail's August 29, 1996, proposal to terminate the trackage rights. CSX/NS-176, Volume 1 at 78HC. Because Conrail had given up these trackage rights, Applicants argue that Gibson "simply is not a 2-1 point." *Id.*

Statements by the Applicants in their primary application indicate that Conrail has trackage rights on NS between the Cyprus-Amax mine and Gibson. CSX/NS-18, Volume 1 at 39; CSX/NS-20, Volume 3B at 139; CSX/NS-25, Volume 8B at 101 and Volume 8C at 793-95. The Department relied on those statements in conducting its competition analysis. The application has not

⁵⁰ Woodward VS at 6-7.

been amended to conform with the position taken by the Applicants in their Rebuttal papers. Nor has Conrail or NS filed with the Board a notice of their intention to terminate these trackage rights pursuant to the provisions of 49 U.S.C. § 10903-10905, and the rules and regulations governing discontinuance of trackage rights as set out in 49 CFR § 1152.

Notwithstanding Applicants' prior statements, if the NS-Conrail termination agreement as finally executed by NS on October 24, 1996, is valid, then it cannot be said that the Gibson plant would become a 2-1 point as a result of the proposed transaction. The Department therefore will not continue to press for a remedy at Gibson if the termination agreement is valid. However, if the agreement is not valid, then Gibson would become a 2-1 point and would suffer a significant reduction in competition after the transaction.⁵¹ In that case it would be appropriate for the Board to remedy the situation by requiring CSX rather than NS to receive Conrail's trackage rights on NS from Amax's Wabash Mine near Keensburg, Illinois, to the Gibson power plant.⁵²

VI. REMEDIES ARE REQUIRED TO ADDRESS LIKELY COMPETITIVE HARM

For the reasons set forth above, the proposed transaction is likely substantially to lessen competition in at least two significant coal markets. The Board should require conditions

⁵¹ Woodward VS at 14-15.

⁵² Woodward VS at 24.

that resolve the competitive problems before approving the transaction. In imposing conditions, the Board may order that the Applicants grant trackage rights to other carriers. Although trackage rights do not always provide an effective remedy, they appear to be appropriate in this case. Here the trackage rights that would resolve the competitive problems would be limited in scope, would cover a very small portion of the transaction, and would not reduce the benefits of the transaction.

A. Conditions Required at IPL

Pursuant to the terms of the proposed transaction, CSX will acquire Conrail's lines into Indianapolis, thereby eliminating the CSX-Conrail competition that IPL now enjoys at its Stout plant. Applicants propose to remedy this 2-1 situation by granting NS trackage rights over CSX, with all NS traffic being routed through the Hawthorne Yard, where NS would have to depend on CSX for switching to NS customers such as IPL. CSX/NS-25, Volume 8C at 501-25. While this remedy may appear to permit NS to assume Conrail's position, it is seriously flawed because NS is not granted the same means that Conrail now has at its disposal to compete with CSX at Stout.

At present, IPL-Stout receives its coals from Indiana mines, all of which are within 110 miles to the south of the plant. Conrail serves Stout in a joint movement with ISRR. Under the remedy proposed by Applicants, NS would not have Conrail's convenient access to Indiana coal because it cannot connect with

ISRR at Indianapolis as does Conrail.⁵³ NS could deliver Indiana coal to Stout by interlining with ISRR, or CPRS, or CPRS and ISRR, or it could deliver coal to Stout from NS-served mines in Illinois or Kentucky, but all of these routes involve considerable circuitry, such that each of them is at least twice as long (in rail miles) as Conrail's current route to Stout.⁵⁴ As Dr. Woodward has testified, this doubling of the distance that NS must travel to serve Stout means significantly higher costs for NS, which most likely would be reflected in NS rates to Stout as much as 20-30% higher than present Conrail rates.⁵⁵

Under Applicants' remedy, NS would also be faced with operational problems that Conrail has been able to avoid. At present, on ISRR/Conrail movements into the Indianapolis terminal area, INRD uses its power and crews to "switch" cars from an interchange with Conrail into Stout.⁵⁶ When NS assumes Conrail's position, Applicants propose to route NS traffic through Hawthorne Yard, for switching by CSX into Stout. Hawthorne Yard may be congested, and so the NS-CSX interchange is likely to be worse than the current interchange between Conrail and INRD.⁵⁷ There is also the potential for CSX to use biased dispatching or

⁵³ Woodward VS at 16.

⁵⁴ Woodward VS at 16; see Neuman VS at 5 (ISRR-4).

⁵⁵ See Woodward VS at 16-17.

⁵⁶ See Hoback dep. 38.

⁵⁷ Crowley VS at 14 (IP&L-3, Exhibit 4); Woodward VS at 17.

excessive switching fees to impede NS' ability to compete.⁵⁸

Conrail too depends on its competitor (INRD) for switching services to Stout, but Conrail has an important lever that NS will lack, and that is the ability to receive a build-out from Stout. IPL believes that it could build out to the nearby Conrail branch line for approximately \$[[]], or it could build out to Conrail's Indianapolis Belt Railroad for approximately \$[[]].⁵⁹ Were there a build-out, IPL could bypass INRD, and so the mere threat of the build-out has ensured INRD's cooperation in switching Conrail cars to Stout, which has enabled Conrail to compete with INRD at Stout.⁶⁰

In short, Applicants' remedy will not replicate current competitive conditions for IPL at Stout because it does not put NS and INRD on equal footing. The Board could maintain the competitive status quo after the proposed transaction simply by granting NS the same access to ISRR and INRD that Conrail now enjoys. Hence the Board should grant NS rights to connect with

⁵⁸ Crowley VS at 14; Woodward VS at 17.

⁵⁹ Woodward VS at 17-18; see also Anacker VS generally (IP&L-3, Exhibit 3); Crowley VS at 8; Crowley RVS at 28-29; Porter VS generally (IP&L-3 (Exhibit 2); Weaver VS at 12 (IP&L-3 (Exhibit 1); Weaver RVS at 19-22.

⁶⁰ Weaver RVS at 21-22; Woodward VS at 18. There is no support in the record for Applicants' assertion that Stout's build out to Conrail would not be feasible. CSX/NS-176, Volume 1 at 57HC. CSX witness Thomas Kuhn has a few quibbles about IPL's cost estimates, but he does not say the build out is infeasible. See Kuhn RVS, CSX/NS-177, Volume 2A at 306-324. Even if Mr. Kuhn's higher cost estimates were accurate, IPL remains of the view that the build-out is feasible. Weaver RVS at 19-21.

ISRR at MP 6 southwest of Stout, to run over CSX tracks to INRD, and to run over INRD tracks to Stout, without interchanging with INRD at Hawthorne yard. The Board should also grant NS rights to run over CSX tracks to serve any build-out that IPL might make to any existing Conrail line. With these rights, NS could effectively compete with INRD at Stout. These rights would address Stout's 2-1 situation, and they are narrowly tailored to remedy that anticompetitive effect. See UP/SP at 144-45.

B. Conditions Required at PEPCO

Under the terms of the proposed transaction, CSX will acquire Conrail's line into PEPCO's Morgantown and Chalk Point plants, thereby eliminating the CSX-Conrail competition at both the Dickerson and Morgantown plants. This competition could be fully preserved if the Board were to require as a condition that NS rather than CSX acquire the Conrail line. Alternatively, the Board could grant to NS trackage rights on CSX so that it too can serve the Morgantown and Chalk Point plants. While less than full relief, this remedy would be less intrusive, yet permit NS, as the second railroad, to constrain CSX's rates at Dickerson and Morgantown, both of which otherwise would be captive to CSX. See Woodward VS at 24-25.

CONCLUSION

The record evidence in this proceeding demonstrates that the proposed transaction effectively will result in a monopoly in two, and perhaps three markets. Accordingly, the Department urges the Board to impose appropriate conditions as specified in this final brief to ameliorate or eliminate this loss of competition.

Joel I. Klein
Assistant Attorney General
Antitrust Division

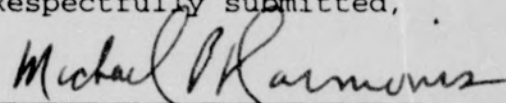
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Respectfully submitted, .


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February 23, 1998

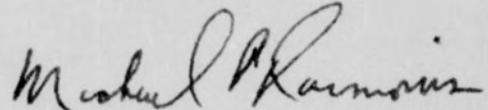
Before the
Surface Transportation Board
Washington, D.C.

Finance Docket No. 33388

CSX Corporation and CSX Transportation, Inc.,
Norfolk Southern Corporation and
Norfolk Southern Railway Co.
--Control and Operation Leases/Agreements--
Conrail, Inc. and Consolidated Rail Corporation

CERTIFICATE OF SERVICE

I certify that I have this 23rd day of February, 1998,
caused to be served copies of the BRIEF OF THE UNITED STATES
DEPARTMENT OF JUSTICE (DOJ-2) on Administrative Law Judge Jacob
Leventhal, counsel for the Applicants, and all other Parties of
Record on the official service list by first-class mail or by
more expeditious means.



Michael P. Harmonis
Attorney

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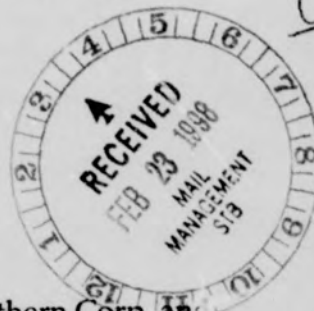
U.S. Department of
Transportation
Office of the Secretary
of Transportation

GENERAL COUNSEL

400 Seventh St., S.W.
Washington, D.C. 20590

February 23, 1998

Vernon A. Williams, Secretary
Surface Transportation Board
Suite 700
1925 K Street, N.W.
Washington, D.C. 20423-0001



Re: CSX Corp. and CSX Transportation, Inc., Norfolk Southern Corp. and
Norfolk Southern Railway Company -- Control and Operating Leases/
Agreements -- Conrail, Inc. and Consolidated Rail Corp.,
Finance Dkt. No. 33388

Dear Secretary Williams:

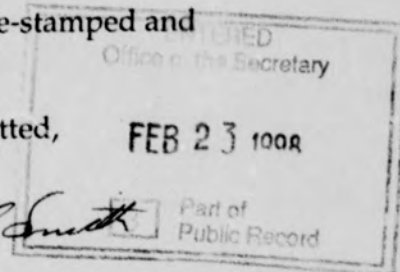
Enclosed herewith are an original and twenty-five copies of the Brief of the
United States Department of Transportation in the above-referenced proceeding.
As requested, this document is also contained in an enclosed a computer
diskette, formatted for WordPerfect 6.0.

I have also enclosed an additional copy that I request be date-stamped and
returned to the messenger.

Respectfully submitted,

Paul Samuel Smith

Paul Samuel Smith
Senior Trial Counsel



Enclosures

cc: Parties of Record

185873

ORIGINAL

DOT-6

Before the
Surface Transportation Board
Washington, D.C.



CSX CORPORATION AND CSX TRANSPORTATION, INC.,)
NORFOLK SOUTHERN CORPORATION AND NORFOLK)
SOUTHERN RAILWAY COMPANY -- CONTROL AND) Finance Docket 33388
OPERATING LEASES/AGREEMENTS -- CONRAIL INC.,)
AND CONSOLIDATED RAIL CORPORATION)

**BRIEF OF THE
UNITED STATES DEPARTMENT OF TRANSPORTATION**

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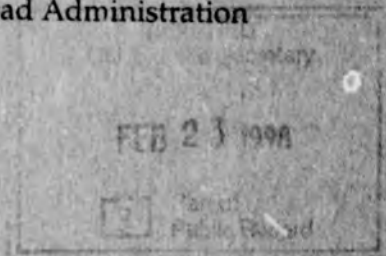
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February 23, 1998



ORIGINAL

Before the
Surface Transportation Board
Washington, D.C.



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**BEFORE THE
SURFACE TRANSPORTATION BOARD
WASHINGTON, D.C.**

)

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**BRIEF OF THE
UNITED STATES DEPARTMENT OF TRANSPORTATION**

I. INTRODUCTION

This proceeding will change the face of rail transportation in the eastern United States. Two of the major Class I rail carriers in the East are seeking to acquire and divide up the third. In the consideration of such transactions, it is the role of the United States Department of Transportation ("DOT" or "Department") to provide "leadership in identifying and solving transportation problems" as well as "in the development of transportation policies and programs." 49 U.S.C. §§ 101(b)(5) and 301(2), respectively. In carrying out this general responsibility the Department seeks to promote the long-term development of a balanced transportation system to serve the nation. DOT's participation in this and similar proceedings is one critical element in that effort.

