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SURFACE TRANSPORTATION BOARD, IN OPEN VOTING CONFERENCE, APPROVES COMMON CONTROL OF CANADIAN NATIONAL AND ILLINOIS CENTRAL

Surface Transportation Board (Board) Chairman Linda J. Morgan, Vice Chairman William Clyburn, Jr., and Commissioner Wayne O. Burkes today voted, in an open voting conference, to grant, with several conditions, the application filed by Canadian National Railway Company, Grand Trunk Corporation, and Grand Trunk Western Railroad Incorporated (CN), and Illinois Central Corporation, Illinois Central Railroad Company, Chicago, Central & Pacific Railroad Company, and Cedar River Railroad Company (IC), for acquisition by CN of control of IC and for the integration of the rail operations of CN and IC (referred to collectively as applicants). This merger, as conditioned, will create a highly efficient rail system spanning the central United States from the Canadian border to the Gulf of Mexico.

Benefits of the CN/IC Merger. The Board, in reviewing a rail merger, must balance merger-related benefits against any merger-related harms that cannot be mitigated by conditions. Here, the Board noted that the CN/IC merger will make possible a new, single-line service alternative for many shippers, and will thereby allow applicants to provide stronger competition, especially for NAFTA traffic, to other Class I U.S. railroads (especially Union Pacific, Burlington Northern Santa Fe, CSX, and Norfolk Southern). The Board also noted that the merger should generate quantifiable public benefits of more than $100 million a year, mainly through integration of support functions and more efficient use of equipment and crews. The Board also concluded that this "end-to-end" merger, which was supported by more than 240 parties, including more than 190 shippers, will not result in a reduction in competition at any location now open to CN and/or IC. Additionally, the Board noted that the transaction is supported by unions representing more than half of applicants' employees.

The Alliance and Access Agreements. The Board, in reaching its conclusions respecting the CN/IC merger, gave full consideration to claims that had been raised respecting two agreements entered into with The Kansas City Southern Railway Company (KCS): an Alliance Agreement (entered into by CN, IC, and KCS); and an Access Agreement (entered into by CN and KCS). The Board rejected the argument that either or both of these agreements had the effect of transforming the two-way CN/IC merger into a three-way CN/IC/KCS merger. The Board concluded, to the contrary, that these two agreements, even taken together, did not bring KCS into common control with CN and/or IC.

Conditions Imposed by the Board. The Board, which has the authority to impose conditions to mitigate the harm that a merger would otherwise produce, imposed the following conditions upon the CN/IC merger.

Geismar Shippers. In 1995, KCS sought regulatory approval for construction of a build-in line that would allow it to access three IC-served shippers (BASF, Borden, and Shell) in Geismar, LA. The CN/KCS Access Agreement provides, among other things, for KCS access to these shippers via haulage rights over IC. Three additional IC-served Geismar shippers (Rubicon, Uniroyal, and Vulcan) have expressed concern that this aspect of the Access Agreement will eliminate KCS's incentive to construct the build-in line, which (these three additional shippers claim) would have enabled KCS to reach not only BASF, Borden, and Shell, but also Rubicon, Uniroyal, and Vulcan. To ensure that the Access Agreement does not result in a reduction in the IC vs. KCS competition that Rubicon, Uniroyal, and Vulcan might otherwise have enjoyed, the Board imposed a condition requiring applicants to grant KCS access to Rubicon, Uniroyal, and Vulcan under the same terms and conditions that will govern KCS's access to BASF, Borden, and Shell.

North Dakota. North Dakota has expressed concern that the CN/IC merger will result in the elimination of an efficient routing via Chicago for its agricultural commodities moving to the Gulf Coast area, which are originated in North Dakota by the Soo subsidiary of the Canadian Pacific (CP), which are then transported by Soo to Chicago for interchange with IC, and which are then transported by IC to the Gulf Coast area. To ensure that the Chicago gateway remains open for these commodities, the Board imposed a condition holding applicants to their representation to keep open and competitive their Chicago gateway with CP's Soo subsidiary.

