

## SURFACE TRANSPORTATION BOARD ISSUES NOTICE OF PROPOSED RULEMAKING ON NEW RULES FOR MAJOR RAILROAD MERGERS

Surface Transportation Board (Board) Chairman Linda J. Morgan announced today that the Board has issued a Notice of Proposed Rulemaking (NPR) proposing new rules for major railroad mergers and consolidations (those involving two or more "Class I" railroads, that is, railroads each with annual revenues of at least \$250 million). The new rules would significantly increase the burden on applicants to demonstrate that a proposed merger transaction is in the public interest, reflecting what Chairman Morgan notes as an awareness of the great risk of failure and the competitive, service, and financial concerns raised in connection with what could be the final round of consolidation in the rail industry. In particular, the new rules would require applicants to show that the transaction would enhance competition, and they would require much more accountability with respect to claimed merger benefits and service. At the same time, in proposing these new rules, the Board indicated that it does not intend to prevent transactions genuinely in the public interest and would continue to look with favor upon private-sector initiatives in the public interest.

**Overall Approach.** A key element of the Board's proposal is a new policy statement that, together with the proposed rules, represents a major shift in basis from the pro-merger approach that has guided agency merger decisions for the last 20 years. The Board noted that there is no longer the pressing need that the Nation's largest railroads once had to consolidate their operations to reduce excess capacity because that rationalization has largely been accomplished. Moreover, the Board emphasized that recent consolidations have brought significant transitional service problems that have harmed rail customers and delayed full realization of the merger benefits that were anticipated from those transactions. Accordingly, the Board found it appropriate to propose new rules requiring applicants to bear a substantially heavier burden in demonstrating that a merger proposal is in the public interest.

**Enhancement of Competition.** The Board recognized that any further consolidations in the rail industry are likely to result in some competitive harms, such as the loss of geographic competition, that are difficult to remedy directly. Because of this problem, and because of the likelihood based on past experience of harms from service disruption during the integration period, the Board proposed that it would require merger applicants in the first instance to include provisions for enhanced competition as an essential aspect of their proposals. The Board would give substantial weight to this enhanced competition in making its public interest determination.

At a minimum, the Board would require applicants to propose specific remedies to keep open major existing gateways, retain build-out and build-in options, and preserve the opportunity of shippers in the so-called bottleneck situation to obtain a contract rate for one segment of a movement in order to separately challenge a rate for the remainder of the movement. The Board also would look for other competition-enhancing proposals, such as those related to paper barriers, emphasizing that it encourages innovative ways of enhancing competition throughout the network. The Board noted that, given the import of future consolidation, it was no longer appropriate to limit the focus of its conditioning power to preserving competition and essential services, and that it would impose conditions as necessary to mitigate or offset all types of harm to the public interest, including conditions that would enhance competition. In this regard, it would look carefully at the proposals made by the applicants to enhance competition.

**Assessment of Benefits.** The new rules recognize that there can be economic efficiencies associated with consolidations. However, because claimed benefits in recent mergers have often been delayed or frustrated by transitional service problems, the Board would carefully scrutinize future claims of merger benefits and associated timeframes to ensure that they are well-documented and reasonable projections. The Board would expect applicants to propose additional measures that the Board could take if the anticipated public benefits should fail to materialize in a timely manner. Additionally, the Board would view proposals to enhance competition as public benefits, and the Board would consider whether the benefits of the particular consolidation claimed by the applicants could be realized by means short of a merger through private-sector initiatives, such as joint marketing agreements and interline partnerships.

**Downstream Effects.** The Board also noted that, with only a handful of major railroads remaining, any further merger proposals could trigger other applications that the Board would have to consider. The Board recognized that a transaction involving two Class I rail carriers will affect the entire transportation system, including regional and shortline railroads, highways, waterways, ports, and airports. The Board cautioned that "we must be confident that at the end of the day a balanced and sustainable rail transportation system is in place." Thus, the Board would assess the likely outcome of any major proposal on the future structure of the industry through an examination of its downstream effects.

**Service and Oversight.** Applicants would be required to submit up front detailed service assurance plans, including contingency plans, to permit the Board's staff to assess proposed consolidated operations prior to approval. As part of this process, the Board would expect a discussion of specific service levels to be attained from the proposed transaction. The Board would expand its post-approval monitoring of the implementation of mergers to help ensure that adequate service is provided during the crucial transitional period and beyond. Additionally, applicants would have to establish problem resolution teams and specific problem resolution procedures to ensure that post-merger service problems are promptly and appropriately addressed. The Board would anticipate the establishment of a Service Council consisting of shippers, railroads and other interested persons in each merger proceeding to provide an ongoing forum for the discussion of implementation issues for that transaction. And the Board's proposal would formalize the role of oversight in the merger approval process, with successful applicants required to submit reports on no less than an annual basis, subject to comment by the public, for a period of at least 5 years.

**Employee Concerns.** The Board emphasized that it strongly supports early notice and consultation between the railroads and their employees, and that it prefers negotiated solutions to merger implementation problems. The Board also said that it "respects the sanctity of collective bargaining agreements" and that these should not be changed "except to the very limited extent necessary" to implement a particular transaction. In this regard, the Board urged the railroads and the various rail unions, building upon prior efforts, to negotiate systemwide agreements concerning these issues, and to report back to the Board as soon as possible.

**Transnational Issues.** The proposed rules also reflect additional attention to international issues related to applications involving Canadian and Mexican railroads. The Board would require applicants to cooperate with the Federal Railroad Administration concerning safe implementation of those transactions, and would require applicants to show that any applications approved by the Board are consistent with the North American Free Trade Agreement and would not undermine the Nation's defense needs.

The NPR was issued today in the case entitled *Major Rail Consolidation Procedures*, in STB Ex Parte No. 582 (Sub-No. 1). Vice Chairman Burkes and Commissioner Clyburn commented with separate expressions. The NPR follows the Board's March 31, 2000 Advance Notice of Proposed Rulemaking (ANPR) in that docket. In the ANPR, the agency instituted a rulemaking and sought public comment on modifications to its regulations governing proposals for major railroad consolidations. The ANPR followed March 7-10, 2000 public hearings held by the Board in the case entitled *Public Views on Major Rail Consolidations*, in STB Ex Parte No. 582.

Comments in response to the NPR are due on **November 17, 2000**, replies are due on **December 18, 2000**, and rebuttal comments are due on **January 11, 2001**. The Board will issue its final rules by **June 11, 2001**.

Printed copies of the NPR are available for a fee by contacting **D~To-D~ Office Solutions, Room 405, 1925 K Street, N.W., Washington, DC 20006**, telephone **(202) 466-5530**. The NPR also is available for viewing and downloading via the Board's website at **www.stb.dot.gov**.

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