The Department carefully scrutinizes proposed railroad consolidations to ensure that they are consistent with the public interest. The instant transaction, if approved, would leave two principal rail systems covering the entire eastern United States. It is the first consolidation in the East since the early 1980's, and follows a long series of rail mergers in the West, all of which DOT has closely evaluated in order to determine their public interest impacts. The impacts from this transaction

would extend to competition and service to shippers as well as to other critical subject areas, including the prospect for significant effects on safety, numerous communities, and rail passenger transportation. We have addressed such matters at length in prior filings in this proceeding, but because of their importance they will be noted briefly herein as well.

Finally, it must be underscored that rail consolidation proceedings require a "forward-looking assessment."¹ That is inevitable, for the Board in these cases is attempting to review the likely effects of a proposed -- not a completed -- transaction as the agency determines its consistency with the public interest. The scope of that interest is broad indeed, embracing a transaction's impacts on intramodal competition "in the national rail system." See 49 U.S.C. § 11324(b)(5). The law and sound policy combine, therefore, to necessitate that the pending transaction be considered not only in the context of the present composition of the railroad industry in the United States, but also in light of the influence it may have on that industry in the foreseeable future.²

A. The Proceedings to Date

By application filed June 23, 1997, CSX Corporation, CSX Transportation, Inc. (collectively, "CSX"), Norfolk Southern Corporation, Norfolk Southern Railway Company (collectively, "NS"), Consolidated Rail Corporation, and Conrail, Inc. (collectively, "Conrail") have sought approval from the Surface Transportation Board ("STB" or "Board") for: (1) the acquisition by CSX and NS of control of Conrail, and (2) the division of the assets of Conrail by and between CSX and NS.³ 49 U.S.C. §§ 11323 - 25.

CSX operates approximately 18,500 route miles in 20 states east of the Mississippi River and in Ontario, Canada. CSX serves almost every major metropolitan area in this vast region, including Chicago, St. Louis, Memphis, New Orleans, Philadelphia, Atlanta, Detroit, Washington, and Miami, as well as many

¹/ Santa Fe Southern Pacific Corp. -- Control -- SPT Co., 2 I.C.C. 2d 709, 744 (1986) ("SF/SP").

²/ DOT notes, for example, that the Canadian National and Illinois Central railroads have already announced plans to merge.

³/ Conrail, CSX, and NS are referred to collectively herein as "Applicants."

other points. Major commodities transported on CSX include coal, automobiles and automobile parts, and chemicals; CSX is also a major carrier of container traffic.

NS operates more than 14,200 route miles, also in 20 states and in Ontario. NS serves virtually every major market from Kansas City to Norfolk, Virginia and from New Orleans to Buffalo, New York, including Chicago, Memphis, St. Louis, Detroit, Cincinnati, Cleveland, Atlanta, and many other points. Major commodities carried by NS include chemicals, coal, grain, and intermodal traffic.

Conrail operates approximately 10,500 miles of track in the Northeast and Midwest. Its primary network forms a rough "X" connecting Chicago, Indianapolis, and St. Louis in the West with Boston, New York, Baltimore, and Washington in the East; the major lines of this system intersect in the Cleveland, Ohio area. Conrail also serves Pittsburgh, Philadelphia, and Montreal, Canada. Major commodities hauled by Conrail include coal, metals and metallic products, and intermodal traffic.

Following a series of competing bids for Conrail tendered by NS and CSX, the Applicants ultimately agreed that NS and CSX would pay approximately \$10 billion for all of Conrail's common stock. That stock is now held in a voting trust. The Applicants further agreed to a detailed division of Conrail's assets whereby NS and CSX would both expand their systems by thousands of miles of track and reach geographic areas they have not previously served. *See CSX/NS-18, Verified Statement ("VS") of McClellan at 527-44; NSX/NS-19, VS Kalt at 3-26.*

In an unprecedented arrangement, the Applicants have agreed that both NS and CSX, as well as Conrail (in truncated form), will operate in so-called Shared Asset Areas ("SAAs") in northern New Jersey, southern New Jersey (including Philadelphia), and Detroit. CSX/NS-18, at 3-5, 46-49.⁴ The division of assets includes a division of existing contracts between Conrail and shippers: those that entail transportation services that can only be performed by either NS or CSX (but not both) after consummation of the transaction will be assumed by that carrier, and those that could be handled by both CSX and NS after consummation will be allocated by the two carriers between themselves. The Board accepted the application for consideration by Decision No. 12, served July 23, 1997.

⁴/ The Applicants also propose to establish similar areas in which both CSX and NS will operate; these include the Monongahela coal fields in Pennsylvania and West Virginia, and a port facility in Ashtabula Harbor (Ohio) on Lake Erie. CSX/NS-18 at 49-52.

Mindful of these complicating factors and the densely populated and heavily industrialized areas into which NS and CSX would be expanding, the Board required the preparation of an environmental impact statement ("EIS"), in fulfillment of its obligations under the National Environmental Protection Act, ("NEPA"). 42 U.S.C. §§ 4231 *et seq.*; Decision No. 6, served May 30, 1997. A staff unit of the STB, the Section of Environmental Analysis ("SEA"), with input from the Applicants and many interested public and private parties, issued a draft environmental impact statement ("DEIS") on December 12, 1997. The DEIS attempted to identify the likely effects of the transaction on many aspects of the human environment, including railroad safety, communities facing increased rail traffic, and rail passenger carriage. On February 2, 1998, numerous parties, including DOT, submitted comments on the DEIS. The SEA is now preparing a final EIS to recommend to the Board; it is scheduled to be complete in April or May of this year.

B. The Positions of the Parties

The Applicants submit that the pending transaction will bring the public substantial benefits in the form of extended single line service, increased intramodal and intermodal competition, reduced pollution (primarily through the diversion of traffic from motor carriers), and enhanced vehicular and rail operating safety. CSX/NS-18 at 16-18, 22, and VS Goode at 331-38, VS Snow at 311-18. They quantify the value of these benefits at over \$1 billion. The application is supported by 14 states, 85 railroads, hundreds of public officials, and thousands of shippers.

The Applicants also contend that they have remedied the few areas in which rail competition would otherwise suffer from the acquisition, that their operations will not adversely affect intercity or commuter rail passenger service, and that they have met most of the major concerns expressed by some shippers through an agreement with the National Industrial Transportation League ("NITL"). NS and CSX have also criticized significant portions of the DEIS. *See* NS Comments on DEIS (undesigned); CSX Comments on DEIS (undesigned).

Other parties dispute this view of the nature and extent of the application's impact. Numerous public and private bodies contend that, by introducing railroad competition to shippers located within the SAAs, the transaction threatens to disadvantage shippers outside of these favored areas, who will continue to receive service from only a single carrier. *E.g.*, the Erie-Niagara Rail Steering Committee, the New York Economic Development Corporation, and the Coalition of Northeast

Governors. Such parties seek the creation of additional SAAs or their equivalent to restore the competitive equilibrium.

The United States Department of Justice ("DOJ") acknowledges that the transaction would create new competition, but it also identifies three markets involving coal-fired power plants that would lose rail competition. Several utility companies (e.g., Indianapolis Power & Light ("IPL") and Potomac Electric Power Company ("PEPCO")) expressed substantially identical concerns, as did parties in the Toledo, Ohio area (e.g., AK Steel and the Toledo-Lukas County Port Authority).

Other shipper organizations and their members emphasize that the competitive bidding between NS and CSX ultimately resulted in their payment of billions of dollars in excess of the original prevailing market price for Conrail's stock. E.g., NITL-7 at 15-27 (National Industrial Transportation League), 42-48; GPU-02, VS Crowley at 6-22 (GPU Generation, Inc.); ACE, et al.,-18 at 32-49.⁵ They are concerned that in order to service the debt on this enormous "acquisition premium," NS and CSX will seek to raise rates or reduce service to shippers that do not enjoy the benefit of intramodal or intermodal competition. *Id.* Such parties would have the Board exclude the premium from NS and CSX regulatory cost bases, so that the premium would not affect calculations of their revenue adequacy or the outcome of rate reasonableness cases involving these carriers. *Id.*

The NITL originally expressed significant concern with a number of aspects of the transaction, including the loss of single-line service by some shippers, the allocation of contracts between NS and CSX, and doubts about the viability, accountability, and safety of operations by multiple railroads in the SAAs. An agreement with the Applicants has caused NITL to withdraw its opposition in each of these areas. CSX/NS-176, Appendix B. This agreement preserves for three years rail rates for shippers losing single-line service, provides arbitration for shippers dissatisfied with the service of the carrier to whom their contracts with Conrail are assigned, requires CSX and NS to provide additional information and take specific steps in preparation for operations in the SAAs, imposes reporting requirements, and proposes a three year oversight period by the Board. *Id.* NITL, however, has reserved its right to continue to try and negate the perceived effects of the financial

⁵ / Atlantic City Electric Co. and Indianapolis Power & Light initially submitted joint filings using the "ACE" designation. Atlantic City Electric Co. subsequently withdrew from the case, but Indianapolis Power & Light has not.

premium paid for Conrail stock.

Although some commuter railroads have decided to support the application after reaching agreement with the Applicants (*e.g.*, the Massachusetts Bay Transportation Authority and the Maryland Department of Transportation), several other commuter operators and Amtrak continue to believe that the transaction could impair their ability to offer reliable service, to offer new service, or to extend their operations. *See* Virginia Railway Express Corp., New Jersey Transit Corp., and the Southeastern Pennsylvania Transportation Authority.

Most of the major rail labor organizations continue to oppose the transaction, including the Allied Rail Unions ("ARU"), the Transportation Communications International Union ("TCU"), the International Association of Machinists ("IAM"), and the Transportation Trades Department, AFL-CIO ("TTD"). They continue to express concerns about the personal, operational, and safety impacts of expected job reductions and forced relocations, abrogation of collective bargaining agreements, and dissatisfaction with what they perceive to be the increasingly illusory nature of traditional labor protection measures. *See* ARU-23; TCU-6; IAM-4; TTD-3. The Brotherhood of Locomotive Engineers ("BLE") and the United Transportation Union ("UTU") are the only rail unions that have offered support for the transaction.⁶

Several smaller (Class III) railroads contend that consummation of the transaction will divert sufficient traffic to jeopardize their ability to provide essential rail services to shippers.⁷ *E.g.*, Ann Arbor Railroad, New England Central Railroad, and Indiana Southern Railroad. For the most part these carriers request that the Board grant them trackage rights to gain access to new sources of revenue in order to prevent this outcome.

The Department in its participation to date has concentrated on the transaction's implications for rail safety. DOT-1 through DOT-5. Working with the Applicants, the Federal Railroad Administration ("FRA") has brought its safety expertise to bear in the production of detailed safety integration plans ("SIPs"). These documents and related commitments from the Applicants adequately address

⁶/ The UTU's support is conditional. UTU-6.

⁷/ An essential rail service is one for which there is sufficient public need but for which adequate alternative transportation is unavailable. 49 C.F.R. § 1180.1(c)(2)(iii)

safety concerns in DOT's view.

II. SUMMARY OF ARGUMENT

The pending transaction holds the prospect of expanding intramodal rail competition to an extent not seen before in rail consolidation proceedings. It poses relatively few competitive difficulties, although those that have been identified must be addressed. Operations in the Shared Asset Areas, through which much of this expansion is to take place, raise their own questions in some of the most important markets in the nation. Because these cannot now be answered with confidence, it is critical that the Board monitor developments in the SAAs, and consider corrective action should that become necessary.

The pending transaction also poses unprecedented potential impacts on safety, on community life, and on passenger rail operations. The Department has worked closely with the Applicants to ensure that safety remains the most important consideration in the implementation of their very complex integration plans. We have also reviewed those plans and found that the projected increases and reroutings of rail traffic may degrade the quality of life in particular communities in terms of health, noise, vehicular delays, and other indicia. The operation of freight and commuter and intercity passenger lines in the northeastern U.S. on the same tracks requires close coordination to ensure safe and reliable service. Prudence dictates a period of oversight to ensure that this cooperation continues.

As noted in our comments on the DEIS, DOT submits that the single best way to reduce or eliminate many of the potential adverse consequences at risk is to encourage the Applicants and the affected parties to continue to resolve potential problems among themselves. DOT-5. They have the most at stake and are most familiar with the circumstances in each case. Indeed, a significant number of private agreements already have been reached. But major points of contention continue to exist (particularly in the areas centered in Cleveland, Ohio and New York City), and the Board can and should encourage this process. Continued oversight is essential here, too, to gauge (and if necessary mitigate) the true impacts of the transaction and to protect the public interest in viable, efficient rail transportation.

