

STB

FD

33388 (Sub 39)

2-23-98

E

185900

OPPENHEIMER WOLFF & DONNELLY

1020 Nineteenth Street N.W.
Suite 400
Washington, D.C. 20036-6105

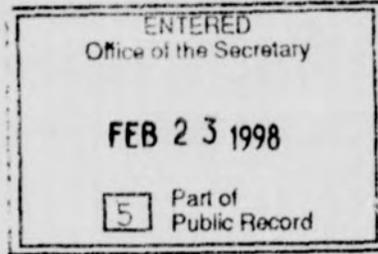
(202) 293-6300
FAX (202) 293-6200

Direct Dial: (202) 496-4906
Email: ksheys@owdlaw.com

February 23, 1998

BY HAND DELIVERY

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



Sub 39

**Re: 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 -- Transfer of Railroad Line by Norfolk Southern Railway
Company to CSX Transportation, Inc.**

Dear Secretary Williams:

Enclosed you will find an original and 25 copies of the Brief of Livonia, Avon & Lakeville Railroad Corporation (LAL-7). 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,

Kevin M. Sheys
OPPENHEIMER WOLFF & DONNELLY

Enclosures

cc: All Parties Referenced in Certificate of Service



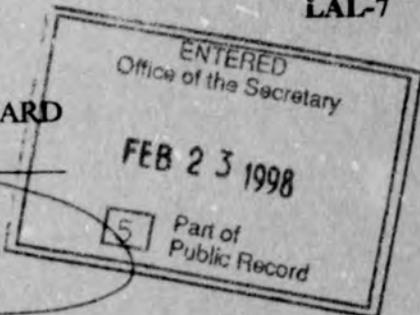
185900
E

- Brussels
- Chicago
- Detroit
- Geneva
- Irvine
- Los Angeles
- Minneapolis
- New York
- Paris
- Saint Paul
- San Jose
- Washington, D.C.

185900

LAL-7

BEFORE THE
SURFACE TRANSPORTATION BOARD

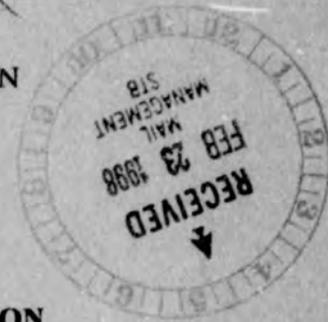


FINANCE DOCKET NO. 33388

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. 33888 (SUB-NO. 39)

LIVONIA, AVON & LAKEVILLE RAILROAD CORPORATION
--TRACKAGE RIGHTS OR OWNERSHIP--
LINES OF CONSOLIDATED RAIL CORPORATION



**BRIEF OF
LIVONIA, AVON & LAKEVILLE RAILROAD CORPORATION**

Conrail E-mail, dated October 19, 1994:

From: Jim Hartman
Subject: Rochester Cluster - Cutline.
Lee, the Division has asked that we adjust the cutline on the Rochester Cluster to MP 361.45 This would leave us with a firewall of .44 miles and two bridges between the cutline and Genesee Jet Yd. (Rochester Southern)....

Sergeant W. Wise
Livonia, Avon & Lakeville Railroad Corporation
5769 Sweeteners Boulevard
P.O. Box 190-B
Lakeville, NY 14480
(716) 346-2090

Kevin M. Sheys
Christopher E.V. Quinn
Oppenheimer Wolff & Donnelly LLP
1020 Nineteenth Street, N.W.
Suite 400
Washington, DC 20036-6105
(202) 496-4906

**ATTORNEYS FOR LIVONIA, AVON &
LAKEVILLE RAILROAD CORPORATION**

Dated: February 23, 1998

TABLE OF CONTENTS

	<u>Page</u>
INTRODUCTION AND SUMMARY	1
STATEMENT OF FACTS	2
I. The Genesee Junction Firewall	2
II. Support For Eliminating The Firewall	4
ARGUMENT	7
I. THE CONDITION REQUESTED BY LAL FITS SQUARELY WITHIN THE BOARD'S CRITERIA FOR IMPOSITION OF CONDITIONS IN RAILROAD MERGERS	7
A. Applicable Standard for Imposition of Conditions	7
B. The Conrail Takeover Will Harm Industries Served by LAL	8
1. Diversion of Resources Away From CSX/LAL Joint Line Service	8
2. Substitution of Joint Line For Single-Line Service	12
3. Elimination of Neutral Gateways	14
C. Professor Kalt's Analysis and the Applicants' Promises Do Not Obviate the Need for a Competitive Check for Transaction-Related Harms	15
D. LAL's Requested Condition Will Ameliorate the Demonstrated Harms	16
E. LAL's Requested Condition Is Narrowly Tailored To Remedy the Demonstrated Harms	17
F. LAL's Requested Condition Is Operationally Feasible	17
G. LAL's Requested Condition Will Not Diminish the Benefits of the Conrail Takeover	20

II. THE BOARD SHOULD USE ITS BROAD DISCRETION
TC IMPOSE A NARROWLY TAILORED CONDITION TO
ELIMINATE A GOVERNMENT-CREATED FIREWALL
THAT IS NO LONGER NEEDED20

CONCLUSION24

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. 33888 (SUB-NO. 39)

LIVONIA, AVON & LAKEVILLE RAILROAD CORPORATION
--TRACKAGE RIGHTS OR OWNERSHIP--
LINES OF CONSOLIDATED RAIL CORPORATION

BRIEF OF
LIVONIA, AVON & LAKEVILLE RAILROAD CORPORATION

INTRODUCTION AND SUMMARY

The takeover of Conrail by CSX and Norfolk Southern (hereinafter, "the Primary Applicants" or "Applicants") represents one of the most significant rail mergers in history. Parties on all sides agree that it is a transaction, which, if approved, will permanently change the freight railroad industry in the United States. The primary public benefits claimed by the proponents are that it will create new single-line routes for freight rail transportation and that it will open up major portions of the Northeast to rail competition for the first time in 22 years.

