



*"The roads you travel so briskly
lead out of dim antiquity,
and you study the past chiefly because
of its bearing on the living present
and its promise for the future."*

—LIEUTENANT GENERAL JAMES G. HARBORD,
K.C.M.G., D.S.M., LL.D., U.S. ARMY (RET.)
(1866-1947)

*Late American Member of Council at London
The Newcomen Society
for the study of the history of
Engineering and Technology*



Rise from the Wreckage

A Brief History of Conrail

L. STANLEY CRANE





“Were American Newcomen to do naught else, our work is well done if we succeed in sharing with America a strengthened inspiration to continue the struggle towards a nobler Civilization—through wider knowledge and understanding of the hopes, ambitions, and deeds of leaders in the past who have upheld Civilization’s material progress. As we look backward, let us look forward.”

—CHARLES PENROSE

(1886-1958)

Senior Vice-President for North America

The Newcomen Society

for the study of the history of
Engineering and Technology

(1923-1957)

Chairman for North America

(1958)



This statement, crystallizing a broad purpose of the Society, was first read at the Newcomen Meeting at New York World’s Fair on August 5, 1939, when American Newcomen were guests of The British Government.

“Actorum Memores simul affectamus Agenda”

This address, dealing with the history of Consolidated Rail Corporation, was delivered at a "1988 Pennsylvania Meeting" of The Newcomen Society of the United States, held in Philadelphia, when L. Stanley Crane was the guest of honor and speaker on May 4th, 1988.



“In the dozen years of our existence, we lived out 100 years of railroad history—moving from the restrictive regulation and capital-starvation of the past into the market-driven, innovative and successful company of today and tomorrow.”

—L. STANLEY CRANE



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L. STANLEY CRANE

MEMBER OF THE NEWCOMEN SOCIETY
CHAIRMAN AND CHIEF EXECUTIVE OFFICER
CONSOLIDATED RAIL CORPORATION
PHILADELPHIA, PENNSYLVANIA



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INTRODUCTION OF MR. CRANE IN PHILADELPHIA,
ON MAY 4TH, 1988, BY THE HONORABLE JAMES J.
FLORIO, MEMBER OF THE UNITED STATES HOUSE
OF REPRESENTATIVES FROM NEW JERSEY, AND
CHAIRMAN, HOUSE SUBCOMMITTEE ON COMMERCE,
CONSUMER PROTECTION AND COMPETITIVENESS

Members of Newcomen and guests:

GOOD evening. It is my pleasure and honor to introduce L. Stanley Crane tonight.

Let us take a few minutes to reflect on Stan Crane's remarkable accomplishment in helping to turn Conrail around.

Twelve years ago, it would have been almost impossible to imagine Conrail becoming the success it is. Conrail was formed in 1976 out of the remnants of several bankrupt railroads, most notably the Penn Central. In its early days, Conrail was anything but a success. In many cases Conrail even lost track of its own rail cars.

Between 1976 and 1981, the federal government invested about \$3.2 billion directly in Conrail. But, at the beginning of the '80s, Conrail had shown little improvement. True, its track and equipment were in better shape thanks to the federal investment, but Conrail was still a chronic money loser.

Indeed, by early 1981, things were so bleak that, when the Reagan Administration took office, it argued there was no hope for Conrail. The Administration proposed that Conrail should be broken up and its assets sold piecemeal. However, many of us in both parties in the House saw cause for hope. In 1980, Congress had passed the Staggers Rail Act, which removed much of the outmoded regulatory regime that had hampered the nation's rail industry. The freedoms provided by the Staggers Act would allow Conrail to finally compete and survive in the transportation marketplace. Also, in early 1981, new leadership took over at Conrail. L. Stanley Crane, an experienced railroader who successfully ran the highly efficient Southern Railway, became Conrail's new chief executive officer.