Moreover, the application of standard labor protection measures in past merger cases has resulted in less protection than we believe was intended. DOT urges the Board to clarify the nature and extent of any approval it may grant here, so

that railroad workers are better able to negotiate agreements and secure the benefits that the law affords them.

Finally, shippers whose contracts with Conrail contain clauses that would otherwise prevent their assignment to CSX or NS should be able to choose which of these carriers actually performs the terms of the contracts, when either carrier can do so.

The Department concludes that the pending transaction can be rendered consistent with the public interest, and so warrant approval, by the judicious exercise of the Board's conditioning power. Traditional measures to restore lost competition are required. So, too, is a significant period of oversight. Only by the Board's retaining jurisdiction, monitoring the actual consequences of this most ambitious transaction, and remaining open to demonstrations of adverse impacts and imposition of mitigation measures, where appropriate, can the pending application be deemed consistent with the public interest.

III. APPLICABLE STANDARDS

Federal law requires the Board to approve consolidations involving Class I railroads that it finds to be "consistent with the public interest." 49 U.S.C. § 11324(c). Statutory provisions and agency precedent further define that broad standard.⁸ The statute expressly directs the STB in its consideration of the public interest to take into account the following factors in the context of a proposed merger: (1) the effect of the proposed transaction on the adequacy of transportation to the public; (2) the effect on the public interest of including or failing to include other rail carriers in the area involved in the proposed transaction; (3) the total fixed charges that result from the proposed transaction; (4) the interest of carrier employees affected by the proposed transaction; and (5) whether the proposed transaction would have an adverse effect on competition among rail carriers in the affected region or in the national rail system. 49 U.S.C. § 11324(b). See Finance Docket No. 32760, Union Pacific Corp., Union Pacific Railroad Co., and Missouri Pacific Railroad Co. --

⁸/ The Interstate Commerce Commission Termination Act created the STB and preserved Interstate Commerce Commission ("ICC") precedent and made that precedent applicable to the STB unless and until changed by the Board. Section 204(a) of P.L. No. 104-88.

Control and Merger -- Southern Pacific Transportation Co., St. Louis Southwestern Railway Co., SPCSC Corp., and the Denver & Rio Grande Western Railroad Co., Decision No. 44 (served August 12, 1996) (slip opinion) ("UP/SF") at 99; Finance Docket No. 32549, Burlington Northern, Inc. and Burlington Northern Railroad Co. -- Control and Merger -- Santa Fe Pacific Corp. and the Atchison, Topeka and Santa Fe Railway Co. (served August 15, 1995) (slip opinion) ("BN/SF") at 51; Finance Docket No. 32133, Union Pacific Corp. Union Pacific Railroad Co. and Missouri Pacific Railroad to - Control -- Chicago and North Western Transportation Co. and Chicago and North Western Railway Co. (served March 7, 1995) (slip opinion), ("UP/CNW") at 53; Finance Docket No. 32133, Union Pacific Corp., Union Pacific Railroad Co. and Missouri Pacific Railroad Co. -- Control -- Missouri-Kansas-Texas Railroad, 4 I.C.C. 2d 409, 426 (1988) ("UP/MKT"), *pet. for review dismissed sub nom., Railway Labor Executive Assn. v. I.C.C.*, 883 F.2d 1079 (D.C. Cir. 1989).

The statute also lists 15 elements that together establish as the nation's rail transportation policy an emphatic "reliance on competitive forces, not government regulation, to moderate railroad actions and to promote efficiency." UP/MKT, 4 I.C.C. 2d at 427 (citation omitted); *see also* BN/SF, slip op. at 52; UP/CNW, slip op. at 54. This reliance on competitive forces underscores the important role played by antitrust principles in the agency's consideration of merger cases.⁹ *See McLean Trucking Co. v. United States*, 321 U.S. 67, 87 (1944); BN/SF, slip op. at 52-53; UP/CNW, slip op. at 54; UP/MKT, 4 I.C.C. 2d at 427. While the Board (like the ICC before it) does not sit as an antitrust court, its obligations under the law's public interest standard require it to engage in a balancing of a transaction's potential public benefits against its potential public harms, including the loss of competition. Railroad Consolidation Procedures, 363 I.C.C. 784 (1981), *codified at* 49 C.F.R. § 1180.1.¹⁰

Public benefits derive from operating efficiencies and marketing opportunities that can make the consolidated carrier a more formidable competitor. BN/SF, slip op. at 51; UP/CNW, slip op. at 56; UP/MKT, 4 I.C.C. 2d at 428. Public

⁹/ The statute immunizes from the antitrust laws and other laws, as necessary, transactions approved by the STB. 49 U.S.C. § 11321(a).

¹⁰/ The STB in particular focuses on intramodal competition where long-haul movements of bulk commodities are concerned. 49 C.F.R. § 1180.1(c)(2)(i).

harm in merger cases historically has most often arisen from significant reductions in competition and serious threats to an unaffiliated rail carrier's ability to provide essential services. *Id.* In this proceeding, public harm is threatened in non-traditional ways as well.

Moreover, the Board has broad authority to impose conditions on its approval of a merger proposal in order to ensure that the public interest standard is met. 49 U.S.C. § 11324(c). Applicable precedent recognizes that conditions may reduce the benefits of a merger, however, and thus conditions are imposed to mitigate public harm only when specified criteria are met. In the face of merger-induced reductions in competition or a loss of essential services, corrective conditions are appropriate when they will (1) effectively ameliorate the adverse effects, (2) be operationally feasible, and (3) produce public benefits that outweigh any reductions they might engender in the public benefits produced by the transaction. Union Pacific -- Control -- Missouri Pacific; Western Pacific, 366 I.C.C. 459, 562-65 (1982) ("Union Pacific Case"); 49 C.F.R. § 1180.1(d)(1). See also BN/SE, slip op. at 55-56. These standards are also appropriate for mitigating environmental and other adverse effects of rail consolidations. See UP/SP, slip op. at 221-23; Finance Docket 32760, UP/SP Merger - Wichita Mitigation Study, Preliminary Mitigation Plan at 2-3, 2-4; UP/SP Merger - Reno Mitigation Study, Final Mitigation Plan at 2-2.

IV. THE PROPOSED TRANSACTION WARRANTS APPROVAL ONLY IF APPROPRIATE CONDITIONS ARE IMPOSED TO MITIGATE THREATENED PUBLIC HARM

As noted earlier, the pending transaction is unprecedented in many respects. The financial burdens undertaken, the implications of dividing one Class I railroad between two others and of introducing multiple rail carriers into areas long served by only one, would alone be sufficient to require unusual scrutiny. The fact that the effects of the transaction will be directly felt in some of the most densely populated, heavily industrialized communities in the nation only adds to the necessity for a most careful analysis. Because these effects include, but extend far beyond, the competitive sphere, so, too, must the proper scope of inquiry.

The Board has acknowledged this throughout the proceeding, by insisting upon an adequate procedural schedule, by directing the preparation of an EIS, and by requiring the submission of detailed safety integration plans to govern the

implementation of the Applicants' operations following any approval. These precautions have borne fruit; they have identified threatened harms to the public interest. Applicable precedent demands corrective conditions when a pending consolidation threatens harm to competition or essential services. So, too, in this case must the Board also mitigate harms to other facets of the public interest posed by the transaction. Only in this fashion can the application be rendered consistent with the public interest and warrant approval. The Department summarizes below the harm that, in our view, necessitates exercise of the STB's conditioning power.¹¹

A. Safety

The Department's primary concern in this proceeding has been to ensure that the proposed acquisition, if approved, will be implemented in a safe manner. FRA has been working with the Applicants to prepare and review the SIFs required by the STB, and to secure detailed commitments of the resources and steps necessary to implement them properly.

1. Corporate Culture

A railroad's attitudes and practices -- its "corporate culture" -- with respect to safe operations can be a cause for concern. When different cultures come together, as in the merger of two large carriers, the implications of failing to address individual deficiencies and to plan for a harmonious integration can be devastating. The performance of the Union Pacific railroad following its merger with the Southern Pacific stands as a stark example in terms of both safety and service.

In the Department's view, Union Pacific management took a primarily productivity-driven approach to implementing its merger, rather than one focusing on personal and corporate safety.¹² DOT-3, and VS of Edward English at 14. For example, dispatcher performance at UP was gauged by the number of train movements rather than the safety record of the operation. The manner and extent to which labor forces were reduced at the outset of the merger led to a shortage of over 1,500 train and engine, mechanical, dispatching and supervisory personnel and

¹¹/ DOT expresses no opinion on the issues in this proceeding not addressed herein.

¹²/ This course was also evident in the performance and safety problems which followed UP's 1995 acquisition of the Chicago and North Western railroad.

what has been described as a virtual "meltdown" in service performance. More significantly, these and other merger-related decisions led to several major incidents that resulted in injuries, loss of life, and property damage. *Id.* UP/SP has yet to fully recover from the consequences of these corporate culture-related problems.

DOT has therefore been extremely concerned about the corporate cultures of CSX and NS and the manner in which these carriers intend to implement their transaction following any approval that they receive from the Board. FRA expended substantial resources in preparing its formal Safety Assessment of CSX/NS Proposed Acquisition of Conrail. DOT-3, VS English. In addition to a detailed evaluation of the Applicants' proposed operating plans and an analytical risk assessment, FRA also closely examined the Applicants' differing corporate cultures.

As a result of a review of CSX practices conducted in 1997, FRA identified specific concerns with CSX's safety culture, including a lack of commitment to safety at the local supervisor level. *Id.* at 15. FRA also found a widespread perception by employees that harassment and intimidation existed at many locations on the CSX system. Similarly, NS historically has had a very strong sense of identity and confidence in corporate policies, which has been reflected in the company's attitude toward safety. This in some respects may have led NS management to hold rigidly to its own rules and practices, and a consequent failure to acknowledge that NS may not in every instance already follow the "best practices" in the industry.

DOT is pleased to report that the Applicants have made great improvements on this score. They have demonstrated their commitment to resolving the cultural problems by hiring several Conrail senior managers to work with CSX, NS, and in the SAAs. They have worked with FRA closely, they continue to do so, and they are to be commended. We offer below specific examples of their progress. Because FRA intends to monitor vigilantly the Applicants' safety performance, in our view safety is no longer an issue with which the Board need be concerned.

2. CSX

CSX has already established a "Safety Culture Planning Team" to review existing programs and possible new programs, and to lead a safety culture reinvention effort. The carrier has also pledged that within the first year following approval of the acquisition it will integrate the "best practices" of both Conrail and CSX related to safety cultures. CSX will adopt some form of Conrail's "B-Safe" safety program, which has been used by Conrail to effectively perform job,

behavioral, and environmental safety observations, identify problem areas, and communicate issues to personnel. CSX also pledged to develop a standardized safety cultural enrichment action plan based upon collaboration with rail labor and the FRA.

Moreover, CSX will implement a series of listening sessions with field managers and labor to better understand Conrail views on safety culture issues and to reinforce two-way communications. CSX is also developing an "ombudsman" process to document, handle, and follow-up on non-routine employee concerns, and plans to review its Operations Center with dispatchers, supervisors, and officers to develop an improvement plan. CSX plans to extend its existing Senior Staff Site Visit program to allocated Conrail territory starting in early 1998. CSX will pursue active training programs for all of its acquired forces from Conrail where training needs are identified. Finally, CSX will extend its "Employee Quality of Life" programs to Conrail-acquired personnel.

3. NS

NS has retained a safety consultant who has inspected Conrail facilities to be acquired by NS and who has offered recommendations for their integration. NS has adopted the "Six Tenets of Safety" identified by that consultant, and has pledged to incorporate them for all property to be acquired from Conrail. NS also appointed a Vice President with full time responsibilities for implementation planning. The carrier has established direct dialogue with Conrail officers through frequent observation and planning meetings, field trips, staff meetings, and the distribution of a publication to most Conrail employees every two months.

If the proposed acquisition is approved, NS plans to have in place prior to the closing date a new Northeast Region Safety Committee to represent the acquired Conrail lines. NS expects to quickly establish an umbrella committee system for the former Conrail district/local employee committees and divisional and regional committees. NS expects to honor for a time Conrail's commitments to a program rewarding its employees for superior safety performance ("Safety Shares"), and then extend its own Safety Incentive Plan in the first full calendar year after the closing date.