The Livonia, Avon & Lakeville Railroad Corporation ("LAL") believes that the Conrail takeover, as proposed, would significantly reduce competitive options for the shippers it serves. LAL has identified specific harms arising from the Conrail takeover which can be ameliorated if the Surface Transportation Board grants the relief requested in LAL's Responsive Application. See Responsive Application of Livonia, Avon & Lakeville Railroad Corporation for Trackage Rights or Ownership, LAL-4 ("LAL Resp. App."). The relief sought by LAL is operationally feasible and enhances rather than reduces the public benefits of the proposed Conrail takeover.

STATEMENT OF FACTS

I. THE GENESEE JUNCTION FIREWALL

LAL was organized in 1963 as a community effort to save branchline trackage proposed for abandonment by the Erie-Lackawanna Railroad ("EL"). LAL is a Class III railroad which owns and operates 29.4 miles of lines between Genesee Junction Yard in the Town of Chili, New York (immediately south of Rochester) and Lakeville, New York. LAL has 17 full-time employees and is owned by some 520 stockholders.

LAL originally operated between its namesake towns, interchanging cars with EL at Avon, New York. EL operated the line from Avon westward to Caledonia, New York, where EL intersected branchlines of both Penn Central and Chessie System. As an economic subsidy to prop up a fledgling Conrail in 1976, the United States Railway Association decided to have Conrail serve Avon from Rochester, inserting a competitive "firewall" 2/10ths of a mile long between the LAL/EL connection (milepost 366.2) and the east end of EL's Avon-Caledonia line (MP 366.4). Simultaneously, it rendered EL's Avon customers captive to Conrail. Verified Statement of William D. Burt, LAL-4, ("Burt VS") at 6.

In 1993, Conrail approached LAL with a proposal to sell its Avon-Genesee Junction trackage to LAL.¹ Badly deteriorated after years of neglect, the line still functioned as the sole outlet for LAL traffic that in 1995 accounted for 84 percent of all cars handled thereon. In the sale negotiations, Conrail representatives made it clear that the firewall would simply be moved north. Burt VS at 4.

Genesee Junction Yard thus became the new firewall when LAL acquired Conrail's "Rochester South Cluster" in 1996. Although LAL's acquisition of the line conveyed ownership of trackage reaching the east end of Genesee Junction Yard, Conrail retained the yard itself in order to block LAL from connecting with the RSR, a Class III carrier that acquired Chessie System's line between Rochester and Silver Springs, New York in 1986. RSR connects to the west end of Genesee Junction Yard and, like LAL, holds rights to operate in Genesee Junction Yard. At Silver Springs, 44 miles south of Genesee Junction Yard, RSR connects with Canadian Pacific and Conrail's "Southern Tier Line." The Southern Tier route will be allocated to Norfolk Southern as part of the proposed division of Conrail's assets.

As part of its acquisition of the "Rochester South Cluster," LAL was permitted to operate throughout Genesee Junction Yard for purposes of interchange with Conrail. Thus, while LAL

¹ Applicants' rebuttal refers to "LAL's efforts to buy access to other carriers at Genesee Junction Yard" and state that "on two occasions" LAL unsuccessfully sought to acquire the yard. Applicants' Rebuttal CSX/NS-176 ("App. Reb."), at 372. This misrepresents the factual record that LAL's interest in acquiring the yard was expressed as part of an ongoing negotiation that Conrail initiated in late 1993, which continued until the Avon-Henrietta line was sold in early 1996, and in which LAL participated under the duress of mounting service interruptions and threatened sale of the line to another railroad. The accompanying claim that Conrail turned down LAL a third time in 1996 is totally unfounded. LAL Resp. App., 7-8. Applicants' assertion that LAL is attempting to revise bargained-for terms is similarly unfounded. See Rebuttal Verified Statement of William D. Burt, LAL-6, ("Burt RVS") at 12-15 for discussion.

and RSR can both operate in Genesee Junction Yard, Conrail prohibits LAL and RSR from interchanging cars with each other.

II. SUPPORT FOR ELIMINATING THE FIREWALL

Traffic interchanged between Conrail and LAL at Genesee Junction Yard amounted to 2,295 cars in 1995, which was 56 percent more than five years before. Recognizing LAL's 34-year record of growth based on high levels of service, *Railway Age* magazine named LAL "Short Line Railroad of the Year" for 1997.

LAL service is essential to the survival and competitiveness of food processing and agricultural businesses, as well as other local industry, in the greater Rochester region. Accordingly, all--nine out of nine--of LAL's customers have come forward in strong support of LAL's Responsive Application. See LAL Resp. App., Exhibits 23-24. None of these customers' facilities has access to other rail carriers, and given the costs of alternative modes, all are dependent on LAL for service. Notably, the Primary Applicants have failed to garner the support of even one of the industries served by LAL. This uniform support for LAL's Responsive Application is telling.

