

TESTIMONY OF
ROBERT W. BLANCHETTE
ADMINISTRATOR OF THE FEDERAL RAILROAD ADMINISTRATION
BEFORE THE SUBCOMMITTEE ON SURFACE TRANSPORTATION
COMMITTEE ON COMMERCE, SCIENCE AND TRANSPORTATION
UNITED STATES SENATE
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Mr. Chairman and Members of the Subcommittee:

I am pleased to be here this morning to share with you the preliminary views of the Department of Transportation regarding the future of Conrail and rail service in the Northeast. As provided by the Staggers Act, the final results of the detailed studies undertaken by Conrail and the United States Railway Association (USRA) must be presented by the end of this month. The Department is under a similar statutory obligation to make recommendations with respect to the future structure and operations of Conrail not later than April 1. By May 1, 1981, the Department is required to submit its comments and recommendations with respect to the USRA and Conrail reports.

Recognizing that the schedule set out in the Staggers Act may not permit a timely legislative response to the Conrail issue, the Department will make its first report, rather than the May 1 document, its definitive statement. The Department will also use preliminary information available to it to accelerate its evaluation of the USRA and Conrail reports from May 1 to mid-April.

In the past few weeks, dozens of meetings have been held at all levels with representatives of USRA, Conrail, and other interested parties and agencies. Over this last weekend, the USRA Board, including representatives from the Departments of Treasury and Transportation, met and reviewed the USRA staff recommendations. In essence, the Department is prepared to move the Staggers Act schedule up a month so that an action program may be implemented expeditiously.

The three reports you will receive next week will not be identical in their recommendations for continuing rail service in the Northeast. We do believe, however, that each will convey a sense of urgency, will find the status quo totally unacceptable, and will concur in the conclusion that massive changes are needed. The Department looks forward to the opportunity of participating in the process of developing a solution.

One conclusion is presently clear. No further studies are needed. Rather, we must focus on an action program. The chronic problems of rail service in the Northeast have been studied since the Transportation Act of 1920 ordered the ICC to recommend a limited number of railroad systems to handle the Nation's railroad freight traffic. Many times since then, the Nation has struggled with various aspects of

this problem, especially in the Northeast. There was an opportunity to solve the structural problem with an overall plan during the prosperous 1920's. Again there was a chance to solve it in the 1950's when the major Eastern trunk lines were considering mergers. Another opportunity was presented in the early Seventies, when the Penn Central contemplated liquidation of its system. At that time, USRA could have recommended major line transfers as an alternative to Conrail in its Preliminary and Final System Plans, but finally opted for a "Unified" Conrail. That decision has proven to have been in error since we now have the same problem before us.

Without precluding ideas that others may have, there are four major courses of action available to deal with the Conrail problem. First, Conrail could maintain the status quo, with modest reforms, and continue to limp along with an annual Federal infusion of funds. Second, we could attempt to make Conrail approach self-sufficiency through maximum realization of reforms in labor, route abandonments, and pricing changes. Third, most of Conrail's principal lines could be transferred to profitable railroads or other buyers. Finally, through an auction process, much of Conrail's traffic could be assumed by other railroads through modest extensions of their own lines to reach Conrail's shippers. Each of these basic options may have one or more variations.

In developing the future structure for rail service in the Northeast, two basic considerations must be met. Adequate rail services in the Northeast must be continued, but within the private sector.

The status quo is unacceptable by all admissions. The Northeast rail problem has cost the Government over \$7 billion, much of which will never be recaptured. Since 1976, Conrail alone has cost the taxpayers \$6 billion. If all the funds that currently are authorized are appropriated and spent, the total 5-year cost will reach \$6.7 billion and the basic problems will still remain unsolved. While the effort by Conrail's managers and employees to rehabilitate Conrail's physical plant and equipment and improve its service should not be discounted, Conrail is not, and cannot become, financially self-sufficient as presently structured. In fact, Conrail will require more than \$385 million in additional supplemental Federal subsidies during Fiscal Year 1981.

Attempting to make Conrail into a financially self-sufficient corporation, the second option, will require unprecedented cooperation and sacrifices by Conrail's employees, connecting carriers, suppliers, shippers, and state and local governments. On the basis of information available to

date, it is clear that this option is a high risk, high-cost proposition. The analysis USRA presented in its December 1980 report shows that, even if Conrail were to make significant improvements, it would be short between \$1.5 and \$2.1 billion over the next 5 years, exclusive of labor protection. Its final report calls for even greater improvements to achieve viability, but in the Department's view, there is little likelihood that Conrail's traffic and revenue will reverse a 20-year trend or that the revenue/cost picture can be changed to the extent required.

The third option is to transfer Conrail's principal lines to profitable, private sector railroads. The complexity of such an undertaking should not be underestimated, but the Department must consider an option which would ensure that the region's most essential traffic is handled in the private sector by successful railroads.

The fourth option is to auction as much of Conrail's traffic as possible to other railroads, which would acquire only those segments of Conrail needed to connect their systems to Conrail's customers. This solution would be more disruptive to Conrail shippers and employees than an organized transfer. However, it remains available if all other options fail.