4. Safety Integration Plans

It bears repeating that the Applicants have worked closely with the FRA to produce the SIPs previously filed in this proceeding. With the use of merger-related Safety Integration Plan Guidelines developed by FRA specifically for this purpose, the Applicants have addressed all of the safety concerns identified by FRA. As noted, subsequent to the initial filing of the SIPs, a SIP review team (made up of FRA experts and representatives from each Applicant) has worked to prepare for the implementation of the SIPs by the Applicants under the supervision of FRA, in the event that the STB approves the proposed transaction. DOT wishes to emphasize again that each of the Applicants has cooperated fully with FRA and continues to do so, and we highly commend their efforts. The Department is now satisfied that each Applicant has systematically considered all potentially significant sources of increased safety risk, and has adopted sound procedures for implementing this transaction. Pursuant to its plenary safety oversight authority, FRA will continue to work actively with the Applicants throughout that process.

5. Safety and Service

Recent history and the circumstances of this case require that the Department join with the Applicants, shippers, and others in seeking to avoid service problems of the type that have occurred and that continue to occur in the western U.S. following the UP/SP merger. Severe congestion and related service difficulties have resulted largely from unanticipated complications with integrating the UP and the SP. The operating difficulties following the merger led directly to significant railroad safety shortfalls resulting in a sharp increase in rail accidents and fatalities.

Integrating two large organizations with different histories, cultures, and operating procedures presents a management challenge of the highest order. In the UP/SP case, provision of the most extensive trackage rights ever granted, instead of divestiture, may have contributed to the operational complexities resulting in both service and safety degradation.

The Department, in developing SIPs with both CSX and NS, has insisted on specific emphasis, identification, and resolution of operating culture issues. DOT believes that through its continued oversight of the SIP implementation process, we will have greater opportunities to identify operational concerns, as well as safety issues, prior to any negative impact on the public interest. The Department intends to work with the STB with regard to any such operational information developed

through the SIP process, in order to help assure that unforeseen contingencies do not overwhelm the most carefully prepared plans.

DOT is concerned that mitigation measures required to address various impacts of the pending transaction, particularly measures not arrived at by means of voluntary agreements, not become threats to safety or potential sources of disruption. In cases where rail service could suffer to a significant extent or where operational changes are deferred as the result of, say, construction of particular mitigation projects, there is a potential for creating bottlenecks with serious implications for national rail service and safety. The Department understands that the implementation of SIPs may need to be modified to address new safety issues presented by any such measures, and will work with the Applicants in this regard.

Assuming adoption of appropriate and feasible mitigation measures, the Board should clarify that it is the Applicants' responsibility to provide safe and reliable rail service from the first day of their operations.

B. Community Impacts

1. Ohio and Indiana

The record in this case identifies several communities concentrated in the Midwest (*i.e.*, Cleveland, Ohio and the surrounding area and northwest Indiana) that face the prospect of significant increases in rail traffic as a result of this transaction. The DEIS has documented the extent of some of the consequences of this commerce, but it has failed to locate several other communities in similar circumstances. DOT-5. DOT continues to urge the Board to do all that it can to encourage the Applicants and the affected communities to reach mutually satisfactory mitigation measures. There has been significant progress using this approach, and there is reason to trust that, properly nurtured, it will continue. Oversight is necessary, however, to ensure that all significant impacts have been addressed and properly mitigated. In some cases, as recognized by the Applicants themselves, this may require grade separations and other construction projects. DEIS, Appendix S.

In northeastern Ohio, DOT is concerned that an agreement be reached in a timely manner because this area is the key to the entire transaction. The major rail routes of Conrail being allocated to CSX and NS in this transaction form an "X," one leg of which is the Conrail lines from Boston and New York City (via Albany) to St.

Louis, and the other of which is the lines from New York (via Philadelphia) to Chicago. The cross-point of the Conrail "X" is in the Greater Cleveland area. One of the core concepts of the transaction's allocation of the Conrail routes is that CSX will take the first-named leg of the "X", and NS will take the other leg. The "X" will no longer be operated as part of a single system, but the two legs of the "X" will be operated on a competitive basis by the two carriers. CSX Comments on the DEIS, at 121.

In the aggregate, NS and CSX intend to operate approximately 120 trains per day on the two branches of the "X" through Cleveland. It should be noted that the pending transaction will not materially change the number of trains traversing Cleveland on "Day One" (although traffic may ultimately increase in Cleveland, as elsewhere, on the CSX and NS systems as the benefits of the transaction generate added business, including the diversion of freight from truck to rail). However, rather than operations at the center of the "X" being coordinated by a single railroad operating in its overall best economic interest, two rivals will be directing their competing services. These carriers have proposed operating plans and allocations of routes in the Cleveland area that will permit each of the two to operate without interference from the other. Were such interference to occur, however, there would exist the potential for a deterioration of service similar in scope and duration to that in the West following the UP/SP merger, and possibly more difficult to cure. *Id.* at 121-122.

The original application calls for CSX to operate in the Cleveland area principally over the Short Line and for NS to operate here principally over the Lake Shore Line. *Id.* NS would also continue to operate its existing line through Cleveland and the former Pennsylvania Railroad Line from Pittsburgh and Alliance, Ohio to the connection with the Lake Shore Line near downtown Cleveland. As a result of this allocation, several communities will see increased train traffic, in some cases substantially increased train traffic. The Applicants' original proposal would route CSX traffic over the Short Line, a line currently lightly used. Train traffic increases would impact neighborhoods in Cleveland and East Cleveland as well as certain sensitive areas in the University Circle area. NS traffic increases over its current route would affect neighborhoods in Cleveland, East Cleveland, Lakewood, Bay Village and Rocky River. This route has a large number of at-grade highway crossings.

NS has proposed to mitigate the problem caused by increases in its trains by

using certain connections in Cleveland and/or Vermilion, Ohio. DEIS, Appendix S. CSX has proposed noise mitigation for the Short Line operations in Cleveland and certain other measures in East Cleveland. The City of Cleveland has proposed to reverse or "flip" the original allocation of lines, giving NS the Short Line and CSX the Lake Shore Line. This option would reduce train traffic impacts from the Short Line in East Cleveland and adjacent areas of Cleveland, but would require an overpass in Berea, Ohio to separate the NS and CSX lines, since an at-grade crossing of the two rail lines (which would handle more than 100 trains a day) would not be practical.

Negotiations among the railroads and the various communities continue, and DOT sincerely hopes that they will reach agreement. While we have elsewhere stated our overall concerns about the Applicants' responsibility to provide safe and reliable rail service, it should be stressed that operations in the Cleveland area -- the center of the "X" where CSX and NS systems would intersect -- have potential consequences for safe and efficient rail service elsewhere in the nation.

The Department continues to urge the Board to clarify the mitigation required if agreements are not reached. As part of its consideration, the Board should assess the impact on the national transportation system of requirements or conditions that interfere with safe and efficient train operations. We also urge the STB to direct the Applicants and Cleveland area communities to exert their best efforts to reach agreements that would remedy the effects of the transaction in the larger Cleveland area. If agreement is not reached, of course, the Board as a condition of approval of the transaction should impose necessary measures to mitigate identified environmental impacts, without adversely affecting rail service and safety.

2. New York City

In the New York/New Jersey region, the transaction raises substantial public interest and environmental concerns. The Applicants contend that by providing railroad competition in northern New Jersey, the SAA will divert to rail certain long-distance truck traffic, thereby reducing congestion and air pollution in the eastern U.S. CSX/NS-18, VS Goode at 15; CSX/NS-176, at HC-13. This argument, however, fails to take into account the specific impacts of the transaction to the areas east of the Hudson River -- in particular New York City and Long Island.

In these communities, inadequate rail access (which the application does not remedy) means that the transaction is likely to prompt increased truck traffic in

already congested and environmentally degraded areas. For this reason, and in light of the strong public interest in maintaining and improving rail access to this populous region, the Department urges the Board to require the Applicants to work with affected communities to produce a plan to mitigate the transaction's adverse environmental impacts. If the Applicants and the affected communities cannot agree upon such a plan, the Board should order specific corrective action.

Approximately 12 million people live in areas of New York State east of the Hudson River. Trucking now has a virtual monopoly in freight transportation in this area of the State. The share of New York City, Long Island, and southern Connecticut intercity freight that travels by rail is 2.8 percent; by contrast, on a national basis rail handles a growing 40 percent of such traffic. Rebuttal Statements Submitted on Behalf of the Congressional Delegation (January 12, 1998) (undesigned) ("Congressional Rebuttal"), VS of Galligan at 13. This has significant environmental repercussions. According to statements by the Director of the Mayor's Office of Transportation for the City of New York,

nearly 50,000 trucks cross the City's bridges and tunnels daily. These trucks are then routed on only three major truck routes that must provide access to the New York City, Long Island, and Southern New England markets. Endemic traffic congestion, air pollution and infrastructure deterioration are some obvious symptoms of this access problem.

NYS-25/NYC-18, RVS Kaye at 1-2.

Moreover, the New York Metropolitan Area has been designated by EPA as a severe non-attainment area for ozone. Several of the most severe environmental "hot spots" are located along major truck routes, *e.g.*, Canal Street in Manhattan. The Clean Air Act requires such areas to track vehicle miles traveled ("VMT"), congestion levels, and vehicle emissions from growth in VMT or trips. 42 U.S.C. § 7511(a). The health impact of the region's air quality problems is illustrated by the fact that the South Bronx is experiencing hospitalization and death rates linked to asthma at eight times the national average.¹³

Dependence on trucks has been exacerbated by the deterioration over time of rail service east of the Hudson. In New York City and surrounding areas, a cobbled network of rail lines (necessitating costly interchanges) combined with inefficient

¹³/ See Intervention Petition, Exhibit E.

float operations has discouraged the use of rail and led to a pattern of infrastructure neglect. The remaining rail freight originating in this area and destined for points south often follows a route north toward Albany, crosses the Hudson River at Selkirk, and then travels south until reaching New Jersey. This circuitous route has substantial negative cost and competitive impacts for shippers: it typically adds one day to transit times (if appropriate switching schedules are met), and also adds approximately 300 miles, and \$5 per ton to shipping costs (compared with the use of a more direct float operation to New Jersey). Congressional Rebuttal at 13. Rail shippers in this region who are unable to use motor carriage as an alternative are thus at a competitive disadvantage with their counterparts enjoying more direct rail access and routing options. These additional costs are passed along to retail consumers in New York, where the cost of living is among the highest in the nation. The 300 mile detour made by many trains also increases rail-related emissions, further exacerbating the region's environmental problems. In addition to the other impacts noted above, the Congressional Delegation and the City and State of New York also allege that the dwindling of rail services to the area is responsible for the loss of manufacturing jobs and continued failure to attract new industry. Intervention Petition at 6.

An alternative route is available to ship goods south from east of the Hudson origin points: it utilizes a float operation from Brooklyn to the Greenville Yard in New Jersey. If approved, the acquisition will provide both CSX and NS access from the Greenville Yard (in the northern New Jersey SAA) to rail lines east of the Hudson via the float operation currently operated by the New York Cross Harbor Railroad. However, there is concern that the Applicants cannot or will not use this operation as currently owned and configured. Once an integral component to rail shipments to the Northeast, carrying approximately 300,000 car loads per year in 1954, the deterioration of the cross harbor service's infrastructure now limits its potential to transport significant carloads efficiently into the national rail network. Intervention Petition, Exhibit A.

Congressman Jerrold Nadler and twenty-three members of the U.S. House of Representatives (the "Congressional Delegation") have called upon the Board in its consideration of the pending application to include in the proposed transaction other railroads operating in the territory. Intervention Petition filed October 8, 1997 (undesignated). The Congressional Delegation has accordingly requested that any approval of the transaction be conditioned on the extension of the northern New

Jersey SAA so as to benefit shippers east of the Hudson River. Id. The Congressional Delegation filings call for a responsible float operation to transport freight rail cars across the Hudson River and two viable railroads to operate certain trackage east of the Hudson. Id. New York City and New York State have endorsed the plan in correspondence to the STB.

The Congressional Delegation considers a cross-harbor operation as critical to improving rail access to the area east of the Hudson River. They contend that shippers east of the Hudson will not benefit from the efficient routings advertised by the Applicants as a major benefit of the acquisition. By contrast, they assert that as a result of the acquisition there will also be serious negative environmental impacts for economic development and air quality associated with increasing truck traffic passing through these communities enroute to the northern New Jersey SAA. The City has expressed a further concern that the lack of competitive rail access to New York City will hinder its efforts to improve air quality and to come into compliance with the Clean Air Act. NYC-19, at 2. The DEIS issued by the SEA did not address these negative environmental impacts and consider means to mitigate them.