For example, Sweeteners Plus Inc. depends on LAL rail service for its operation of a large sweeteners processing plant at Lakeville that receives cars of corn syrup and sugar by rail. Its President, Carlton E. Myers, has submitted a verified statement explaining that trucking is not a feasible alternative to LAL. He states that:

Our Lakeville facility could not exist without access to efficient, highly responsive, and low cost transportation. Truck transportation of inbound corn syrup and sugar is comparatively costly due to the superior weight-carrying capacity of rail cars. If Sweeteners Plus did not have efficient rail service to its Lakeville facility, rates for truck transportation of corn syrup and sugar would drive up the costs of our [products]. Sweeteners Plus is not in a position to absorb increased

transportation costs while attempting to continue to compete with sweeteners products produced by other companies.

Verified Statement of Carlton E. Myers ("Myers VS") at 1. Mr. Myers further emphasizes that LAL's "on-demand" switching and related services make it possible to respond in a timely way to the demands of its customers. Sweeteners Plus recently expanded its Lakeville sweeteners plant and is diversifying its operations by building another new facility to handle a new product. Myers VS at 2, Burt VS at 7.

Similarly, George Bagley of ADM Corn Processing has submitted a verified statement attesting to his facility's dependence on LAL, due to the fact that "Inbound truck transportation would be impossible and noncompetitive because of the weight carrying capacity of the rail cars and the long distance from our parent company refineries." Verified Statement of George Bagley ("Bagley VS") at 1. ADM Corn Processing operates a sweeteners processing facility at Lakeville that receives cars of corn syrup by rail and ships the processed product over the highway.

Ag Network Incorporated operates a grain (corn and wheat) processing and transshipment facility that was constructed in 1994 near Lakeville. Construction of this facility required LAL to rehabilitate and restore to service about a mile of disused, overgrown track. Due to the commodity nature of its business, Ag Network cannot operate without access to competitively priced rail service. Burt VS at 7. As Ag Network's President, Les Cole, makes clear, his company is dependent upon LAL's service and "cannot exist without access to efficient, highly responsive, and low cost transportation." Verified Statement of Les Cole ("Cole VS") at 2.

In addition to these and all of the other local industries served by LAL, LAL's Responsive Application is vigorously supported by the State of New York, the Genesee Transportation

Council (the regional planning agency having responsibility for transportation planning in the Rochester area), the Business Council of New York, the Livingston County Chamber of Commerce, the Livingston County Board of Supervisors, and the Livingston County Industrial Development Agency. See LAL R. 3p. App.

New York State's Comments on LAL's Responsive Application, ("NY^c Comments"), NYS-20, urges the Board to grant LAL's requested conditions. New York emphasizes that state and federal programs have provided tens of millions of dollars to assist New York's short line railroads, including LAL, and notes that:

Unlike CSX--who would hold the yard solely as an anti-competitive firewall--LAL has a significant interest in the upkeep of Genesee Junction's yard and facilities.

Conversely, the only lost "benefits" the Applicants could claim as a result of LAL's proposed relief are "private" benefits rather than public, in the form of monopoly profits collected on captive LAL traffic and investments saved through lower-quality service to LAL shippers. Such "benefits," however, do not weigh against imposition of LAL's requested condition; as the Board has specifically stated, "benefits to...combining carriers that are the result of increased market power, such as the ability to increase rates at the same or reduced service levels...detract from any public benefits associated with a control transaction." Thus, on balance, LAL's Responsive Application seeks relief that serves the public interest, and imposes no burden upon any public benefits that the Applicants' transaction might otherwise produce.

NYS Comments at 14-15 (footnotes and citations omitted)

CSX proposes to acquire Conrail's "Water Level Route" from New York City and Northern New Jersey to Buffalo, New York via Albany and Rochester, including Genesee Junction Yard. LAL's Responsive Application seeks elimination of the Genesee Junction firewall as a narrowly-tailored remedy to transaction-related harms.

ARGUMENT

I. THE CONDITION REQUESTED BY LAL FITS SQUARELY WITHIN THE BOARD'S CRITERIA FOR IMPOSITION OF CONDITIONS IN RAILROAD MERGERS

A. Applicable Standard for Imposition of Conditions

The Board's authority to impose conditions on rail consolidation transaction is broad.²

Setting aside (for the moment) the unique aspects of this case,³ the Board prescribes conditions only upon finding that:

- 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 condition will yield public benefits outweighing any reduction in the benefits of the railroad consolidation.

As explained below, LAL's requested condition meets each of these criteria and therefore should be granted.⁴

² 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. 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*").

³ But see Section II of this Argument.

⁴ In their Application and Rebuttal, the Applicants attempt to rewrite the standard to be applied, adding provisions that are not part of the caselaw. For example, Applicants state that a condition "may not be imposed to change the competitive balance among shippers." App. Reb. at 42. However, the standard as determined by the Board is a different one. The Applicants themselves quote the real standard from the *BN/SF* case that the Board is "disinclined" to grant a condition that "would broadly restructure the competitive balance among railroads." *BN/SF* at 55-56. App. Reb. at 37. Applicants again fail to follow

B. The Conrail Takeover Will Harm Industries Served by LAL

LAL represents the only rail service to all nine of its on-line industries, which comprise an important part of the Rochester regional economic base. See Verified Statement of Comments and Request for Conditions of the Genesee Transportation Council, GTC-2, at 8. LAL has demonstrated that it is a vital link for its shippers, and that there exists no viable transportation alternative to LAL's rail services for these industries. Burt VS at 7-10. These points are unrebutted by the Primary Applicants.⁵

LAL has identified three categories of specific harm resulting from the Conrail takeover:

1. Diversion Of Resources Away From CSX/LAL Joint Line Service

It is standard economic analysis that a monopoly will tend to divert scarce resources away from captive markets to competitive markets. This analysis has not been rebutted by the Applicants.