As a result of these hopeful developments, and, I might add, the persistent persuasion of Stan Crane working in tandem with other

Conrail stakeholders, such as its employees and shippers, Congress developed an alternative to the Administration's approach. This alternative became the Northeast Rail Service Act (NERSA), which took as its premise that Conrail could become profitable and could be eventually returned to the private sector as an entity. NERSA required that all of Conrail's stakeholders would have to sacrifice to achieve this goal, but the sacrifices were far less than what would have occurred had Conrail been broken up. NERSA was enacted in August of 1981.

The score was now Stan Crane, one, Department of Transportation, zero. Strike one for the DOT.

Well, Stan Crane told us in 1981 that if we gave him the tools to turn Conrail around, he would do it. Those of us in Congress are used to hearing agency heads promise that with just a little more money, and a little more time, things would be different. Usually, these are just empty promises. But with Stan Crane, his promises turned to concrete results. Thanks to regulatory reform, NERSA, the sacrifice and cooperation of labor, and the management ability of Stan Crane, Conrail became profitable.

That Stan Crane was a man of results and not just promises stood him in good stead as 1985 rolled around. At that time, the Administration was seeking to return Conrail to the private sector. Stan Crane suggested that a public offering was the best way to proceed. But his views were rejected by the Department of Transportation, which, in February of 1985, recommended that Conrail be sold to Norfolk Southern. The Administration argued that Conrail could not survive as a stand-alone entity and that a merger with a major competing railroad was necessary. Of course, those of us in Congress remembered similar doom and gloom stories from the Administration back in 1981, when we were told Conrail could never be profitable.

Stan Crane, in 1985 and 1986 as in 1981, fought back. He argued that Conrail could survive as a stand-alone railroad and that a sale to Norfolk Southern was both anti-competitive and unnecessary. It seemed that he and Secretary Elizabeth Dole just could not agree on how to remove Conrail from the "Dole."

While Secretary Dole was a very persuasive advocate, Stan Crane had a track record running railroads and credibility with Congress.



L. STANLEY CRANE
CHAIRMAN AND CHIEF EXECUTIVE OFFICER
CONSOLIDATED RAIL CORPORATION

It became clear the Administration proposal could never pass the House. After a year and a half legislative battle, Norfolk Southern withdrew. Finally, in the fall of 1986, Congress enacted legislation providing for a public offering of Conrail's stock.

The score was now Stan Crane, two, Department of Transportation, still zero. Strike two for the DOT.

And, on March 26, 1987 the federal government's stock in Conrail was sold, in the largest initial public stock offering in American history. Stan Crane had successfully presided over the turnaround and privatization of Conrail.

As they say, three strikes and you're out. I'm looking forward to hearing Stan Crane's upcoming revelation of his secret plan to strike out the DOT. Anyway, it's my pleasure to introduce L. STANLEY CRANE.



Fellow members of Newcomen and guests:

THANK you and good evening. It is a great honor to be here.

Nearly three centuries ago, Thomas Newcomen, in whose honor the Newcomen Society is named, invented the first commercially successful steam engine—laying the track, as it were, for the birth of the railroad industry.

The railroads built America. For most of the nineteenth century, they joined the coal mines, iron fields, forests and prairies of the South and West to the factories and markets of the East, making possible economic integration on a truly national scale. By the turn of the century, railroads were America's growth industry—the biggest, the wealthiest and the most sophisticated business enterprises in human economic history. The men who built the great railroads—Cornelius Vanderbilt, J. P. Morgan, James J. Hill, Frank Thompson and Edward H. Harriman—had the power to shape our national destiny.

In the eyes of many, including at least one president of the United States, that power was excessive. And so, eighty-three years ago, on January 30, 1905, in this very building—perhaps in this very room—President Theodore Roosevelt, fresh from his 1904 electoral victory, urged the members of Philadelphia's Union League Club to support his initiative to put railroad rates under the regulatory umbrella of the Interstate Commerce Commission (ICC).