Although the Department is hesitant to recommend the alteration of the SAAs, the circumstances involving questions of basic rail access for one of the most populous areas of the country are unique, and action is warranted to assure mitigation of the environmental impacts and protection of the public interest in rail access to the area east of the Hudson River. Assuring a strong, viable float operation and efficient, environmentally sound connections to the shared asset areas would have substantial public interest benefits. A study by the New York Economic Development Corporation ("NYEDC") has estimated that an improved car float operation will increase the rail share of the region's inter-regional freight by 40 percent, or an increase of 4.2 million tons of freight annually. Intervention Petition at Exhibit L. With adequate investment in facilities, the cross-harbor float could reduce the 24 hour journey via Selkirk to about two hours, and could provide a \$5 per ton cost advantage over the Selkirk route. Id. The Department supports the development of this service to create a viable operation that can help the region achieve its environmental goals and enhance rail transportation for businesses and millions of residents in New York City and Long Island.

The City and State of New York cite public interest factors as well. For example, they have just invested over \$200 million in rail facilities east of the Hudson River, including the Bronx Connector and the 65th Street Yard. NYS-24, at

5-21; NYS-26 (Comments on the DEIS) at 11. These funds have been committed in order to encourage a shift in moving freight from truck to rail. As currently proposed, however, the pending transaction would undermine this goal by adding an estimated 1,000 additional trucks each day to the already congested roads and bridges in this area. Congressional Delegation Comments on the DEIS at 4 (undesignated).

We recognize the Applicants' arguments that shippers that dray freight to the northern New Jersey SAA will enjoy the benefit of competition provided by two carriers instead of one (Conrail). But this argument fails to address the public interest in substituting rail carriage for truck transport. The public interest is best served by addressing environmental impacts linked to the transaction and, more broadly, by facilitating the expeditious enhancement of rail alternatives in this region, rather than by allowing continued degradation.

The Board's broad mandate is to assure that railroad consolidations like this one are "consistent with the public interest." 49 U.S.C. § 11324(c). The Department submits that, as with other problem areas, the Applicants and the parties most affected by this transaction should attempt to reach a mutually satisfactory resolution of their differences. We therefore ask the STB to promote such discussions. Should these fail within a reasonable time, DOT encourages the STB to require the Applicants to develop more specific proposals leading to the development of a viable, efficient rail transportation system east of the Hudson River, including viable float operations. In particular, DOT strongly recommends that the Board carefully consider the potential adverse environmental impact from projected increases in truck traffic and from truck traffic now moving to intermodal terminals rather than directly to shippers and receivers in New York and New Jersey. As a condition to any approval of this transaction, the Board should require the Applicants to develop a mitigation plan responsive to these impacts that serves the public interest in having viable, efficient rail transportation east of the Hudson River.

C. Rail Passenger Operations

The transaction also has the potential to affect significantly intercity and commuter rail passenger service, particularly in the northeastern U.S. Rail passenger transportation is an important national resource that contributes substantially to reducing air pollution and roadway congestion. The status of pollution and congestion in the Northeast renders those benefits even more important to the area under consideration. In this region, too, passenger and freight railroads operate on each others' lines, and so must coordinate extensively in order to accommodate sometimes disparate interests. DEIS, Vol. 1, at 4-22. Consequently, the replacement of Conrail with two independent Class I railroads and the shared asset operator raises a concern about the extent of future cooperation.

Reliability is critical to the success of passenger train operations, and DOT has already expressed its view on the effects of this transaction on that subject. DOT-5 at 9-11. We continue to support a five year oversight period, during which periodic reports would provide the information necessary to monitor developments. *Id.* This condition would not reduce the transaction's public benefits, and would ensure that the public interest in rail passenger operations is appropriately safeguarded.

D. Operations in the Shared Asset Areas

The establishment of SAAs holds the potential for very real benefits for shippers and the nation's economy. Introducing rail competition and extending single-line service through much of the eastern U.S. should result in lower rates and improved services.

But there is also an undeniable risk to this approach. This transaction proposes to place in the SAAs two (or three, counting the remnants of Conrail) carriers where the existing rail network has previously accommodated only one. The SAAs are concentrated in northern New Jersey, Philadelphia, and Detroit, where rail passenger transportation thrives. Although CSX and NS are large and capable railroads in their own right, their operations have taken place in less densely populated areas with relatively little passenger rail presence. Moreover, the Applicants have never had the need to cooperate to the extent they will have to in order for the SAAs to work smoothly and produce the benefits they have promised. Unfortunately, the smooth integration of huge rail systems is something that can no longer be taken for granted.

The Applicants have submitted detailed SIPs that, as DOT has already

acknowledged, satisfy any concern the Board¹ may have with respect to the issue of safety. DOT-5. But integration from the perspective of safety and integration from the perspective of efficient and reliable long-term commercial operations are not identical. Concerns related to operations within the SAAs were identified early in the proceeding (particularly by the Port Authority of New York and New Jersey, in NYNJ-13), acknowledged by the Board (Decision No. 44, October 15, 1997), and addressed again in a wide-ranging settlement agreement between the Applicants and the country's largest organization of shippers (CSX/NS-176, Appendix B). Nonetheless, the consequences of a UP/SP-style service fiasco in the East would be catastrophic.

DOT therefore strongly urges the Board to retain jurisdiction for five years over the commercial implementation of any approval it may grant in this proceeding, and to impose reporting requirements to monitor developments.¹⁴ Such a condition meets all the traditional criteria: it is related to the consequences of the transaction, it raises no questions of operational feasibility, it does not entail any reduction in the public benefits promised by the transaction, and indeed it imposes no proactive obligation on the Applicants (except for reporting, to which in some respects they have already committed in the NITL agreement). It would have the benefit of providing pertinent, ongoing information about the status of traffic movement into, out of, and through the competitive centerpiece of this transaction. Finally, this scrutiny would provide additional incentive for the Applicants to ensure that their operations in the SAAs will be adequately capitalized, equipped, and staffed, that their business plans are solid, and that the efficiencies they envision will emerge and foster high service levels.

One additional condition is necessary in this regard. The Applicants have created multiple corporate entities to serve various purposes in the course of this transaction. *See, e.g.,* CSX/NS-18 at 6-9. DOT ascribes no particular motive or effect to any of this structure, but the Board should ensure that responsibility for operations in the SAAs rests squarely with those who would create these areas, operate in them, and secure their most immediate benefits. No technically independent corporate structures should be allowed, as a legal device, to limit or avoid the Applicants' exposure to liability in the event of difficulties. *Cf.* CSX/NS-18

^{14/} Presumably, the content of the reports would be similar to those imposed on UP in Ex Parte No. 573.

at 42-43. This step would instill in the Applicants themselves every possible incentive (if any is lacking) to succeed in their ambitious plans. DOT sincerely hopes that they will succeed, and if there were not a basis for cautious optimism we would likely be urging greater caution and recommending more specific conditions. But consistency with the public interest requires at a minimum that in the event of failure, shippers, rail passenger operators, and communities need to be able to turn to NS, CSX, and Conrail for full recourse.

V. EFFECTS OF THE PENDING TRANSACTION ON RAILWAY LABOR MUST BE ADDRESSED

A. The Impacts on Applicants' Employees

The Applicants anticipate that the implementation of the proposed acquisition will result in a net loss of 2,670 jobs on a consolidated basis over the first three years (3,822 jobs abolished and 1,152 new jobs created). CSX/NS-20, VS Peifer/Spenski at 522. This represents 3.6 percent of the combined workforce of the Applicants. In addition, a total of 2,323 jobs will be transferred. Id.

Although these effects are not large in view of the total employment of the Applicants (72,000 positions), they will be significant in some geographic areas, and among certain non-operating crafts. Specifically, in the state of Pennsylvania a net loss of almost 3,000 jobs, including almost 1,800 jobs abolished and nearly 1,500 jobs transferred out of state, is anticipated. CSX/NS-26, Labor Impact Exhibit at 1-16. These losses will be offset by about 300 jobs either created or transferred into the state. Id.

Clerical employees, carmen, and maintenance of way employees will absorb virtually all the negative impacts among agreement employees, including the abolishment of 843 current clerical positions, 405 current maintenance of way positions, and 338 current carmen positions and the transfer of 702 clerical positions. Id.

With respect to collective bargaining agreements, NS proposes to extend the NS agreements to the acquired Conrail territories. CSX/NS-176 at P-680. CSX proposes a significant rearrangement of the Conrail seniority districts and a repositioned combined workforce. CSX/NS-20, Appendix A at 485-519. CSX also maintains that for several crafts existing collective bargaining agreements and crew districts would preclude the improved operations envisioned by the operating plan.

Id.

B. Protections for Affected Employees

1. The Negotiation and Arbitration Process

Several rail labor unions argue that approval of a railroad consolidation has come to imply approval of the collective bargaining changes submitted by railroads in their applications as part of their operating plans. ARU-23 at 161; IAM -4 at 10,11. The International Association of Machinists ("IAM") suggests that in the event this transaction is approved, the STB should clarify that such approval is not tantamount to "findings regarding the necessity of overriding any provisions of the Conrail collective bargaining agreements to effectuate this transaction." Comments of the IAM, at 11.

The Department joins in this recommendation. Regardless of its technical or legal accuracy, there does indeed appear to exist a perception among significant numbers of railroad employees that by including ever more detailed references to labor agreements in their applications to the ICC or STB, railroads are thereby gaining an advantage in the bargaining and arbitration processes that follow regulatory approval.¹⁵ It is therefore important to clarify to employees, rail carriers, and arbitrators that approval of a transaction does not imply prejudgment of the proposed changes to the collective bargaining agreements submitted in conjunction with the carriers' application. This will help ensure that traditional rights under New York Dock will not be eroded.

2. Labor Implementing Agreements

Implementing agreements are labor-management contracts that spell out in detail how formerly independent groups of union employees will be integrated following a merger. Typically an implementing agreement will cover the consolidation of seniority rosters, the boundaries of the seniority district, the scope of work and which of the previous labor contracts will apply to the new seniority district. Implementing agreements may also cover changes in reporting points and

¹⁵/ These processes and the applicable standards are prescribed in New York Dock Railway -- Control -- Brooklyn Eastern Terminal, 360 I.C.C. 60 ("New York Dock"), *aff'd sub nom.* New York Dock Railway v. United States, 609 F.2d 83 (2d Cir. 1979).

the relocation/transfer of employees.

The agreement negotiated between the NITL and the Applicants provides that the Applicants will complete "necessary" implementing agreements prior to the "Closing Date." CSX/NS-176, Appendix B at B-3. Several individual shippers and other shipper organizations have also championed pre-approval of implementing agreements or the imposition of a fixed timetable for the resolution of implementing agreements. See CARG-5 at 3 (Cargill Industries); DUPX-02 at 6 (E.I. Dupont DeNemours & Co.); CMA-10 at 27 (Chemical Manufacturers Association).

The Department recognizes that safety and service concerns are better met if labor implementing agreements are in place prior to the integration of previously separate rail systems. However, we do not support pre-approval requirements or the imposition of a fixed timetable for completion. Section 4 of New York Dock already provides a "streamlined" process for resolving any impasse that may arise. CSX/NS-176, at P-621.

3. Additional Benefits for Transferred Employees

The Transportation Communications International Union ("TCU"), which represents both clerical employees and carmen, contends that the work of hundreds of its members will be transferred as a result of this transaction, and that they should not be compelled "to follow that work without being offered the alternative option of receiving a separation allowance" comparable to that extended to Conrail management personnel. Comments of the Transportation Communications International Union, at 7. The Applicants consider that applicable New York Dock provisions constitute the appropriate level of labor protection for positions that are to be relocated. CSX/NS-176, at P-575.

The Department is of the view that pertinent circumstances have changed since New York Dock protections were formulated some twenty years ago. Virtually every existing Class I rail carrier, including the Applicants, is the product of one or more mergers that have occurred since that time. The proposed transaction is assuredly larger than any that could have been contemplated when New York Dock protections were first imposed; it encompasses the realignment of three huge Class I railroads, covering virtually the entire United States east of the Mississippi River.

