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REMARKS PREPARED FOR DELIVERY BY SECRETARY OF TRANSPORTATION BROCK ADAMS,  
TO THE MIDWESTERN RAILROAD RESTRUCTURING HEARING, CHICAGO, ILLINOIS,  
JANUARY 18, 1978.

I am sure we would all prefer to be here under happier circumstances, but the issue at hand - unpleasant though it may be - demands our undivided attention and our concerted action. I appreciate the response to this public hearing. I thank you all for coming. I spoke with Chairman Dan O'Neal about today's meeting and I am pleased that he has sent a representative. He has assured me that the full resources of the commission are available to assist in finding a workable, financially practical solution to the problem that brings us together today.

While the specific event that precipitated this meeting was the bankruptcy of the Chicago, Milwaukee, St. Paul and Pacific railroad, the failure of that line is - as I said in scheduling this hearing - "only the tip of the iceberg." This is the second bankruptcy in the Midwest in the past three years, and there are other carriers in this region that are in poor financial condition. As you know, I am not a newcomer to the problems of the nation's railroads. I spent considerable time during my years in Congress working in support of legislation that would preserve and improve rail service. In fact, as one of the Congressional architects of the 3-R and 4-R Acts, I concurred in language directing the Secretary of Transportation to take certain actions in the public interest which, as Secretary, I am now obligated to fulfill.

The truth is, we face a potentially disastrous rail situation in the Midwest, and the dimensions of that problem - and the costs of coping with it - will only be aggravated by delay or vacillation. It is therefore essential that we work toward a solution as swiftly as possible.

I hope that in weighing the options before us we will put aside as undesirable any considerations of large-scale reorganization legislation. We do not want, nor do I believe we need, a "Conrail West." There are, in my judgement, adequate legal provisions and ample restructuring opportunities to support a private sector solution to rail problems here in the Midwest.

For my part in this hearing let me outline, first, the differences between the rail situation here and in the Northeast; second, indicate why I believe a cooperative restructuring process is preferable to the kind of government rail reorganization instituted in the Northeast; and, third, suggest how we might proceed toward such a solution.

We are fortunate in that Section 401 of the 4-R Act\* permits rail and transportation department officials to get together, with all interested parties, to search out solutions to the problems of ailing rail lines. It is that authority, which I also view as a responsibility, that is the genesis of this hearing. I believe that everyone concerned - shippers, consumer representatives, labor and management, and Federal, state and local officials - must share in seeking a resolution to the problem before us. We may not find a solution totally satisfactory to each participant, but we must find one essentially acceptable to all. I ask for the cooperation and good faith of everyone as we work together to design answers to the railroad problem here in America's heartland.

There are several reasons why the formula for rescuing the freight railroads in the Northeast - as applied in the Rail Reorganization and Recovery (3-R) Act - should not be adopted in the Midwest.

For one, the economies of the two regions are different. The Northeast is industrial; the Midwest agricultural. Generally speaking, the economic decline was sharper in the Northeast relative to the rest of the country.

The railroad structures themselves also are different. The Penn Central was far more dominant in the Northeast than any single carrier is in the Midwest. Seven other carriers in the Northeast also were in bankruptcy. Moreover, in the congested Northeast a manufacturer is often dependent on a single rail line, with no or few other shippers using that same line. In the Midwest, on the other hand, shippers may have the choice of several lines, the result of "spider web" rail construction in the last century which spun track in all directions throughout the plains. Iowa and Kansas each have more than 7,500 miles of track, compared to 5,200 in New York state and only some 7,000 miles of track in all of California.

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The 1976 Railroad Revitalization and Regulatory Reform Act.



There is also the matter of rail passenger service, the need for which is much more acute throughout the densely populated Northeast than it is in the Midwest - Chicago itself, of course, being an exception to that distinction.

For these reasons, then, the Northeast carriers were in the most difficult position of all. Their reorganization required a major governmental planning process, during which funding of \$660 million in trustee certificates, grants and rehabilitation loans were required to keep them alive. In order to provide an income-based reorganization and to capitalize the new company - Conrail - we have, thus far, authorized \$2.1 billion in preferred stock and income debentures.

Still, while there have been too many rail facilities in the Northeast, the basic problem was not one of "too many carriers" or "redundant facilities" or "excess plant" to the extent that those factors have affected the railroads in the Midwest. The region has been overbuilt for years, and despite several mergers and a succession of consolidation plans there are still five carriers operating between Chicago and Omaha and eight between Chicago and Kansas City.

But in the years that I have spent on rail matters, I have continually been amazed by the staying power of the railroads. Despite high fixed costs, substandard earnings and aging facilities, railroads continue to provide service. Railroads are also highly competitive among themselves. While competition is normally a healthy thing, in an overbuilt region like the Midwest it means that there is too much service, at rates too low to support the equipment and facility investments that would improve efficiency.