Railroads must cooperate to handle interline traffic. Allocation of resources needed to support traffic handled jointly by two or more railroads takes place in a process of ongoing negotiation where the parties share a common but unequal incentive to win the business and opportunities exist to shift costs to the other "partner." Burt RVS at 8. As between Class I

BN/SF when they state that "conditions are not appropriate if alternative remedies exist." App. Reb. at 40. Nowhere in *BN/SF*, *UP/SP* or other merger decisions is such a rule articulated. Instead, a condition must be "narrowly tailored." *BN/SF* at 55-56. Even under Applicants' view of the law, LAL meets the criteria inasmuch as LAL's requested condition protects LAL shippers against the loss of routing options they currently enjoy. Furthermore, it is the most narrowly tailored condition available, involving less than a mile of track that is used for no other purposes than interchange of cars between LAL and Conrail and access by RSR to a nearby industrial spur, which uses will be unaffected by LAL's requested condition.

⁵ Applicants' response to the concerns expressed by LAL's customers is to dismiss them, without foundation or analysis, as "speculative." App. Reb. at 373

railroads and short lines, the process is especially unequal because the Class I can easily walk away from smaller-volume business that would be vital to the short line.⁶

To the extent that the Applicants deal with this issue at all, they caricature it as an allegation by LAL that CSX will be more likely to "diminish the level and frequency of interchange with LAL." App. Reb. at 373. Inasmuch as the Conrail takeover is supposedly focused in part on service improvements, this kind of dumbing-down of the discussion is disappointing. Applicants' executives give speeches about conquering the next frontier of improved earnings through better service and increased market share, through becoming more "truck-like," and through assuming responsibilities for managing customers' logistics. Then they present to the Board a rebuttal reflective of rail industry attitudes of fifty years ago: "Does the train show up three times a week? . . . Is the track still there?"

Like many other short lines, LAL is already doing many of the things to create customer value that Class I railroads talk about. Some LAL customers require just-in-time service and expect LAL to operate special trains when even one "shutdown" car misses its expected delivery date. LAL also adds value by performing on-demand switching, managed car storage, transload services, coordinated rail/truck movement, product inventory management, temperature checks, car heating, and other ancillary services. LAL-served industries also derive value from the fact that LAL shields its customers from unacceptably common errors in Class I railroad rating and billing, forestalling disputes. Burt VS at 10.

⁶ As further explained in the Burt RVS at 9, note 5, the bargaining is made even more lopsided where the Class I has the power and incentive to divert short line traffic and industrial development prospects to distribution facilities, transload terminals, and industrial sites directly served by the Class I, which already largely controls the pricing and service of any joint-line service they might offer.

In fact, the viability of the competitive transportation options LAL offers to its shippers, and in the long run of LAL itself, is more than ordinarily dependent on these innovative services. Burt VS at 11-18. But LAL's ability to offer high levels of service depends partly on the degree of cooperation it receives from its Class I connection. Additionally, LAL's traffic is heavily weighted to food and agricultural commodities with high service requirements and/or thin margins, and many moves are short haul. See LAL-4, Exhibits 23-24.

In this context, therefore, the issue of whether each partner to the Class I/short line relationship fully supports the service they jointly offer is a bit more complex and pressing than acknowledged by the Applicants. The relevant "resources" include capital investments and operating expenditures for:

- a) Maintenance and operation of yards or tracks used for interchange at levels consistent with safety and customer requirements.
- b) Operating personnel and fixed plant investments to permit the Class I's major classification yards to make blocks at the appropriate locations rather than haul a short line's cars back and forth across the landscape simply because the Class I wants to economize on yard expense and capital investments.
- c) Operating personnel and equipment to provide appropriately fast, frequent, and reliable connecting train service--particularly with respect to the "way freights" and other lower-priority freight trains that represent the actual interface with short line train operations.
- d) Marketing personnel and systems to provide timely and competitive responses to requests for price/service quotations and deal with other business development issues.
- e) Customer service personnel and systems to deal with car tracing, claims, and other related issues in a way that exceeds customer expectations.
- f) Administrative personnel and systems to deal with billing, revenue settlement, and other accounting issues on a timely and accurate basis.
- g) Joint efforts at industrial development.

An inspection of the foregoing list makes it apparent that the ways in which resources can be rationed and reallocated are manifold and subtle. If Conrail is broken up in such a way that certain customers and short lines gain new access to competitive rail service, the tendency of Conrail's successor to divert resources away from captive markets will be exacerbated as newly competitive markets (such as Northern New Jersey) make fresh demands on the railroad's capabilities and it responds to these demands, lest it lose market share. Where the markets that gain new access to intramodal competition are large, as in this case, the diversion of resources will be significant, and remaining captive short lines (such as LAL) will find it even more difficult than before to persuade the successor railroad to do its part in supporting their joint line business. For example, interchange tracks will receive minimum maintenance and connecting local freight service will be cut back while capital is poured into double-tracking main lines and raising speeds to permit 70 MPH intermodal trains to fly between Chicago and North Jersey. Administrative support functions for captive business will be skeletonized while marketing and industrial development resources are lavished upon markets enjoying railroad competition. LAL Resp. App. 11-13; Burt VS at 12-14. In the extreme, CSX will have the power to unilaterally and coercively rewrite the terms of doing business, as Conrail attempted to do with "Conrail Express." Burt VS at 15-17.