Under the plan proposed by the Applicants, Conrail's clerical employees, currently largely located in Pennsylvania, will in many cases be asked to relocate to

distant locations such as Jacksonville, Florida and Atlanta, Georgia. Failure to accept such relocation offers will result in forfeiture of all New York Dock benefits. By contrast, employees who actually lose their jobs will have the option of up to six years of income and fringe benefit protection or a separation allowance equal to approximately one year's earnings.¹⁶

The Department does not endorse the view that in these circumstances there must be direct comparability to the apparently generous benefits afforded to some of Conrail's management personnel. However, DOT is persuaded that a Conrail employee who must transfer to a position a significant distance away as a direct result of the transaction should receive at least some of the same benefits as an employee who loses his or her job following the transaction. We therefore recommend that the Board modify the existing New York Dock terms (Section 7, Separation Allowance) to the extent necessary to provide employees subject to forced relocation the option of a separation allowance equivalent to the separation allowance currently available to dismissed employees.¹⁷

VI. THE PROPOSED TRANSACTION THREATENS TO REDUCE COMPETITION, WHICH REDUCTIONS MUST BE AMELIORATED BY APPROPRIATE CONDITIONS

A. The Proper Analytical Framework

The importance of competitive analysis in the assessment of the public interest in rail merger proceedings is evident from the final decision in almost every prior case. In those decisions the ICC and STB have drawn heavily upon antitrust law and precedent by recognizing that competition takes place, and so is measured, within markets.

^{16/} The Applicants project that most employees who lose their jobs as a result of the transaction will be recalled within three years. CSX/NS-176, at P-580.

^{17/} This would be a relatively minor extension of benefits in reality. First, insofar as a separation allowance requires forfeiture of seniority, only employees for whom relocation is a true hardship are likely to avail themselves of this option. Second, in such cases the railroad will obviously not have to bear relocation expenses, which can be significant. Third, job openings caused by an employee who elects not to transfer may in some cases be filled by employees who would otherwise be entitled to receive six years' income protection.

Because competition takes place within economic markets, we must define the economic markets that would be affected by [a proposed consolidation]. A relevant market is the area of effective competition, and necessarily has two dimensions, product and geographic. Generally, two products, whether they are goods or transportation services, are in the same market if they are close substitutes. The closeness of substitution is measured (in principle, though only imperfectly in practice) by the extent to which consumers shift their consumption in response to a change in relative price or quality.

UP/MKT, 4 I.C.C.2d at 432; UP/CNW, slip op. at 57.

1. The Relevant Product Market

The relevant product market for assessing the competitive effects of proposed consolidations includes all products that are "reasonably interchangeable." UP/MKT, 4 I.C.C. 2d at 432, citing United States v. E. I. Dupont de Nemours Co., 357 U.S. 377, 395 (1959). In other words, if buyers of a product can turn to another product and/or another supplier and thus prevent a merged firm from sustaining a price increase, then the definition of the market must be expanded to include the additional product or supplier. The product provided by railroads is the transportation of freight. In past railroad merger proceedings, the ICC and the STB have not applied a single, fixed definition of the relevant market, but instead have examined the specific circumstances and the evidence of record in each instance, to determine whether the relevant market was confined to rail freight transportation or was broad enough to include other transportation modes or products. See UP/SP, slip op. at 116-32; UP/CNW, slip op. at 57; UP/MKT, 4 I.C.C. 2d at 433-34 and cases cited therein.

At the same time, the Board is specifically required under 49 U.S.C. § 11324(b)(5) to examine the effect of a transaction on "competition among rail carriers in the affected region." The ICC observed in this regard that the intent of the nation's Rail Transportation Policy (49 U.S.C. § 10101) is "to ensure the development and continuation of a sound rail transportation system with effective competition among railroads and with other modes." SE/SP, 2 I.C.C. 2d at 721.

In this proceeding the Applicants have not formally defined the relevant product market, but they point out that in the Northeast, truck penetration of markets and the resulting intermodal competition have been substantial. CSX/NS-19, VS Kalt at 14-17 and VS Gaskins at 90-98. The U.S. Department of Justice has

defined the relevant product market to include other modes of transportation. DOJ recognizes that for some movements truck and barge transportation can be substituted for rail to constrain the surviving railroads from increasing rates to non-competitive levels. DOJ-1 at 5. Extensive evidence has also been presented in this proceeding by coal-fired electric utilities that the transmission of electricity over the various power grids constitutes another measure of competition.¹⁸

Based on the evidence submitted by the parties, the Department submits that the relevant product market in this proceeding generally consists of freight transportation, which includes rail, truck, and barge/water carriers. For the utility companies in this case, analysis of the relevant product market also requires an analysis of available coal alternatives, principally the wheeling of electricity that may constrain rail market power.

2. The Relevant Geographic Market

The geographic market is the area in which suppliers of a service or product operate, and to which buyers can turn to meet their requirements. Competitive analysis must also encompass any "economically significant submarket" where the transaction may substantially lessen competition. UP/MKT, 4 I.C.C. 2d at 435. As the ICC noted in the Union Pacific Case, 366 I.C.C. at 505, "the distinctions between product and geographic markets are not as clear in transportation as they are in other industries, for carriers, in particular railroads, effectively sell their geography." Thus the determinations of the relevant product market and the relevant geographic market in a particular case will necessarily be interrelated. In analyzing the geographic market, the ICC and the Board have analyzed traffic flows between city pairs, as well as flows in rail corridors, and at specific points in the area in which merging rail firms operate. UP/SP, slip op. at 106-07, 121-31; UP/MKT, 4 I.C.C. 2d at 437.

Based upon the evidence submitted by the parties and its own analysis, the Department submits that the relevant geographic market in this transaction consists of the points and rail corridors presently served by Conrail, where the proposed acquisition would reduce the number of serving railroads from two to one. The general area of interest encompasses the entire northeastern United States and part

^{18/} See PEPC-4, VS Felton at 10 and VS Kaplan at 6-7; NIMO-6 at 6 and VS Bonnie at 2; NYSEG-14, VS Mulligan at 41.

of the Midwest.

DOT conducted its own competitive examination of the proposed transaction, using the 1995 Rail Carload Waybill Sample. Our review found that the proposed division of Conrail lines between CSX and NS largely preserved intramodal rail competition where it presently exists. The remaining areas of reduced competition identified in our analysis generally correspond with the ten geographic markets identified by the Applicants as facing a reduction in the number of railroads from two to one.

B. The Transaction's Impact on Competition Generally

This transaction poses both traditional and unique effects on competition. The competitive analysis in a typical rail consolidation requires a focus on those areas in which the reduction in the number of railroads translates into reduction in competition. Indeed, as noted above, this proceeding presents such areas. This transaction would also reduce service to some shippers by depriving them of existing single line service. Although this transaction will effectively eliminate one carrier, its division between NS and CSX will have the effect of expanding the area in which these two railroads compete. Similarly, although the creation of the SAAs will further enhance that ongoing competition, it has also raised concerns about competitive effects on shippers outside of the SAAs. We address these matters below.

1. Loss of Intramodal Competition

The Applicants acknowledge that their proposed acquisition plan and allocation of the Conrail lines creates a limited number of instances -- ten -- where the number of serving carriers would go from two to one if no corrective action is taken. CSX/NS-18, VS McClellan at 512-14. For CSX, affected shippers are located in Indianapolis and Crawfordsville, Indiana and in Upper Sandusky and Sidney, Ohio. For NS, such shippers are located in Avon Lake, Fairlane and Sandusky, Ohio; in Red Key and Alexandria, Indiana; and in Normal, Illinois. CSX/NS-18, VS McClellan at 546. The Applicants deny that Toledo (Ohio) Dock will lose rail competition, because both CSX and NS will serve this facility following the transaction. CSX/NS-176 at HC-70. The Applicants maintain that all shippers who have access to two railroads today will have two carrier access post-transaction through either trackage rights or haulage rights. CSX/NS-18, VS McClellan AT 548-

549. Finally, the Applicants represent that they stand ready to address the concerns of any shipper that they may have overlooked in their 2-to-1 analysis. CSX/NS-19, Vol., 2A, VS Hart at 149.

The Department has conducted its own analysis of the effects of the transaction on intramodal competition. We agree with the Applicants' identification of the ten locations in Ohio and Indiana that would otherwise lose two carrier service. DOT has also concluded that Wabash County, Indiana will lose intramodal competition. The Applicants claim that CSX and Conrail now serve different shippers in the County (CSX/NS-19, Vol. 2B, VS Harris, at 57 note 36), but that is immaterial. The presence of two railroads within a single county must offer at least some existing shippers competitive options, and the prospect of intramodal choice also serves as a factor in future rates and services for current shippers and as an attraction for future shippers. We therefore recommend that the Board impose a condition requiring continued two railroad service in Wabash County.

As noted, the Applicants have proposed to address competitive losses with a combination of trackage rights and haulage rights. CSX/NS-18, VS McClellan at 548-49. DOT considers trackage rights, the standard response to loss of intramodal competition in rail consolidation cases, to be a superior competitive constraint to haulage rights. We also recognize, however, that operational realities may favor haulage rights in certain cases. In these circumstances the burden should be on the Applicants to justify, if they can, the use of less effective haulage rights.

Several shippers, supported by DOJ, claim that they will lose intramodal competition after the transaction unless corrective action is taken. DOJ-1, at 8-10; IP&L-3, VS Weaver at 3-4; PEPC-4, VS Felton at 2-3. We will address the Indianapolis Power and Light's Stout Plant here and the PEPCO situation in our discussion of the competitive effects of the SAAs.¹⁹

¹⁹/ DOJ identified one other utility, PSI Energy, Inc., that faces a loss of rail competition at its Gibson power plant. DOJ-1 at 9-10. PSI Energy, however, has not participated in this proceeding. Moreover, the Applicants point out that Conrail's trackage rights to the Gibson plant ended the year before the pending transaction was first proposed, and therefore that there is no effect on the status quo. CSX/NS-176, at HC-78. DOT has insufficient information to take a position on this matter.

(a.) Indianapolis Power & Light

The IPL's Stout Plant is a coal-fired electric utility that is served only by the Indiana Railroad ("INRD"), a subsidiary of CSX. Today, Stout receives 90 percent of the coal it burns from mines in southern Indiana served by the INRD. DOJ-1, VS Woodward at 8. The remaining 10 percent originates from mines served by the Indiana Southern Railroad ("ISRR"), is interchanged with Conrail, and then switched to INRD for final delivery. IP&L-3, VS Weaver at 8. According to DOJ, IPL used the threat of the build-out to a Conrail line (a distance of 2.5 miles) to ensure that it receives satisfactory switching services and reasonable switching charges from INRD. DOJ-1, VS Woodward at 8, 18. After the transaction, it contends, CSX will replace Conrail and thereby eliminate both the build-out threat at the Stout Plant and IPL's ability to discipline INRD/CSX market power. *Id.* at 19.

CSX charges that IPL used the threat of truck competition to constrain rail charges at Stout, not the threat of the build-out to Conrail. CSX/NS-177, Vol. 2A, RVS Hoback at 196-98. CSX further disputes DOJ's and IPL's claim that a reciprocal switch agreement and published reciprocal switching charge exist for Conrail to serve Stout. CSX/NS-176, at HC-54. CSX asserts that the existing switching agreement is a private contract. *Id.* However, CSX has expressed a willingness to maintain competitive conditions for a period of time. *Id.* at HC-55.

In the UP/SP merger, the Department joined other parties in arguing that maintaining the competitive status quo for shippers necessarily entails preserving build-in/build-out opportunities that exist prior to the transaction under consideration. DOT-4 (filed June 3, 1996) at 41. The potential for a shipper to use the threat of a build-in/build-out to another carrier has been shown to be an effective form of competition and has constrained rail rates. The Board embraced this view and preserved this competitive option in perpetuity for all shippers on the lines affected by that transaction, regardless of whether the threat had ever been used. UP/SP, slip op. at 146. In this situation, Applicants' restructuring of the rail service around Indianapolis would eliminate this competitive option for IPL's Stout Plant. The Department recommends that the STB preserve this build-out by granting to NS overhead rights to the point on the CSX line where Stout would construct the build-out and receive NS coal shipments.

2. Loss of Single Line Service

A number of Conrail shippers who currently enjoy single-line service between origin and destination would receive joint-line service from CSX and NS after the transaction is consummated, and claim that they will be disadvantaged by this reduction in service. *See, e.g.*, CEC-6, VS Kovack at 10-14 (Centerior Energy Corporation); NYSEG-14, VS Edwards at 81-83 (New York State Electric and Gas Corp.); IP-4, at 3-4 (International Paper Co.); NIMO-6, VS Bonnie at 13 (Niagara-Mohawk Power Co.); ISI-5, at 4 (Inland Steel Industries). The Applicants claim that the creation of these joint-line moves was an unavoidable by-product of the transaction and one that does not represent a reduction in rail competition since none of the shippers is losing a rail option. CSX/NS-176, at HC-490. They further contend that while 133,000 units (cars, containers, or trailers) of traffic will lose single-line service as a result of the transaction, 712,530 units will gain new single-line service.²⁰ The Applicants also point out that some of the shippers who will lose single-line service in certain corridors will gain single-line service in corridors that are today joint-line moves.