Still, because the problem is primarily one of excess facilities and because none of the marginal or bankrupt carriers in the Midwest is dominant as was Penn Central in the Northeast, I do not believe a Conrail-type solution is either necessary or advisable for the Midwest. There are two reasons for favoring an alternative course of action.

First, much of the "excess plant" can be stripped away without terminating service to important shipping points. This can be done in several ways. "Market swaps," for example, can shorten distances and eliminate the need for some secondary tracks or even certain mainlines. "Joint use" arrangements can consolidate overhead services on fewer facilities, with old mainlines perhaps reverting to local service or being abandoned. Branch line abandonments can be speeded up, especially where alternative service is available. Purchase of some lines by stronger carriers is another important option.

I've avoided talking about mergers as a means of reducing "excess plant," because I've come to believe that merger per se is far less promising as an effective way to improve the economics of railroading than these other elements I just mentioned. Merger happens at the corporate level. "Market swaps," "joint use," and abandonments are the elements that actually reduce plant, whether as part of a merger or as steps short of merger. They are what count. This



is why we emphasize the "restructuring" of rail service rather than mergers. It is a critical distinction, one that I will be making repeatedly. I could say few things of more importance today than to consider why this is so.

Let me be clear that I am not against mergers, but I believe any proposed merger must pass two acid tests: will the consolidation help in the restructuring of the industry, to improve profitability; and will it be in the public interest, in terms of service.

Here in the Midwest I believe circumstances favor restructuring. It is in the interests of all carriers to reduce costs for the same total revenue, and I know most, if not all, are willing to pursue these opportunities. The Rock Island, as you know, has already proposed a plan calling for the consolidation and coordination of its freight services with those of four other Midwest railroads. Under this plan, the consortium of privately-owned railroads would jointly share terminals, rail yards, equipment and revenues. I would reserve judgement on this specific plan, however, until the costs and prospective benefits can be fully assessed.

The broader point is that many solvent carriers exist in the Midwest to provide service throughout the region. There is no need to set up a new government-aided firm to ensure continuation of service to important markets. Railroads in the region will have to make many adjustments. New investments will be needed to improve the efficiency of restructured operations. There may need to be some changes in the division of revenues among carriers. These are difficult adjustments, but they are not impossible.

The second reason I oppose any government sponsored reorganization process in the Midwest is related to the first. I firmly believe the industry should be given a chance to restructure itself before the government takes over the job. What would the government do with two bankrupt railroads? Merge and refinance them? Such an approach would make it more difficult to benefit from the cooperation (and resources) of the solvent carriers. There would be less trimming of unnecessary plant. And in a fundamental way, government assistance is unfair to the self-sufficient competing carrier.

I propose, therefore, that we pursue the provisions of Section 401 of the 4-R Act to the fullest. The law allows government to assist in the restructuring, without getting financially involved - it suspends the anti-trust restrictions against carrier discussions.

We are prepared to assist in any and everyway possible and at all levels. At Jack Sullivan's suggestion, I've asked Robert Gallamore, the Deputy Federal Railroad Administrator, to take on this assignment. Bob has a lot of familiarity with this subject. He has my full confidence and I am sure he will win the confidence of everyone he deals with during the coming months.

Funding through Title V is a part of the way we can help. We have always sought the coordination of facilities as an objective implicit in the Title V program and we will accelerate our efforts in that regard. I expect to see the funds directed at projects emerging from the 401 process where needed, and indeed I expect most of the difficult security issues FRA has had to handle to be eased by that process. Title V funds are only a portion of the answer to the Midwest rail problem, but where their use is indicated you have my assurance that they will flow in a fair and timely manner.

The ICC will be involved in the process, as the Commission must approve property transfers, trackage agreements or abandonments. I will be willing to argue for such changes before the ICC if DOT can achieve agreement with the parties involved in the 401 process.

I am also willing to seek facilitating legislative change where that is needed. We are already doing that with Title VIII, the branchline subsidy program. Our legislative proposals in that area will be ready in a few weeks. Minor changes may be needed in Title V. But I hope we can avoid large scale railroad reorganization legislation at this time. We should make what we have work first. I am committed to that.

Now, as you know, the major initiative under the 401 process, by statute and as a matter of policy, lies with the carriers. They must make the proposals and they are the ones who can make new arrangements work. Planning and implementation must go hand in hand. The very first step, a letter of request to initiate the 401 process, must come voluntarily from a carrier. Indeed, I would welcome a letter of initiation from each carrier interested in participating in the Midwest restructuring process.

This is the last, but it may also be the best opportunity that has come along for a private sector solution of the Midwest railroad problem. To walk away from it now would be to mark the beginning of the end. None of us - carriers, labor, shippers, communities, or government - can afford that. Perhaps it is not a pleasure trip that has brought us to this forum. We meet out of necessity; but also as prudent and responsible people, joined in a common concern for the preservation and improvement of rail service. Let us reason well together. Let us act willingly, wisely, and expeditiously.

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