The difficulty captive customers face will be further exacerbated when the remnants of Conrail are merged into two much larger railroads that are already generally competitive throughout the Eastern United States, pitting the resource requirements of captive customers inherited from Conrail against those of a now substantially larger customer base enjoying access to competitive railroad service.

Applicants' only reply to this allegation of transaction-related harm is to assure the Board that "CSX will be assuming Conrail's existing agreements with LAL, and while these agreements are in effect, CSX will abide by their terms." App. Reb. at 373. Applicants' boilerplate assurances are simply not responsive. Apparently, they are unaware that Conrail has no relevant agreements with LAL. Applicants say nothing to rebut LAL's evidence regarding the likelihood of increased diversion of resources, or to give LAL's customers any reason to believe that CSX will address their requirements in the same manner as it will address those of shippers in, say, Northern New Jersey.

2. Substitution Of Joint Line For Single-Line Service

LAL has identified certain traffic that the proposed transaction will convert from single-line to CSX-NS joint-line service, to the detriment of industries and agricultural producers served by LAL. Where this traffic currently moves single-line Conrail to or from the LAL, it will be necessary to interline between CSX and NS in the future. Movements include grain shipments to Conrail points on the Delmarva Peninsula and in Pennsylvania that will become Norfolk Southern points. The duplicative costs and additional interchanges attendant upon CSX/NS service will effectively kill LAL-originated shipments of grain to these points, depriving Western New York farmers of an outlet for their products and poultry producers of a competitive source of feed. Burt VS at 19.

The Applicants failed to rebut this evidence of harm caused by the proposed transaction. They do not deny that joint-line service is subject to duplicative costs, their own application touts the efficiencies of single-line service, their rebuttal acknowledges that "single-line service is generally preferable to joint-line service," and they are poorly positioned to justify imposing

similar impediments to commerce on others. Rebuttal Verified Statement of John W. Orrison, CSX/NS-177 ("Orrison RVS"), at 146-147. CSX's Executive Vice President for Sales and Marketing further concedes that "there are certain inherent difficulties in achieving joint-line transit times that can match those of single-line service." Verified Statement of John Q. Anderson, CSX/NS-19 ("Anderson VS") at 296. In fact, one of the public interest justifications for the Conrail takeover is based upon the Applicants' claim that expanded single-line service will produce new efficiencies and divert freight traffic to rail. What is good for the goose is good for the gander, however. They cannot tout the public interest benefits for intermodal customers in Jersey City while simultaneously scorning the petition of carload freight customers in Rochester.

Substitution of joint-line for single-line service results in adverse impact for all the reasons identified in the Verified Statement of Darius W. Gaskins, Jr., CSX/NS-19 ("Gaskins VS"), at 12-15. Moreover, as Mr. Gaskins observes, joint-line service is particularly problematic with short and medium-haul lanes and low-margin commodities. *Id.* Inasmuch as the shipments that currently move LAL-Conrail are inherently short-haul and often involve agricultural commodities, Gaskins' comments apply directly. Any decrease in car utilization or degradation of other service parameters such as reliability, transit time, ease of car tracing, billing accuracy, resolution of freight claims, and other factors driving transaction costs will usually be sufficient to render the route useless to the customer. Thus, the oft-repeated mantra that there is no harm because "shippers will have the same number of rail options at origin and destination" (App. Reb. at 490-492) sidesteps the fact that transportation is a business of moving goods between origin and destination and that counting the number of options at each point is irrelevant if degraded service effectively closes some routes between them.

Given that the overriding themes of the Conrail takeover stress the introduction of competition and efficient new single-line routes to the Northeast, the Applicants' willingness to impose joint-line service on some customers and short lines constitutes nothing more than a hypocritical cold shoulder.

3. Elimination Of Neutral Gateways

LAL has identified certain traffic that the proposed transaction will convert from NS-Conrail joint-line service to NS-CSX joint-line service, again to the detriment of LAL customers. Whereas Conrail has long held itself out to be the "neutral" carrier for the Northeast, it will now be necessary to interline between two archrivals, CSX and NS. Movements include corn syrup shipments from plants solely served by NS at Lafayette, Indiana and Decatur, Alabama. Burt VS at 19.

In addition, the loss of a neutral connection (Conrail) willing to work with NS frustrates any realistic possibility that ADM Corn Processing's Lakeville facility can be linked via NS to ADM's large plant at Decatur, Illinois. As noted in the Burt VS at 20, Norfolk Southern's 1996 annual report announces that ADM has selected NS to expand service to its Decatur, Ill. plant, which "means the addition of numerous lanes for NS...[including] sweeteners." The fact that Lakeville is frozen out of this deal cannot bode well for the future.

Making LAL dependent upon joint-line service requiring the cooperation of two rival carriers fatally injures the viability of some of the routings LAL is able to offer its customers. As such, it injures the competitiveness of LAL and the industries it serves. CSX and NS agree that they will be fiercely competitive with each other following the division of Conrail. The notion that CSX-NS interline routings will be transparently equivalent to Conrail-NS service (or single-

line service, for that matter) therefore possesses no credibility.⁷ Burt VS at 20. Moreover, it is at complete variance with the Applicants' insistence that they need to acquire and divide Conrail because the short hauls, excessive costs, and lack of operational control inherent in joint-line operations frustrate truck-competitive rail service.