That he succeeded is a matter of historical record. For the next seventy-five years, a rising tide of government regulation eventually crippled America's railroads, robbing them of capital, draining them of their competitiveness with other modes of transportation, and directing the attention of America's innovators and capitalists toward the less fettered possibilities of a newly emerging transportation technology—the internal combustion engine, the pneumatic tire, the paved road.

I stand here tonight, in the footprints of Theodore Roosevelt, so to speak, to bear witness to the historical error of regulation as it was administered for the better part of a century with increasing disregard of economic reality. For I, a railroad man all my life, have had the rare privilege of presiding over the rebirth of some of the oldest of America's great railroads into Conrail—the youngest of America's

great railroads. That rebirth could not have come without the dismantling of a significant part of the regulatory system that Roosevelt believed would benefit the people of the United States—the regulatory system that ultimately would hold the entire railroad industry in chains.

Today, Conrail is at a turning point. We have proven our ability to survive and prosper in a free transportation marketplace. We have passed from government wardship to private sector ownership. This year marks the end of my tenure at Conrail. Now it is up to the next generation of railroad people to guide Conrail into the twenty-first century.

Turning points are traditionally times for looking back. I have much to look back on, and much to be thankful for. After forty-three years in the railroad business—all but two at the Southern Railway, where I became chief executive officer—I was not ready for retirement in 1980.

So when the opportunity to manage Conrail came along, I grabbed it. My eight years at the throttle turned out to be the most difficult—and among the most rewarding—of my life. Conrail tested me in a way I was never tested before: I had to use every bit of the knowledge and experience I'd gained during my first career—and then some—to help Conrail's people to make it the profitable and vital railroad it has become. It also gave me the chance to keep on working hard at something I love. That I was also able to make a contribution to our employees, our customers, our region and our country makes the memories I will take with me all that much sweeter.

If luck is a matter of being in the right place at the right time, then I was lucky in many respects. On January 1, 1981, the day I officially came to work, I stepped into an organization and a situation poised at the threshold of change. Conrail could not have succeeded as well as it did beginning in 1981 without the enormous efforts of the people who managed the railroad, fought for it, and stayed up nights worrying about it before 1981. Nor could we have succeeded since then without the creativity, commitment and hard work of many, many people—both inside and outside of Conrail.

And so this turning point in Conrail's history is also a fitting time to say "Thank you" to many of the people without whose efforts

Conrail would not be here today. I would like to do that by telling the Conrail story from a different vantage point than most of you know—as we inside the company really lived it.

The Forces of History

The creation of the Consolidated Rail Corporation in 1976 by an act of Congress was the outcome of a set of historical conditions that began early in this century and culminated in the total financial collapse of the Northeast-Midwest rail systems by the early 1970s.

The problems were not new. A president of the United States said it well, when he concluded that, "The major factor in the present distressed condition of the railroads is the low volume of their traffic. A contributing factor is the depressed character of many of their rates. Competitive modes of transportation are partially responsible for the former and almost wholly responsible for the latter. To the extent that the inroads made upon railroad traffic and revenues by other modes of transportation are not due to natural advantages which the latter possess, but are attributable to artificial advantages accruing to their competition as a result of governmental favoritism in any respect, the railroads have a right to object. Such favoritism now exists in pronounced degree in the important matters of regulation, taxation and subsidies."

The president who said that was Franklin Roosevelt, and he made that observation in 1938! As I said, our industry's problems were not created in the 1970s.

Since the passage of the Hepburn Act in 1906, an ever-tightening web of state and federal controls on pricing severely limited the railroads' ability to recover costs. Further, the ICC mandated the methods railroads used to divide the joint revenue they received for multi-line freight movements. These divisions were especially unfair to the northeastern railroads, whose handling and terminal costs were far higher than those of the southern and western railroads.