The Applicants and the NITL have crafted an agreement that will maintain current Conrail rates (subject to established rail cost adjustments)²¹ for a three-year period for affected shippers. NITL-7 at 50.²² The agreement also obliges the carriers to work with these shippers to provide fair and reasonable joint-line service. *Id.*

The Board and its predecessor have recognized that the efficiencies of extended single-line service brought about by rail consolidations constitute a significant public benefit. UP/SP, slip op. at 113, and cases cited therein. This

²⁰/ We understand that 45,666 units on NS and 87,432 units on CSX will lose single-line service, and that 291,182 units on NS and 421,348 units on CSX will gain single-line service. *See, e.g.*, CSX/NS-18, at VS McClellan at 550.

²¹/ Specifically, the rail cost adjustment factor, or "RCAF," is a regulatory cost index reflecting changes in the cost of goods and services purchased by railroads. AAR Railroad Cost Indexes at 25 September, 1997. Its purpose is to provide an objective measure by which railroads can recover inflationary cost increases. The specific RCAF employed in the NITL agreement is not adjusted for railroad productivity gains.

²²/ To qualify for this treatment shippers must have shipped fifty cars during the calendar year prior to the "Control Date" in single-line Conrail service.

acquisition, however, presents shippers and the Board with the loss of that service. Although the NITL agreement is intended to protect affected shippers, maintaining the same rate while introducing less efficient joint-line service results in an increase in shippers' service-adjusted rate.²³

The Department urges that the Board assess the efficiencies and benefits from new single-line service in the aggregate together with the losses from new joint line service. Although it may well be that the benefits outweigh the losses overall, applicants in rail consolidations should be held to their representations. Here, NS and CSX have promised that "[t]he needs of each customer impacted by the loss of single system [Conrail] service will be addressed specifically in the months ahead in order to minimize adverse effects to the greatest extent possible." CSX/NS-18, VS McClellan at 550. These carriers have apparently done so with certain large shippers, and the Board should require them to continue this process with others as well.

C. Competitive Effects Resulting From the Shared Asset Areas

As already noted, one of the unique aspects of this transaction is the establishment of SAAs in northern New Jersey, southern New Jersey (including the Philadelphia area), and Detroit. CSX and NS will have equal access to all customers in these areas. CSX/NS-18, VS McClellan at 514.²⁴ According to the Applicants, implementation of the SAAs will provide competitive options to a large number of shippers that were solely-served by Conrail. CS/NS-177, Vol. 2A, RVS Kalt at HC-233.

A number of parties, particularly those adjacent to these areas, have expressed concerns with the introduction of railroad competition to shippers within the SAAs with which they compete. ISRI-6, at 3 (Institute of Scrap Recycling

²³/ We also note that solutions advanced by some parties allegedly to restore single-line service would, in fact, enhance their competitive position by providing two-carrier service where previously there was only one. See CEC-05, VS Kovach at 12.

²⁴/ Similarly, shippers in the Monongahela coal region in southwest Pennsylvania and shippers at the Ashtabula Harbor facilities on Lake Erie in Ohio will have equal access to both carriers in these joint use areas. CSX/NS-18, at 4.

Industries); RWCS-3, at 2 (Resources Warehousing and Consolidated Services, Inc.); ENRS-6, VS Fauth at 46 (Erie-Niagara Rail Steering Committee). These parties contend that the new SAAs will place them at a competitive disadvantage because of new rail competition and potentially lower transportation rates in the SAAs. Several utilities have also advanced this argument because of the intense competition for electricity on the various power grids throughout the Northeast. NIMO-6, VS Bonnie at 11; PEPC-5, VS Felton at 2. They claim that utilities gaining access to two carriers in an SAA will gain a competitive advantage in selling electricity on the grid through lower transportation rates. NIMO-6; VS Fauth at 47-49. To remedy this situation, these parties typically request that the Board condition the transaction by ordering the extension of current SAAs and/or the creation of new ones. MPI-2, at 8; RWCS-3, at 2; NIMO-6, VS Bonnie at 18; PEPC-5, VS Felton at 3.

The Applicants counter that such requests should be denied. They emphasize that the ICC and Board have squarely and consistently rejected requests to impose conditions to preserve any "competitive balance" among the industries served by railroad carriers. CSX/NS-176, at HC-121. The Applicants also argue that were the Board to restructure and expand the currently proposed SAAs, "the economics of the Conrail acquisition and Transaction Agreement would be dramatically and drastically changed -- possibly to an extent warranting reconsideration by the Applicants of the pro-competitive structure that could well be rendered commercially impracticable and/or operationally infeasible by such conditions." CSX/NS-176, at HC-122.

The Applicants also contend that competition within the SAAs will, in fact, benefit shippers outside these areas. For example, shippers of products that may be trucked to an SAA will enjoy the competitive influence of increased rail options in SAAs. CSX/NS-177, Vol. 2A, Rebuttal Verified Statement ("RVS") of Kalt at HC-242. In addition, they assert that the geographic and source competition that link SAA and non-SAA shippers will discipline rail rates. *Id.* at HC-243.

From a competitive standpoint, service by two railroads is generally superior to service by one. However, intramodal competition is not the only form of competition at work in the marketplace. Conrail (or any monopoly-serving railroad) would be expected to exercise market power and extract monopoly rents if it were able to do so. In fact, however, Conrail's monopoly power is presently constrained by competing truck and water carriers and by the geographic and product competition facing its shippers. See UP/SP, slip op. at 130; BN/SE, slip op. at 99.

The very concerns expressed by parties seeking to expand the SAAs attests to the perceived effectiveness of these forms of competition. The proposed elimination of Conrail's rail monopoly in the SAAs will further enhance the effectiveness of that competition.

The Department accordingly believes that the benefits of competition within the SAAs could well spill-over into areas outside the SAAs. Both CSX and NS are well aware that shippers outside of the SAAs compete with shippers inside the SAAs. If the non-SAA shippers served only by CSX or NS post-transaction do not receive transportation rates and services that allow them to compete with those in the SAAs (who will be getting rates and service terms produced by direct intramodal competition), they will lose business to their competitors within the SAAs. As business shifts to shippers within the SAAs, both NS and CSX must compete directly for it and thus neither is guaranteed of retaining traffic. Providing competitive rates to shippers served only by CSX or NS outside the SAAs at the very least ensures the serving carrier that it will not face the risk of losing that traffic. It should also be noted that this transaction will not affect the rights of shippers, whether in or out of the SAAs, to seek relief from unreasonable rail rates or discrimination before the Board. 49 U.S.C. §§ 10701, 10704, 10741.

DOT expects that this competitive dynamism will address the concerns expressed by shippers such as the Potomac Electric Power Company. PEPCO asserts that the utilities located in the SAAs will have the advantage of lower production costs due to reduced rail rates for the transportation of coal, and that PEPCO, as a consequence, will be unable to compete effectively with those utilities in selling power to the Pennsylvania-Maryland-New Jersey Interconnection pool ("PJM") grid. PEPC-4, VS Felton at 12, 13. It also claims that it will lose competitive leverage as a result of the transaction, because now two of its major power plants are served only by Conrail and the third is served only by CSX, and afterwards all three will be served only by CSX. *Id.* at 2; *also* DOJ-1, VS Woodward at 21.

The Department believes that as CSX and NS compete within the SAAs for coal traffic and as rate reductions (potentially) occur, CSX must keep coal rates to PEPCO competitive in order to prevent the very outcome that concerns PEPCO. If PEPCO loses power sales to utilities within the SAAs, coal moving to PEPCO will decline while coal moving to utilities within the SAAs will increase. In those circumstances, CSX cannot be assured that it can retain coal traffic to utilities within the SAAs, because it must compete with NS for that business. Consequently, CSX

has every incentive to provide PEPCO with competitive rates to avoid the risk of losing coal traffic to NS. Maintaining PEPCO's ability to compete on the grid will at the very least assure CSX that it can keep that traffic while it competes with NS in the SAAs for coal and other freight.²⁵

D. The "Acquisition Premium" Paid for Conrail

Numerous parties maintain that CSX and NS paid an excessive price for Conrail. These parties include the NITL, the Chemical Manufacturers Association/Society of the Plastics Industry, and various coal-fired electric utilities.²⁶ They contend that the escalating tender offers made by CSX and NS between October, 1996 and February, 1997, when the two carriers each were attempting to purchase the carrier separately, resulted in an "acquisition premium" for Conrail because the purchase price exceeded Conrail's historic book value by billions of dollars. GPU-02, VS Crowley at 6; ACE, *et al.*-18, VS Crowley at 26.²⁷ They further assert that to pay down this debt in the face of new competition in the SAAs, Applicants will resort to raising rates on "captive" shippers. See NITL-7 at 16-27. Accordingly, these parties consider it inappropriate to value Conrail assets at the "inflated" acquisition price for inclusion into the CSX and NS investment bases. See ACE, *et al.*-18, VS Crowley at 36.

Witness Crowley points out on behalf of these parties that the higher capitalization of the investment base would (1) necessarily reduce the carriers' calculated rate of return on investment used in revenue adequacy determinations,

^{25/} Naturally, it is unlikely that a utility like PEPCO would be allowed to cease operations as a matter of public policy. Nonetheless, the presence of power grids and deregulation of the power industry exposes PEPCO and other utilities to far greater competition than has historically been the case. The result is that PEPCO must behave far more like other market-driven shippers, and that railroads serving utilities must treat them as such.

^{26/} E.g., Indianapolis Power and Light (ACE, *et al.*-18), Niagara Mohawk Power Corp. (NIMO-6), PEPCO, Centerior Energy Corp. (CEC-05), and Consumers Energy Co. (CE-04). The Atlantic City Electric Co. was of this view originally, but it has withdrawn from the proceeding.

^{27/} For a complete listing of the different definitions of the premium at issue in this proceeding, see CSX/NS-177, Vol. 2A, RVS Kalt at HC-287.

and (2) by reflecting higher road and equipment values in system average variable cost calculations, distort the application of the Board's jurisdictional threshold to ensure that rail rates are reasonable.²⁸ Both results, it is argued, would permit railroads to raise rates to captive shippers without risking regulatory scrutiny by the Board. To forestall this extraction of higher rates, these parties urge that the Board condition the acquisition by requiring CSX and NS investment bases be calculated using the pre-acquisition book value of Conrail assets. ACE, et al.-18, VS Crowley at 36.

The Applicants, on the other hand, argue that: (1) they did not pay an excessive price for Conrail; (2) the Board should not be swayed by arguments either to overturn Generally Accepted Accounting Principles ("GAAP") or to abandon sound STB/ICC precedent; (3) competition will not permit them to raise rates; and (4) improved efficiencies and revenue growth will provide sufficient funds to pay the purchase price, not escalating rates on shippers, captive or otherwise. CSX/NS-176, at 106-09 and Appendix A at HC 737-67; CSX/NS-177, Vol. 2B, RVS Whitehurst at HC-649.

It is important to note at the outset that the Department does not have substantial doubts about the ability of CSX and NS to repay acquisition-induced debt, even if the Applicants' traffic projections turn out to be overstated.²⁹ We do

²⁸/ Railroad "revenue adequacy" is the measure of whether a railroad is earning a rate of return equivalent to the cost of capital as calculated by the STB. A rate of return less than the cost of capital generally means that a railroad will not be able to replace capital assets over the long run, and it effectively lessens regulatory scrutiny of rail rates. The "rate of return on investment" is defined by the STB as net railroad operating income divided by the railroad net investment base used for transportation purposes. Railroad Revenue Adequacy - 1988 Determination, 6 I.C.C.2d 163, 170 (1989). System average variable costs are calculated using the Board's uniform rail costing system ("URCS"). The Board allocates costs to rail movements based upon agency models and utilizes railroad operating expenses and operating statistics. Ex Parte No. 431 (Sub-No. 1), Adoption of the Uniform Rail Costing System as a General Purpose Costing System for All Regulatory Costing Purposes, (January 26, 1989). By statute, the STB has jurisdiction only over those rail rates with a revenue-to-variable cost ratio ("r/vc") of 180 percent. 49 U.S.C. § 10707(d).