The Applicants' response to these demonstrated harms is to assert, *ad hominem*, that LAL is "manufacturing" evidence and engaging in "speculation." Instead of attempting to make a substantive response to LAL's evidence, the Applicants have chosen to ignore factual information not to their liking, brushing it off with unsupported, conclusory bluster. They also trot out the irrelevant "compliance with contracts" warhorse mentioned above, and assure the Board that shippers will continue to have the same number of rail options as before. App. Reb. at 374. Unfortunately, in the real world, measuring the effects of the proposed transaction does not begin and end with making sure that the tracks are still in place. Burt RVS at 5-7.

C. **Professor Kalt's Analysis And The Applicants' Promises Do Not Obviate The Need For A Competitive Check For Transaction-Related Harms**

The Applicants cite the Rebuttal Verified Statement of Joseph P. Kalt, NS/CSX-177 ("Kalt RVS") in an attempt to rebut LAL's evidence of transaction-related harms. Professor Kalt ignores the specific harms LAL has demonstrated while dismissively alleging, without apparent

⁷ Throughout the process, the Applicants have dealt with the problem of CSX-NS service only grudgingly. The proffered solution--"efficient" CSX-NS routings--is little more than a triumph of hope over experience, and it is a telling detail that the solution is always described in operating terms. Never (to LAL's knowledge) do the Applicants, whose managements reportedly subscribe to the view that railroading should be a market-driven business, state that they plan to aggressively market CSX-NS joint-line service, and it is highly doubtful that they have any such plans. Accordingly, such service will surely die out in time, as did the Conrail/Delaware & Hudson gateways that were supposed to preserve shippers' routing options after Conrail was created.

foundation, that LAL's Responsive Application "inappropriately" engages in "self-serving policy advocacy." Kalt RVS at 13.

Professor Kalt has the unenviable task of explaining the importance of expanding competitive rail service to such markets as Northern New Jersey while attempting to justify the reduction of competitive options currently enjoyed by LAL shippers and imposition of new cost and service burdens on their commerce. Of course, he cannot have it both ways. If expansion of single-line service and its resultant efficiencies are in the public interest, then forced substitution of joint-line service provided by two archrivals for either single-line service or neutral gateways cannot simultaneously serve the public interest. Kalt RVS at 4. Professor Kalt in effect argues that competition is good for some but not for others, and that some customers deserve efficient service while others should be content to accept their fate at the hands of the negotiators for CSX and Norfolk Southern who divided the market as best suited their companies' private interests.

D. LAL's Requested Condition Will Ameliorate The Demonstrated Harms

The Applicants make a simplistic argument that the LAL-RSR-NS routing that LAL seeks would be no better than the LAL-CSX-NS routing with which LAL would be saddled post-merger, absent imposition of LAL's requested condition. As if performing an elementary school addition problem, the Applicants compare the number of carriers in each option. Finding the number the same, they assert that all things must be equal.

Applicants' argument ignores the fact that CSX and RSR have fundamentally different economic incentives and operations, and that they therefore do not represent interchangeable parts of an overall movement. Burt RVS at 7-10. Unlike CSX, RSR is not Norfolk Southern's archrival. Unlike CSX, RSR has no incentive to divert NS-RSR traffic to its own long-haul

routes; indeed, traffic handled between NS at Silver Springs, New York and LAL at Genesee Junction would move over substantially all of RSR's route. *Id.* As the Applicants have themselves stated, short line railroads like RSR can and do provide "seamless" service in conjunction with Class I railroads.⁸ LAL expects that NS and RSR will work closely together to provide such service. *Id.* Finally, LAL management can reach RSR headquarters with a 25-minute drive from Lakeville or a 5-minute drive from Genesee Junction Yard, whereas Jacksonville is hundreds of miles away. *Id.*

E. LAL's Requested Condition Is Narrowly Tailored To Remedy The Demonstrated Harms

LAL requests the elimination of the restriction contained in the interchange agreement between Conrail and LAL that prohibits LAL from utilizing Genesee Junction Yard to interchange traffic with carriers other than Conrail or its successor. This condition is the most narrowly tailored solution conceivable.⁹

F. LAL's Requested Condition Is Operationally Feasible

If LAL's trackage rights request is granted, the east end of Genesee Junction Yard will be used for interchange between LAL and CSX, while the west end can be used for interchange between LAL and RSR. To facilitate operations, LAL is prepared to pay Conrail/CSX the cost of

⁸ See Spring and Summer 1996 Conrail *Partners* newsletters, Fall 1997 CSX *Interchange* newsletter, and NS "Dear Fellow Railroader" letter enclosing a statement of "Our Short Line Principles." Each of these documents is in the LAL document depository.

⁹ LAL's requested condition seeks either trackage rights or ownership. Continued ownership by Conrail/CSX is feasible only if Conrail/CSX upgrades and maintains yard trackage to FRA Class I condition, finally fulfilling Conrail's existing obligation to maintain the yard to a standard adequate to the service. (LAL's position is that FRA "Excepted Track" condition, which has prevailed in Genesee Junction Yard for several years, is by definition a temporary exception rather than an acceptable standard for the long term.) CSX promises to upgrade the yard to FRA Class I and maintain it to that standard. If the Board decides not to grant LAL's requested condition, it should require CSX to abide by its representation on the record.

installing a pair of crossovers midway along the length of the yard, speeding up CSX and LAL operations by cutting approximately in half the time required to run around cars in the yard.¹⁰

Burt VS at 22.