Detroit River Tunnel. CN and CP each holds a 50% interest in the Detroit River Tunnel that runs under the Detroit River between Detroit, MI, and Windsor, ON. CN also has a 100% interest in the recently built St. Clair Tunnel that runs under the St. Clair River between Port Huron, MI, and Sarnia, ON. CP has argued that, because CN now has access to a modern tunnel and CP does not, and because any attempt by CP to modernize or replace the Detroit River Tunnel would involve the right-of-way of that tunnel, CN has an incentive to use its 50% interest in the Detroit River Tunnel to thwart any effort by CP to expand or replace that tunnel. To protect CP's ability to make improvements to or replace the Detroit River Tunnel, the Board imposed a condition holding CN to its commitment not to exercise unfairly any rights it may have under the CNCP Partnership Agreement respecting that tunnel to oppose any proposed improvement project that has sufficient engineering, operational, and economic merit to attract the necessary capital for its construction without derogating the value of CN's existing investment in the CNCP Partnership. And, as part of its oversight, the Board will monitor issues related to CN's operational control of the Detroit River Tunnel.

Rail Labor. In approving mergers such as the CN/IC merger, the Board is required, by statute, to impose "labor protective conditions" for the benefit of the employees of the applicant railroads. The Board therefore imposed, for the benefit of the rail employees of CN and IC, the New York Dock conditions that are customarily imposed in railroad mergers. However, in view of the international character of the CN/IC merger, the Board modified the New York Dock conditions, as applicable to the CN/IC merger, by providing that, if and when CN/IC work is moved to Canada, CN/IC's United States employees who choose not to follow their work to Canada will not be deemed to have forfeited their New York Dock protections. The Board also clarified that good faith bargaining has always been an integral part of the New York Dock process and that an arbitrator, and the Board, if necessary, can properly take notice of any abuse of process in any deliberations over labor matters under that process. As requested, the Board imposed as conditions specific settlement agreements the applicants reached with the United Transportation Union and the Brotherhood of Maintenance of Way Employes. Consistent with established policy, the Board also made clear that approval of the merger transaction did not indicate approval or disapproval of any particular collective bargaining agreement overrides, but rather that such issues should be resolved through negotiation, if possible, or arbitration as necessary. The Board also noted that applicants at oral argument had acknowledged the importance of prior labor agreements, and had indicated that they do not expect that wholesale overrides would be necessary to carry out this transaction. Furthermore, the Board clarified that applicants must abide by their representation at oral argument that they would continue to engage in a consultative role with the Federal Railroad Administration with respect to any future merger-related changes with safety implications for the territorial United States (e.g., a transfer of the dispatching function to Canada) and that they would give sufficient notice of any such proposed changes.

Environmental Matters. To fulfill its obligations under the National Environmental Policy Act, the Board imposed the various mitigation measures recommended by the Section of Environmental Analysis in its Final Environmental Assessment. Included was a safety review process to ensure the safe implementation of the transaction.

Oversight. Various parties have expressed concerns over potential harms that may flow from the merger in conjunction with the Alliance and Access Agreements. In response, the Board has imposed an oversight condition of up to 5 years, which will enable the Board to address: concerns expressed by the United States Department of Transportation and others regarding the operation of the Alliance Agreement, particularly with respect to ongoing IC vs. KCS competition in the Baton Rouge-New Orleans corridor; concerns expressed by North Dakota with respect to the Soo/IC interchange at Chicago; concerns expressed by CP with respect to the Detroit River Tunnel (including concerns respecting CN's supervision of the day-to-day operations of that tunnel); concerns expressed by certain labor unions with respect to lack of appropriate labor protective conditions if unauthorized control of applicants and KCS should occur; and concerns with respect to the potential effects on domestic lumber wholesalers of Canadian lumber producers' alleged unfair pricing practices currently under investigation by the United States Department of Justice. The oversight process will also enable the Board to monitor the environmental conditions it has imposed.

KCS Trackage Rights Application. The Board, though it approved the CN/IC merger application, denied a simultaneously filed CN/IC/KCS terminal trackage rights application that sought, for a KCS affiliate, terminal trackage rights over several miles of Union Pacific and Norfolk Southern track in Springfield, IL. The Board ruled that, because the terminal trackage rights sought by the KCS affiliate had no real connection to the CN/IC merger, the terminal trackage rights application would have to be evaluated on the basis of the strict criteria generally applicable to such applications. The Board further ruled that this terminal trackage rights application failed to satisfy those criteria.

The Board's vote was issued today in Canadian National Railway Company, Grand Trunk Corporation, and Grand Trunk Western Railroad Incorporated--Control--Illinois Central Corporation, Illinois Central Railroad Company, Chicago, Central and Pacific Railroad Company, and Cedar River Railroad Company, STB Finance Docket No. 33556. A written decision of the Board, reflecting the Board's vote at the voting conference, will be issued by the Board on May 25, 1999.

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