Labor also contributed to the financial pressure on the railroads. The creation of the national rail brotherhoods in 1910 gave labor a degree of clout it never had before. With that clout, it was able to win substantial wage gains. To be sure, rail management could always accept a strike. But the cost of a rail strike was invariably perceived



HISTORIC HORSESHOE CURVE, LOCATED IN CENTRAL PENNSYLVANIA ON CONRAIL'S HEAVILY TRAVELED PITTSBURGH LINE, IS A MONUMENT TO THE ENGINEERING SKILL THAT ENABLED THE RAILROAD TO CONQUER THE ALLEGHENY MOUNTAINS AND PUSH ITS WAY WESTWARD OVER 100 YEARS AGO

as too high, and management often preferred to settle quickly, if generously, rather than jeopardize revenues or risk federal intervention. This certainly was the case on the Pennsylvania Railroad, which in 1964 signed an agreement guaranteeing lifetime employment in return for labor's support of merger with the New York Central. By the mid-1970s, railroad labor costs in the Northeast approached 60 percent of revenues, versus less than 50 percent for the southern and western lines.

This pattern of rising costs and severe price regulation cut deeply into the railroads' ability to properly maintain, let alone upgrade, their plant and equipment. Without adequate capital investment, the quality of service deteriorated—leading to the erosion of the traffic base, which drained away revenues. Nor could the railroads effectively reduce the size of their systems: onerous ICC rules on abandonment put the burden of proof on the railroads and denied relief

during the years of litigation that invariably followed an application to abandon.

Wholesale government subsidies for competing modes of transportation after World War II accelerated the railroads' decline and intensified the cost pressure. The substantial completion of the federally funded interstate highway system in 1966 created significant competitive advantages for motor carriers. Railroads, remember, are the only mode of freight transportation that has to pay the entire cost of building, maintaining and replacing its right-of-way.

Despite increased tonnage, railroads' share of total U.S. freight volume fell from 56 percent to under 40 percent between 1950 and 1970. Meanwhile, motor freight volume more than doubled. Barge lines reaped similar benefits from federally aided inland waterway and harbor improvement programs. The use of public funds to subsidize airport construction, along with federal ownership and operation of the air traffic control system siphoned intercity rail passenger traffic—never very profitable, even in the best of times—onto the growing domestic airline network. The rise of the automotive society substantially reduced rail commuter traffic. Nonetheless, railroads were prohibited from shutting down their unprofitable passenger operations by local, state and federal lawmakers whose primary concerns were political, rather than economic.

The 1968 merger of two of America's largest and oldest railroads into the Penn Central—and its collapse almost two and a half years later in the largest corporate bankruptcy in American history up to that time—were spectacular events, but hardly unique. Throughout the late 1950s and early 1960s, the railroad industry underwent a wave of restructuring aimed at reversing its fortunes. The railroad bankruptcies a decade later attest to the prior restructuring's failure. In quick succession, the northeastern and midwestern railroads fell like dominoes—the Central of New Jersey in 1967, the Penn Central and Lehigh Valley in 1970, the Reading in 1971, and the Lehigh & Hudson River and Erie Lackawanna in 1972.

Faced with its imminent collapse, Washington acknowledged the economic and strategic importance of the rail infrastructure. To preserve rail service in the Northeast, Congress passed the Emergency Rail Services Act, which provided for direct federal assistance to the

bankrupt railroads—nearly \$1 million a day—until a longer-term solution could be found.

As early as 1972, the court-appointed Penn Central trustees concluded that the railroad could not climb out of bankruptcy; under the circumstances, the only solution was liquidation. The regulatory price structure made it impossible to recover costs. The railroad was much too large for the traffic it carried. Labor costs were excessive and showed little chance for decrease. Passenger and commuter operations generated substantial losses, despite the beginning of Amtrak operations in 1971.

The trustees of the other bankrupt railroads shared the Penn Central's conclusions. Although the bankruptcy court agreed that the trustees' proposal qualified as a plan of reorganization, the ICC did not.