As an alternative, LAL stands prepared to acquire Genesee Junction Yard at a price to be negotiated by CSX and LAL (or, failing a negotiated agreement, to be set by the Board), such conveyance to occur concurrently with the division of Conrail between CSX and NS. This approach would enhance safety inasmuch as LAL, which has the strongest interest in maintaining the yard, would have responsibility therefor.

Citing the Orrison RVS, the Applicants make a feeble assertion that granting the LAL's requested condition "could interfere with CSX's long-term plans to develop traffic in that area." App. Reb. at 375; Orrison RVS at 53. John Orrison urges that "divestiture of the yard or any other order granting LAL unbridled operating rights there should be denied as it might interfere with CSX operations." As for substantiation, there is none. Orrison RVS at 53. If all an applicant had to do was state that any given condition "could" or "might" interfere with unspecified plans, the Board would effectively be powerless to ever condition any proposed transaction. Also, LAL has not requested "unbridled" operating rights. Instead, LAL simply seeks either to acquire Genesee Junction Yard (subject to a grant of trackage rights back to CSX and continuation of RSR's trackage rights) or trackage rights to interchange with RSR directly, with all parties efficiently utilizing the yard. LAL Resp. App. at 13; Burt RVS at 21-22.

¹⁰ On page 51 of his Rebuttal Verified Statement, CSX's John Orrison states that Conrail interchanges with RSR at Genesee Junction Yard and that both LAL and RSR operate "to and from" the yard. Neither statement is correct. In the Rochester area, RSR interchanges with Conrail at Lincoln Park only. As discussed in the text, RSR operates through Genesee Junction Yard to reach a nearby industrial spur, but RSR does not have a base of operations at Genesee Junction Yard.

All three carriers--Conrail, LAL, and RSR--currently operate in Genesee Junction Yard. Conrail has no operations in the yard other than interchange with LAL, and installation of the crossovers required to facilitate RSR/LAL interchanges will actually improve the efficiency of operations for Conrail/CSX and LAL. LAL's analysis indicates that the deferred maintenance liability of the yard exceeds its net liquidation value; i.e., sale to LAL at net liquidation value would leave CSX better off. Burt VS at 21.

This is not North Platte Yard or Selkirk Yard. Rather, the "yard" at Genesee Junction consists of three poorly maintained tracks one mile long. Operations are pursuant to "yard rules" under which train crews operate at Restricted Speed, watching out for other trains; permission is not required to enter the yard and Conrail plays no immediate role in coordinating operations. Conrail does not maintain an on-site yardmaster, a yard office of any kind, or a base of operations for track forces. The yard is unfenced, unlit, unpaved, and open to trespassers. Burt RVS at 12, n.9. For the last several years it has been a haven for gun-toting vandals who shoot up everything (switch targets, abandoned signal cabinets, etc.) in sight, and have lately begun breaking into rail cars and blasting their contents at close range. It is--just so the Board has the real picture--an "urban wasteland" that is landlocked, surrounded by wetlands, and situated beneath the runway approach to the Monroe County Airport. Burt VS at 5.

The lack of any real basis for CSX's concern is also demonstrated by the fact that, to the best of LAL's knowledge, CSX failed to object or otherwise attempt to stop Conrail from concluding the recent sale of the "Rochester Industrial Track" or "Lyell spu" which diverges

from the north side of Conrail's West Shore Branch opposite Genesee Junction Yard.¹¹ As part of this transaction, which LAL understands was finalized in December 1997, RSR began operating through the yard twice daily to reach the Lyell spur. If CSX objected to this new and increased use of the yard, it is not part of the record in the present proceeding.

G. LAL's Requested Condition Will Not Diminish the Benefits of the Conrail Takeover

The Applicants cite as the primary public benefit of the proposed transaction the introduction of "rail competition into areas previously rail-served only by Conrail." App. Reb. at 13. They further emphasize the public benefits of substituting single-line for joint line service, which promotes greater efficiency and better enables the railroads to divert traffic from the highways. App. Reb. at 16. Given this backdrop, the Applicants have not disputed that LAL's requested condition leaves intact the cited public benefits of the proposed transaction.

In fact, LAL's requested condition is entirely consistent with those public benefits. LAL's request preserves competitive routing options currently available to industries served by LAL, thus helping to ensure their viability. The only loss that CSX can cite is the elimination of an economic subsidy formerly granted to Conrail in the form of a firewall. This can hardly represent the loss of a public benefit, nor does the Board recognize it as such. *See BN/SF* at 51.

II. THE BOARD SHOULD USE ITS BROAD DISCRETION TO IMPOSE A NARROWLY TAILORED CONDITION TO ELIMINATE A GOVERNMENT-CREATED FIREWALL THAT IS NO LONGER NEEDED

As an economic subsidy to prop up a fledgling Conrail 22 years ago, the United States Railway Association decided to have Conrail serve Avon from Rochester, inserting a 2/10ths of a

¹¹ *Rochester & Southern Railroad, Inc. -- Acquisition and Operation Exemption -- Consolidated Rail Corporation*, Finance Docket No. 33375 (STB served March 31, 1997).

mile long firewall that prevented LAL from acquiring and operating the line to Caledonia, where competitive connections existed. Following Conrail's immediate withdrawal of twice-daily switching services at Avon, rail traffic there virtually collapsed, leaving a still-struggling LAL to cope with irregular Conrail service over a poorly maintained branch from Rochester. Burt VS at 3-4.

