

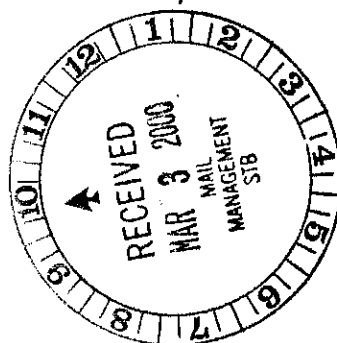
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PUBLIC VIEWS ON MAJOR RAIL CONSOLIDATIONS:

THE VIEWS OF THE STATE OF ILLINOIS
February 29, 2000



The Illinois Department of Transportation (IDOT) is the agency within the state of Illinois statutorily responsible for monitoring and improving rail transportation, as well as for formulating the state's position on rail mergers, acquisitions, abandonments and bankruptcies and recommending to the Governor what positions the State should take on such consolidations. The department appreciates this opportunity to present its views on what has become a virtual tidal wave of railroad mergers, acquisitions and consolidations. The proposed acquisition of the Burlington Northern Santa Fe Railway by Canadian National Railway is only the latest in a recent series that has seen the Union Pacific acquire the Chicago NorthWestern and then the Southern Pacific; the acquisition of Conrail by Norfolk Southern and CSX Corporation; and the acquisition of the Illinois Central Railroad by Canadian National. Each of these acquisitions has had impacts on the rail transportation system, on rail traffic flows, and, in particular, on the heavily-used and already congested Chicago terminal area. One conclusion must be stated at the very beginning of this statement: none of these acquisitions has improved the flow of rail traffic across Chicago, although each consolidation touted that goal as a potential benefit.

Illinois, as the rail hub of the United States, experienced firsthand the problems that resulted from the western and eastern mergers via delays in servicing our industries and agricultural constituents, not to mention lost trains, trains parked due to a lack of power or "dead" crews, near-violent arguments between railroads, and a genuine diminution of competition. We are concerned that one arm of the federal government, the Surface Transportation Board, continues to allow consolidation in an industry whose cost-of-entry is too high to allow any meaningful new competition to emerge, while other arms of the government act to force divestitures and the breakup of companies in much more competitive arenas. A coherent national policy on railroad consolidations is needed, and we believe this hearing (and, we hope, others to follow) can be of exceptional benefit to the country, especially in dealing with rail mergers in rail terminal areas.

The Chicago rail gateway is critical to the economic health of the nation. Every Class I carrier except the Kansas City Southern operates in Chicago (and it has a marketing alliance with Illinois Central to connect its traffic to Chicago). As one of the major points of interchange for freight traffic in the US, Chicago forms an essential link in the nation's freight rail infrastructure. It is said that virtually all containerized traffic passes through Chicago on at least one leg of its journey. The rail lines linking the major railroads in Chicago are among the busiest and most congested in the country, with significant growth in the volume of freight traffic moving through the area, including altered interchange patterns resulting from the recent Conrail transaction.

In addition, it is well to remember the extent to which passenger rail carriers depend on the same tracks and facilities as the freight carriers. Chicago's commuter rail carrier, Metra, operates a heavy pattern of passenger trains over twelve different rail corridors in the Chicago area, with ten of those corridors at least partially owned by freight railroads. Nearly 150,000 people patronize Metra trains daily. Amtrak, which operates 50 daily trains into and out of Chicago over freight-carrier-owned corridors, serves nearly three million people annually at Chicago's Union Station. Freight congestion, especially due to cross traffic at interlockings, is a growing concern as it impacts more and more on passenger train reliability.

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The state of Illinois and the city of Chicago have not stood idly by while rail congestion has worsened. Our first priority for the last twenty years has been the financial health of the railroads themselves. Quite simply, this was a necessary reaction to the wave of even-more-disruptive railroad bankruptcies we went through with the Rock Island, the Milwaukee Road, and the Penn Central, and the near-bankruptcy of the Chicago NorthWestern and Illinois Central. Where we could help financially, we did so. Where we thought that a merger or other consolidation would save rail service by strengthening the underlying economics of a particular railroad, we supported it. Even where the only answer seemed to be abandonment of uneconomic lines, we supported the action while softening the blow to the remaining shippers or local governments by providing capital and the impetus needed for the formation of shortline or regional carriers. As a result of deregulation and enlightened governmental responses, however, the railroad financial crisis was eliminated. It is time for government to rethink its position on railroad institutions.