²⁹/ NS has estimated that rate compression (reductions) stemming from competition in the SAAs will lower its revenues by approximately \$160 million. Seale Deposition Tr. at 68. CSX has provided no comparable figure, but for

have serious concerns, however, with the arguments presented in this proceeding claiming distortions of revenue-to-variable cost ratios and the Board's revenue adequacy findings. If these parties are correct and (1) NS and CSX are found revenue inadequate, and (2) system average variable cost increases (thereby reducing the r/vc ratio), then it seems plausible that both carriers would have the opportunity to increase rates in some circumstances -- competition permitting -- without risking regulatory scrutiny.

DOT concludes, however, that conditioning this acquisition by excluding the so-called acquisition premium from the CSX and NS investment bases is inappropriate. After a lengthy proceeding, the Board's predecessor adopted acquisition cost in revenue adequacy determinations because, as a general rule, that cost represents the most accurate and reasonable valuation of a railroad. Railroad Revenue Adequacy - 1988 Determination, 6 I.C.C.2d 933, 938-939 (1990). This finding comports with GAAP and recommendations made by the Railroad Accounting Principles Board cited by Applicants.

In sum, the concerns raised by those seeking exclusion of the financial "premium" paid for Conrail are serious and cannot be ignored. However, they transcend the confines of this proceeding and have broad implications for future transactions and the industry at large. They would therefore be better addressed in a separate proceeding. DOT strongly recommends that the Board institute such a proceeding to address these serious concerns and afford all interested parties an opportunity to participate and develop a comprehensive record. At its conclusion, the Board's final decision and standards would then be applicable to all railroads.

E Assignment of Conrail Contracts

A number of parties have challenged the succession of either CSX or NS to Conrail transportation contracts in the event the proposed transaction is approved by the Board. These concerns arise principally from two aspects of the Applicants' proposal. First, the basic agreement between NS and CSX provides that all transportation contracts with Conrail that are in effect as of the Closing Date of the

purposes of analysis we have assumed a like amount. Based on the pro forma financial statements submitted by these two carriers, it appears that each will have sufficient resources to repay the acquisition debt even if they realize no traffic gains or operational cost savings and even if the projected rate compression takes place.

transaction shall remain in effect through the end of their stated terms, and that CSX and NS will decide between themselves which railroad will carry out the respective obligations set forth in those contracts. Article II, sections 2.2(c)(i) and (ii). Second, the Applicants seek to have the Board require that Conrail's contracts remain in effect following assignment to either CSX or NS, notwithstanding any extant provisions in the contracts "purporting to limit or prohibit Conrail's unilateral assignment of its operating rights to another person or persons." CSX/NS-18, at 102-03 (Item 1(c) of the Prayer for Relief).

Either expressly or by implication, a number of other railroads and shippers object to an assignment of Conrail contracts to either of the Applicants in disregard of any non-assignment clause. See Eastman Kodak Company (EKC-2), APL Limited (APL-4), the Chemical Manufacturers Association (CMA-10), the City of Indianapolis (CI-5), the Gateway Western Railway and the Gateway Eastern Railway (GWWR-3), Amtrak (NRPC-7), Redland, Ohio (Redland-2), NYK Line (North America) Inc. (undesignated), and Providence and Worcester Railroad Company (undesignated). These parties oppose the automatic substitution of either NS or CSX on a number of grounds. For example, APL argues that CSX should not automatically step into APL's contracts with Conrail since, *inter alia*, "CSX is one of APL's principal competitors; its ocean carrier and its stack train subsidiaries compete head-to-head with APL in a niche market carrying time-sensitive commodities from Asia and the Pacific Rim to the eastern United States." APL-4 at 3; see also Comments of NYK Line (North America, Inc.). Similarly, Kodak objects to the assignment of its Conrail contracts since the non-assignment clause in those contracts was intended by Kodak to short-circuit just such a forced assignment, and since it could as easily deal with either CSX or NS, both of which will serve its plant post-transaction. EKC-2. By and large, all of the parties that have commented on this issue have objected to Board approval that would allow Conrail contracts to be assigned by agreement of CSX and NS, and without any input from the affected shipper parties to the contracts.

The applicants have correctly pointed out (CSX/NS-176 at P-95-96) that the STB has legal authority to override contractual provisions "as necessary" in consolidation cases. 49 U.S.C. § 11321(a); Norfolk & Western Ry. Co. v. American Train Dispatchers Ass'n, 111 S.Ct. 1156 (1991). Nevertheless, the Department is aware of no express holding by the Board, the ICC before it, or by a judicial body, that specifically addresses the assignment of a shipper's railroad contract of carriage

to a different railroad in the face of a non-assignment clause and over the express objections of the shipper that has contracted for such a provision.

The Department suspects that this circumstance may reflect the practical differences between past mergers and the present proposal before the STB. In a merger, where only one carrier survives, the assignment of existing contracts to the surviving railroad realistically has the potential to raise far fewer objections than here. In that context the shipper continues to deal with the only successor of the party with whom it contracted, and oftentimes the only carrier capable of performing the contract. Here, by contrast, there would often be two potential "successors" following any approval by the STB. It is also important that, as a general matter, decisions by competitors such as CSX and NS as to how they will divide customers (such as Conrail's shippers) could raise serious antitrust concerns. See *Palmer v. BRG of Ga., Inc.*, 498 U.S. 46, 49 (1990), citing *United States v. Topco Assocs.*, 405 U.S. 596, 608 (1972).

The Department does not question the Board's statutory authority to override previously contracted-for non-assignment provisions. However, we believe that, particularly in the context of an acquisition of one railroad by two competing carriers, care must be taken in the exercise of this authority.

Specifically, DOT recommends that where Conrail's lines have been divided so that either CSX or NS, but not both, could perform the terms of a shipper contract, it makes sense to assign an existing contract for its duration to the only carrier capable of providing the service previously provided by Conrail, notwithstanding the presence of a non-assignment clause. This situation is analogous to that faced in a traditional merger situation. However, in circumstances where either CSX or NS could perform a contract, and where the Applicants have sought to determine between themselves which carrier will in fact take over the Conrail contract, some protection for the shipper is warranted. In those circumstances we believe that the Board should either (1) preserve the shipper's ability to void its contract by exercising its contracted-for non-assignability option, or (2) impose a condition that allows the shipper to determine which of the Applicants will in fact perform the terms originally contracted for with Conrail. As between these options, we believe that the latter is probably the best, particularly since it is our understanding that the contracts at issue are for relatively short terms.

The Board's authority to supersede contractual obligations in approving mergers provides some basic certainty to railroads in the Applicants' position as

they attempt to allocate the myriad property rights of a third carrier. Although the effect of this is that shippers may find themselves dealing with a railroad with whom they never contracted, they would not seem to be significantly disadvantaged thereby. First, they would continue to receive the service terms and rate(s) for which they have bargained. Second, since the contracts are of short duration, there is both an incentive to the serving railroad to earn the business of the shippers, and a near term opportunity for shippers freely to negotiate with other railroads in any event.

By contrast, preserving non-assignment clauses in all contracts that could have been performed by two railroads -- and thereby preserving a shipper's option to void such contracts and renegotiate if it wishes -- arguably extends to such shippers a windfall that would not be available to shippers in a routine merger, or to shippers in an acquisition that could only be served by one of two railroads. DOT believes that a solution allowing shippers the right to choose between two acquiring carriers in circumstances where either railroad could perform the services previously provided by a third seems a fair compromise between the needs of the railroads and those of shippers.

We think in particular that APL has made a showing that it warrants this type of relief. That party has expressed concern that if its non-assignment clause is voided it will find itself bound to a partnership for some years with a competitor with whom it might well have refused to deal in the first instance.

Lastly, DOT must stress that its general position on this matter is premised on the understanding that the contracts at issue are for relatively short terms. To the extent that is not the case, the better course might be for the Board to preserve shippers' ability to exercise the non-assignment clauses for which they have bargained.

VI. CONCLUSION

The pending transaction warrants approval by the Surface Transportation Board only if appropriate conditions are imposed to mitigate threatened public harms. Although the transaction will extend competition, increase productivity and enhance efficiency, the Department remains concerned about maintaining reliable rail freight and passenger service in the eastern United States. Where necessary, conditions required to ensure continued competition must be imposed. Potential harm to communities and the environment must likewise be mitigated. Above all,

safety must be assured.

FRA has worked with CSX and NS to prepare and review the Safety Integration Plans required in this case, and to secure detailed commitments of the resources and steps necessary to implement the SIPs properly. FRA will continue to work with the Applicants to revise the SIPs if necessary in order to address required mitigation measures. Given DOT's concern that rail safety not be compromised, we will closely monitor the Applicants' implementation of the SIPs, particularly given the impact of unforeseen contingencies, if the Board approves the proposed transaction.

The Department is concerned that increases in the number of freight trains operating on lines that also support passenger rail service may disrupt performance or have other adverse effects on rail passenger service. We therefore support a five year oversight period to ensure that rail passenger service, both intercity and commuter, does not suffer as a result of this transaction.

Similarly, DOT urges the Board to retain jurisdiction for five years over the commercial implementation of any approval it may grant, and to impose reporting requirements on the Applicants in order to monitor developments in the SAAs. The STB should ensure that responsibility for operations in the SAAs rests squarely with those who would create them, operate in them, and secure their most direct benefits -- NS and CSX.

Moreover, many of Conrail's contracts with shippers apparently contain clauses that, in other contexts, would prevent their assignment to CSX or NS. The circumstances of this case require careful exercise of the Board's power to override these clauses. DOT urges generally that where either CSX or NS can perform the terms of such a contract, shippers should be permitted to choose which railroad they will use, particularly in the case of APL.

Measures to assure appropriate labor protections also merit specific consideration. In our view, past application of standard protective provisions has resulted in less protection for railway employees than was intended. DOT accordingly asks the Board to clarify the nature and extent of any approval it may grant, so that railroad workers are better able to secure the benefits that the law affords them. We also suggest a modest enhancement of benefits for some workers subject to forced relocation.

This transaction will have significant impacts on communities and the environment in many areas. DOT is particularly concerned about the potential

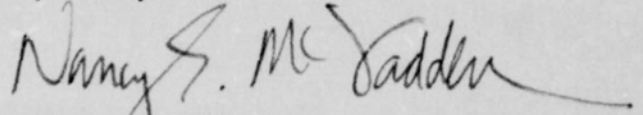
effects on the greater Cleveland, Ohio area. Since the new CSX and NS systems will intersect there, the Board must assure that no unforeseen operational difficulties develop that could potentially affect rail service elsewhere in the United States. At the same time, appropriate measures to mitigate correctly identified material consequences must be adopted.

The New York region east of the Hudson River is another area that may well experience negative effects from this transaction. DOT believes that the circumstances warrant action to assure mitigation of harmful environmental impacts and protection of the public interest in rail access east of the Hudson River. The public interest here is best served by addressing environmental impacts directly linked to the transaction and, more broadly, by facilitating the expeditious enhancement of rail alternatives in this region rather than allowing further degradation. Considering the region's urgent requirement for competitive rail service, DOT endorses the development of viable, efficient rail transportation access east of the Hudson, and we encourage NS and CSX to reach agreement on related issues, including the assurance of a strong, viable float operation across the Hudson River.

The Department overall considers that the best resolution to the problems presented in this proceeding is likely to be found in agreements among those most directly affected. We therefore urge the Board to stimulate further discussions among the Applicants, relevant communities, passenger rail operators, and shippers. For those adverse effects that do not prove amenable to such efforts, DOT recommends that the Board impose remedial conditions. Such conditions must, of course, not themselves present new and unanticipated obstacles to safe and efficient rail transportation.

Properly so conditioned, the pending transaction is consistent with the public interest, and thus warrants approval.

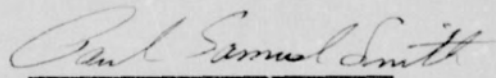
Respectfully submitted.

A handwritten signature in dark ink, appearing to read "Nancy E. McFadden", with a long, sweeping horizontal line extending to the right.

NANCY E. MCFADDEN
General Counsel

CERTIFICATE OF SERVICE

I hereby certify that I have on this day caused to be served on all Parties of Record in Finance Docket No. 33388 by first-class mail, postage prepaid, a copy of the foregoing Brief of the United States Department of Transportation filed in this proceeding.

A handwritten signature in cursive script, reading "Paul Samuel Smith", written over a horizontal line.

Paul Samuel Smith

February 23, 1998