However it was to be accomplished, there was no question that the health of the Northeast-Midwest industrial heartland depended on preserving a basic rail system—pruned though it might be. For despite the postwar industrial migration to the Sunbelt, a substantial portion of America's coal, steel and automobiles still, in 1972, came out of the Eastern District. It was estimated, in fact, that shutdown of the Penn Central alone would affect roughly half of all U.S. manufacturing plants and hundreds of thousands of jobs, depressing the GNP by 2.7 percent within two months after cessation of service.

The Birth of a Railroad

The idea of a massive federal seizure and reorganization of the bankrupts into a private-sector, for-profit entity was largely the brainchild of Frank Barnett, chairman of the Union Pacific. This strategy was less a matter of altruism than of hardheaded business sense: the UP, like the other southern and western railroads, needed an intact eastern rail system in order to maintain access to the most concentrated and affluent market region in America—and preserve its revenue from rate divisions on joint freight movements. For the railroad industry, and for the government, the alternatives—liquidation and nationalization—simply raised too many hard questions.

On January 2, 1974, President Richard Nixon signed into law the Regional Rail Reorganization (3R) Act of 1973, calling it "a turning point in history." The 3R Act created the United States Railway Association (USRA) and mandated it to prepare a detailed plan for a

new regional rail system—later named Conrail—to be assembled from the six bankrupt lines. Once Conrail was up and running, USRA would monitor its progress and control the purse strings on the \$2.1 billion in federal funds the act provided for rebuilding and modernizing Conrail's right-of-way, track, equipment and structures.

The 3R Act also provided that Conrail would operate rail service under contract to local and regional commuter transportation authorities, which were obligated to reimburse the railroad for out-of-pocket expenses. Finally, Title V of the act extended the labor protection of the 1964 Pennsylvania Railroad/New York Central agreement to all Conrail employees who lost their jobs in the rail consolidation.

For the next two years, USRA, under the leadership of Arthur Lewis and Edward G. Jordan, devoted its efforts to developing a plan for Conrail that would draw up timetables, establish priorities, and determine staffing requirements. After many changes, Congress approved the Final System Plan on November 9, 1975; on February 5, 1976, President Gerald Ford signed into law the Rail Revitalization and Regulatory Reform (4R) Act—technically an amendment to the 3R Act—that formally created Conrail and implemented the Final System Plan. Edward G. Jordan was named chairman and chief executive officer. Formal conveyance of the bankrupt properties to Conrail took place on April 1, 1976.

It is here that I would like to say my first “Thank you”—to Ed Jordan, who brought order out of chaos, who provided the leadership in the massive rebuilding program for Conrail, and who, more than anyone else, reversed the course of history and set the wheels of deregulation into motion.

To describe the task facing Ed Jordan as Herculean is to understate it by at least half. On April 1, 1976 Conrail had 34,000 miles of track, 96,000 employees, 4,600 locomotives and 152,000 freight cars. It ran an average of 1,500 freight trains a day, and transported 360,000 commuters daily in metropolitan New York-New Jersey, Philadelphia, Baltimore, Washington, Providence and Chicago. This was bigger than the Penn Central, bigger than Amtrak; Conrail was the biggest railroad in the country—with the biggest problems imaginable.

The day Conrail came into existence, it was a single company in name only. In fact, it was six companies. Penn Central, one of the

six, which was made up of the Pennsylvania and New York Central railroads, primarily, had its separate loyalties and traditions, as well. Each had its own traditions, its own programs, its own marketing organizations, its own yards and maintenance facilities, its own computers, and its own accounting systems. Ed Jordan and his people—most of the latter survivors of the rail bankruptcies—were able to integrate these six or seven distinct corporate cultures into a single integrated organization with one computer system, one marketing department, one operating department, and one finance department. That was no mean feat—certainly, it was something that the management of the Penn Central had never managed to accomplish.

In spite of Ed Jordan's tremendous efforts, however, USRA's Final System Plan for Conrail made two serious and major miscalculations. The first was the belief that restoring the railroad's efficiency would recapture the traffic it had lost over the previous twenty years. Certainly, Jordan was in good company. A great many people—mostly lawmakers and consultants—shared that belief; it was an article of faith, so to speak.