In hindsight, USRA's decision mistakenly elevated concern for Conrail's well-being over the service requirements of customers. As such, USRA's handling of the Avon/LAL situation is part of a larger picture. In its statutory review of the Final System Plan, the ICC concluded that USRA's "Unified Conrail" option was not a satisfactory solution. The Commission stated that Unified Conrail "fails to meet the [Regional Rail Reorganization Act of 1973's] goals of preserving and promoting competition (§ 206(a)(5)) and preserving existing patterns of service (§ 206(a)(4))." ICC, *Evaluation of the U.S. Railway Association's Final System Plan* (1975), 8. The Avon firewall, imposed by governmental action over the vigorous objections of LAL and local industries, is a case in point.

While the Applicants now concede that the Congressionally mandated goal of competition was sacrificed in creating Conrail and ask the Board's approval to rectify that mistake with "the most pro-competitive restructuring in railroad history" (Verified Statement of James W. McClellan, CSX/NS-18, at 5, 50 and 51), the transaction as proposed in its unconditioned form leaves LAL customers captive to Conrail's successor, CSX. On the one hand, the Applicants cite the competitive restructuring of Conrail as the primary public interest justification and, on the other hand, accuse LAL of "relitigating" Conrail's creation. The Applicants essentially assert that it is up to them to decide how much and where competition will exist. In reply, LAL submits that

the Board, not the Applicants, has the authority, obligation, and duty to decide how much competition will remain after the division of Conrail.

The statutory provisions governing the Board's consideration of rail consolidations are set forth at 49 U.S.C. §§ 11321-11327. The central focus in reviewing control applications under the statute is whether the proposed transaction is in the public interest. For example, 49 U.S.C. § 11324(c) states that "[t]he Board shall approve and authorize a transaction under this section when it finds the transaction is consistent with the public interest."

Under the Railroad Revitalization and Regulatory Reform Act of 1976 ("4R Act"), it was "declared to be the policy of the Congress" to "foster competition among all carriers by railroad." *Id.* at § 101(b). This policy of promoting intramodal railroad competition was strengthened by Congress through the enactment of the Staggers Rail Act of 1980, Pub. L. 96-448, and most recently by the ICC Termination Act of 1995, Pub. L. 104-88. Competition is emphasized throughout the statutory and regulatory standards that govern railroad control proceedings before the Board, and competition is at the center of the Board's decision-making process under Section 11324, with Section 10101 directing the Board:

- (1) to allow, to the maximum extent possible, competition and the demand for services to establish reasonable rates for transportation by rail; ...
- (2) to ensure the development and continuation of a sound rail transportation system with effective competition among rail carriers and with other modes, to meet the needs of the public and the national defense; ...
- (5) to foster sound economic conditions in transportation and to ensure effective competition and coordination between rail carriers and other modes; ... and
- (12) to prohibit predatory pricing and practices, to avoid undue concentrations of market power and to prohibit unlawful discrimination...

49 U.S.C. § 10101. The Board's regulations likewise emphasize the importance of competition:

[T]he [Board] does not favor consolidations that substantially reduce the transport alternatives available to shippers unless there are substantial and demonstrable benefits to the transaction that cannot be achieved in a less anticompetitive fashion. Our analysis of the competitive impacts of a consolidation is especially critical in light of the Congressionally mandated commitment to give railroads greater freedom to price without regulatory interference.

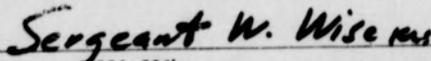
49 C.F.R. Part 1180.1(a.)

Under the law, the priority of the statute governing proposed rail mergers and acquisitions is competition, not consolidation. Applicants thus tout their proposed division of Conrail as one that restores the rail competition which Congress sought in 1973 but was unable to obtain at the time. Yet when faced with LAL's request for a condition eliminating a monopolistic firewall, the Applicants retreat from embracing the public benefits of competition and actually accuse LAL of "relitigating" the Final System Plan. Fortunately, the governing law prevents the Applicants from usurping the Board's authority to correct the transaction-related harms LAL has demonstrated and otherwise satisfy itself that the transaction is in the public interest.

CONCLUSION

WHEREFORE, LAL respectfully requests that the Board condition the Primary Applicants' proposed transaction upon elimination of the Genesee Junction firewall through LAL's acquisition of trackage rights or preferably ownership of Genesee Junction Yard, subject to terms and conditions to be negotiated by the parties or, failing a negotiated agreement, set by the Board.

Respectfully submitted,


Sergeant W. Wise
Livonia, Avon & Lakeville Railroad Corporation
5769 Sweeteners Boulevard
P.O. Box 190-B
Lakeville, NY 14480
(716) 346-2090

Kevin M. Sheys
Christopher E. V. Quinn
Oppenheimer Wolff & Donnelly LLP
1020 Nineteenth Street, N.W.
Suite 400
Washington, DC 20036-6105
(202) 496-4906

Dated: February 23, 1998

CERTIFICATE OF SERVICE

I hereby certify that on this 23rd day of February, 1998, a copy of the foregoing **Brief of Livonia, Avon & Lakeville Railroad Corporation (LAL-7)** 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.



Kevin M. Sheys