The Northeast railroad crisis is as much a railroad industry problem as it is a Government problem. The solvent railroads of

the nation must be a part of the solution. If they are not, Conrail will be forced to take drastic measures to reduce its size and its labor costs. The projections available indicate that, even with a drastic approach, Conrail is not likely to become self-sustaining. This dismal financial outlook and continued Federal involvement will prevent Conrail from ever being able to participate in the dynamic changes occurring in the rail industry, thus forcing Conrail into a regional cocoon for at least the rest of this century.

As the railroad industry evolves into a network of a few large railroads which can offer single-line service to a higher percentage of its customers and can implement the flexibilities and reforms of the Staggers Act, Conrail will be left as an isolated, short-haul regional carrier. Conrail's costs will increase and its traffic base will erode, leaving it little choice but to further pare its system or defer maintenance, until it possibly could no longer provide even those services which are essential to the Northeast.

The inescapable conclusion is that Conrail's services and the properties necessary to provide those services must be assumed by the private sector. Conrail's properties should be acquired by other railroads and must be operated

in the private sector. Most of Conrail's lines have traffic which can be handled profitably by other carriers. Private-sector railroads, both those in the Northeast and the western carriers, should be offered Conrail's properties.

The Department recognizes the impediments to this solution. They are: passenger service in the Northeast Corridor; the Northeast Corridor itself, with its mix of commuter, intercity passenger, and terminal freight switching operations; and labor costs stemming from too many employees and excessive labor protection costs now being paid for by the taxpayer, but soon to be shifted to Conrail. Each of these impediments must be addressed and resolved before any private sector railroad would be willing to acquire major portions of Conrail's properties and services.

The burden of providing passenger and commuter services must be lifted from Conrail or those railroads which assume Conrail's services. The diversion of management resources and the uncertainty of reimbursement by local commuter authorities, which are significant problems for Conrail, are absolute barriers to potential acquisitions by other carriers. The Department presented in testimony last week four options for the provision of commuter service in the Northeast. Each option would have commuter services operated by a

passenger-oriented entity, not by Conrail or any other freight railroad. Assuring that railroads assuming portions of Conrail's service and its lines do not incur a commuter or a passenger liability is an essential prerequisite to securing any railroad's interest in Conrail properties.

The Northeast Corridor itself is an impediment to other railroads acquiring portions of Conrail. The Corridor is predominantly a passenger operation. Freight railroads may be unwilling to accept entrepreneurial responsibility for the present terminal operations in and adjacent to the Corridor. Therefore, there may be problems in selling these operations, principally those between Wilmington, Delaware, and the New York/New Jersey port areas, to the private sector.

In the first instance, the Department can provide incentives for other railroads to buy these terminal operations through provisions of special Federal aid. If this is not sufficient, a separate entity, either a passenger service authority or a separate freight terminal company operating on a cost-recovery basis, could provide terminal freight services for all railroads purchasing Conrail lines if the acquiring railroads are reluctant to take over the terminal

operations. It is essential to recognize that the Federal Government, through its funding of Amtrak and its acquisition of the Northeast Corridor is paying for much of the terminal infrastructure already.

The final impediment to other carriers acquiring portions of Conrail is the large number of Conrail employees and the attendant, high cost of labor protection. The Department will propose legislation to the Congress for the repeal of Title V labor protection in the Northeast because existing labor protection for Conrail employees constitutes a barrier to the implementation of any permanent solution to Northeast rail problems. Any reduction in employment Conrail makes in order to become self-sufficient is negated by the labor protection liability for which Conrail will soon become responsible under the Staggers Act. Savings from the abandonment of unprofitable lines would be quickly offset by current Title V liabilities or similar conditions, if they were to be imposed. Service transfer is not possible under the current level of protective conditions. Other carriers would not assume the large numbers of Conrail employees now utilized in providing service, nor the protection costs associated with reducing the work force. At the same time, the Department does not believe it is appropriate that the total burden of change be shifted to the taxpayer.

The Department is sensitive to the labor dislocations which would result from sales of Conrail's lines to other railroads, and would support a labor protection package which would provide benefits not greater than those provided in the case of Midwest bankrupts. Not all of the essential dialogue on the labor protection issue has yet occurred, and it is essential that rail labor participate in developing the solution.

The ultimate impacts on labor are likely to be less severe in a solution involving sales to the private sector than they would be under a restructured Conrail. In order to achieve viability, Conrail would be forced to make drastic changes in its labor costs and work rules. In contrast, purchasing railroads would implement their own work rules, rules which are the product of the normal collective bargaining process. We will work with Conrail, the other railroads, and labor in resolving these issues.

In summary, the Department believes that there are compelling reasons to integrate the Northeast rail services into those of the rest of the Nation. This can be accomplished only through the sale of Conrail's facilities and services to other railroads. The Department is confident that Northeast

rail services can be provided by the private sector if the impediments related to passenger services in the Northeast Corridor, freight terminal costs in the Corridor, and labor protection costs are removed.

The Department does not favor more Federal funding support for Northeastern railroad service unless it is satisfied that a permanent, private-sector solution is at hand. The Administration will work closely with you, Mr. Chairman, and your Subcommittee to develop a solution that provides a financially-stable, reliable railroad system for Conrail's shippers, employees, and the states and communities it serves.

I should be pleased to answer any questions you might have.

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