But circumstances worked against Conrail. For one thing, nobody counted on the accelerating pace at which manufacturing businesses left the Northeast for the lower-cost Sunbelt; I still remember *Time* and *Newsweek* covers proclaiming "the death of the Rustbelt." Further, Conrail could not provide adequate service to the businesses that stayed on. Two very severe winters in 1977 and 1978 and the constant presence of work crews trying to fix up the track further weakened the quality of service, which was low to begin with.

The second miscalculation was the plan's overly optimistic assessment of Conrail's operating condition. In fact, after the smoke cleared and management had a chance to look at the railroad in the middle of 1976 and afterwards, they saw a very serious situation—almost a quarter of the track under slow orders; acute shortages of locomotives and freight cars in working condition; and severe congestion at yards and terminals. As a result, scheduled on-time service, in many instances, was poor at best.

By 1978, Conrail had spent almost all of the \$2.1 billion authorized for its rehabilitation, plus another \$490 million in private sector financing. Yet, revenues continued to deteriorate and traffic continued to decline; the long-awaited "hockey stick" in the trend lines failed to

materialize. Little progress had been made in lowering labor costs, which, in 1978, still ate up more than 60 percent of revenues. After three years, Conrail's cumulative loss totaled more than \$1 billion—hardly the turnaround envisioned in the Final System Plan. In fact, a computer analysis showed that fully one-quarter of Conrail's lines of business failed to recover variable costs.

The Fight for Deregulation

At that point, it became clear that simply throwing money at the Northeast-Midwest rail problem was not going to make it go away. If Conrail was to survive, Congress would have to turn its attention to the fundamental regulatory and structural problems that had driven the northeastern railroads to bankruptcy in the first place—and which were threatening to do the same to Conrail:

- Rate regulation that limited revenues;
- Rate divisions that discriminated unfairly against the northeastern railroads;
- The inability to abandon unprofitable and underutilized branch lines;
- Federally mandated labor protection that required Conrail to pay furloughed employees their full salaries to age sixty-five; and
- Commuter operations that cost Conrail upwards of \$70 million a year—despite the “make-whole” provisions of the 3R Act.

Ed Jordan and some of his key people realized that there was nothing left to lose; unless fundamental changes were made in the regulatory structure, there was little hope of fulfilling Conrail's mandate to become profitable—ever. And so, from 1978 on, the railroad openly challenged the system. Conrail began to change switching rates to reflect actual costs, attempted to impose surcharges on unprofitable business, and did other things Jordan and his people knew would be struck down, but which would keep public attention on the rail issue and keep pressure on the ICC for change.

Through such actions, Conrail generally succeeded in raising the visibility of the need for rail deregulation. At the time, Alfred Kahn's campaign to deregulate the airlines was attracting a lot of media attention, which certainly helped: Conrail attracted the attention of ship-



DOUBLE STACK INTERMODAL TRAINS, ONE OF THE FASTEST-GROWING SEGMENTS OF CONRAIL'S BUSINESS, BRING CONSUMER GOODS FROM THE FAR EAST TO DESTINATIONS IN THE MIDWEST, METROPOLITAN NEW YORK AND NEW ENGLAND. IN COOPERATION WITH WESTERN RAILROADS, CONRAIL MOVES THESE TIME-SENSITIVE SHIPMENTS FROM WEST COAST PORTS TO CONSUMER CENTERS IN ITS TERRITORY, SAVING TWO WEEKS OVER THE ALL-WATER PANAMA CANAL ROUTE. DOUBLE STACK SERVICE BEGAN IN 1984

pers, and created a great deal of concern among the other railroads, which were satisfied with the current arrangement and opposed any attempt to deregulate rates or divisions. They, after all, gained from the rate divisions that discriminated against the eastern carriers, and were willing to receive compensation for shoveling snow in Atlanta at the same rates as the eastern lines received it for shoveling snow in Buffalo. Interestingly, the job of speaking out against deregulation on behalf of the rail industry in 1978 and 1979 fell to the Southern Railway and its chief executive officer—whose name was L. Stanley Crane.