For one thing, it should be clear that mergers or acquisitions driven by stock market considerations instead of compelling transportation market considerations are a mistake, and only muddy the waters for those trying to make a sensible network emerge from the competitive efforts of disparate parties. The "Invisible Hand" only works when there exists a sufficient number of competitors in the marketplace, acting rationally. The consolidations in the industry seen in the last five years have perhaps already limited competition too much. At the very least, this should be a time for railroads to consolidate their gains, not increase risks for more expansion. More work needs to be done to improve freight train operations and service in and around Chicago. Another wave of mergers could draw the attention of railroads away from continuing their efforts to improve their existing networks. This could well lead to a national crisis as the UP/SP merger and the Conrail/Norfolk Southern acquisition led to local crises in Houston and Elkhart, IN.

The proposed acquisition of Burlington Northern Santa Fe (BNSF) by the Canadian National (CN) is a good case in point. Because Chicago is a significant connection point for BNSF and CN, there is a risk that the transaction will increase traffic volume and congestion. Even if the overall numbers of trains do not change, traffic patterns will. Meanwhile, rail operations in the Chicago terminal area are still adjusting to the changes caused by the recent Conrail transaction. Those impacts were severe enough to cause the freight railroads to initiate an unprecedented cooperative effort to coordinate their operations in Chicago. A consolidated operating center has been established (at Metra) where operating managers share information to improve traffic flows. This effort is in its infancy, with the eastern railroads, in particular, still wrestling with their integration of the Conrail transaction, and the commitment of some of the carriers is still suspect, but at least something is being done to recognize the problems. We fear that introducing another merger-related change in traffic volume and traffic patterns could impede traffic flows for all carriers in the area by adversely affecting the new railroad industry cooperative operating compact in Chicago.

While it is far too soon to predict that the BNSF/CN transaction will cause such problems, the complex nature of the rail operations in and around Chicago and the critical nature of the Chicago terminal lines suggest that this should be closely studied by the Board before it reaches a final decision on the BNSF/CN proposal.

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An excellent example of how such concerns play out in reality can be drawn from the longstanding efforts of the State and the city of Chicago to reroute traffic (particularly CN traffic over its subsidiary Illinois Central) that now moves over the St. Charles Airline route along Lake Michigan, virtually in downtown Chicago. Public agencies in Illinois have been working for years with Illinois Central and the other railroads (including CN, Norfolk Southern, BNSF, Union Pacific and CSX) to create an alternative route to replace the St. Charles Airline, thus diverting freight trains away from the lakefront area and the McCormick Place convention facility. This marks the fourth such effort in the last twenty years, and has come the closest to success, or had done so, before the latest proposed merger was announced. The greatest challenge of this railroad relocation project laid not in the cost, although as much as \$100 million is involved, but in getting all of the railroads involved to agree to cooperate. From the smallest impact – the CSX had to allow itself to be crossed by a new bridge, and two shortlines and a regional carrier with trackage rights over the old Airline had to agree not to fight its abandonment – to the largest (Norfolk Southern agreeing to give up 3000 feet of track in one area and allowing its bridge across the Dan Ryan Expressway to be used by CN/IC) – the City and State negotiated terms and made the necessary concessions and commitments. Financially, CN/IC agreed to contribute in the neighborhood of \$20 million to match a like City investment. The State, Metra, and Amtrak agreed to contribute \$13 million more.

Related projects to improve other bottlenecks in Chicago accredited to the basic relocation project, including an unprecedented joint City/State/railroad effort to secure federal help to grade-separate the Englewood Interlocking, where 68 daily Metra trains cross the path of 45 Norfolk Southern trains plus 16 daily Amtrak trains. The relocation of the St. Charles Airline would add another 4 Amtraks and 12 CN/IC trains to freight corridor, while the relocation would also involve adding 12 daily Metra trains across the interlocking. Including the relocation of this Metra service and the Englewood Flyover costs, plus automation of the second-worst interlocking in Chicago to the St. Charles Airline project drove the costs up, but resulted in a true cooperative effort where every party stood to win. The impact of the proposed BNSF/CN acquisition on those carefully drawn plans and painful compromises made by the railroads and the public agencies needs to be carefully assessed before the potential value of the merger can be determined.

In conclusion, while the state of Illinois has not yet reached a final position on the proposed BNSF/CN consolidation, we have examined it enough to know that the transaction raises serious issues and deserves the most deliberate and extensive assessment by the Surface Transportation Board. Similarly, while the BNSF/CN transaction is not the only reason for the present hearing, it has given rise to concerns that were already building from the UP/SP and Conrail transactions, concerns that need exploration and resolution by the Board. We thank the Board for this opportunity to present, in barest form, our views on the continuing consolidation of the North American railroad industry.