Around that time, however, Ed Jordan had embarked on an aggressive campaign to publicize the computer study that showed how much money Conrail was losing because of the joint rates problem. On several occasions in 1980, he met with me in Washington, trying to convince me to stop opposing Conrail's efforts to change the law;

for without the Southern's help, there was no way Conrail and its allies would get that bill through Congress.

Around that same time, the Southern Railway had developed its own computer analyses of rail freight movements, which clearly showed the magnitude of Conrail's cost disadvantage. I began to recognize the unfairness of the situation—and also that one of these days, fairness was going to change that situation around. The eastern railroads did have higher costs and were not getting enough from the divisions to recover their costs. And so we ended our opposition to Conrail's efforts to deregulate rail rates.

On October 14, 1980, President Jimmy Carter signed the Staggers Rail Act, which gave railroads the freedom to adjust prices in response to market conditions and tailor rates to the specific conditions of various industries and types of freight. More important, Staggers was the wedge that opened the door to substantial deregulation of the eastern railroads less than a year later—under the Northeast Rail Service Act of 1981.

Why did Congress reverse seventy-five years of precedent and deregulate the rail industry? In part, I believe it was because deregulation was in the air at that time. But there were more concrete reasons as well: by mid-1980, Conrail had already gone through about \$3 billion in authorized federal assistance, with no end in sight. Instead of turning the railroad around, Conrail had come back to Congress in 1978, asking for another \$1.2 billion over and above the original \$2.1 billion. Yet, traffic continued to decline; the trend lines still did not look anything like hockey sticks. And Conrail lost another half a billion dollars, bringing its cumulative five-year loss to more than \$1.5 billion.

If I were a congressman at that time, I don't think I would have been very happy with the situation. If northeastern rail service was to be preserved, and if Conrail was to survive as an entity, one of two things would have to happen: either more federal assistance would have to be forthcoming, or government would have to devise some way of helping the railroad raise its revenues and lower its expenses. Of these two options, helping Conrail help itself was clearly the more desirable—for the taxpayers and all the other players, as well.

The Staggers Act did two important things for Conrail—and for the railroad industry generally. The first was to provide a mechanism

by which railroads could do away with joint rates more easily and with them the unfair rate divisions that meant unavoidable losses on certain freight movements. The second was a provision that shifted the burden of proof in rate cases away from the railroads and onto the shippers.

As for joint rates, the act said that railroads could put different prices on different routes and negotiate individual prices with shippers. In addition, Staggers also said that a railroad could impose surcharges on its deficit traffic.

These were important steps. For seventy-five years, the law had assumed that the railroads had a transportation monopoly. When a railroad tried to change its rates, the litigation could go on and on, and typically did. In the meantime, the original rate still applied in many cases, no matter how adverse its effects on the railroad. By the time the case was decided, and the new rate was approved, the business had gone anyway—either to the competition or because the time and opportunity had passed. Staggers gave railroads the right to put new rates into effect right away, in most cases. It recognized that railroads now competed with trucks, barges and pipelines, and needed the freedom to price their product competitively.

Staggers also did a third thing. It called upon Conrail, USRA and the Department of Transportation to recommend the further steps Congress needed to take in order to make Conrail viable without additional federal assistance. This recommendation, which most people refer to as Final System Plan 2, was due on April 1, 1981—Conrail's fifth birthday. I'll say more about that in a few moments; first, let me describe the state of the railroad at the end of 1980.

The Changing of the Guard

By the time Staggers passed, Conrail had come a long way—despite the traffic declines and the disappointing financial performance. Ed Jordan and his people shaped the organization, and got it up and running. During his five years at the head of Conrail, Ed was able to assemble the people who had the intellectual and emotional horsepower it took to get this railroad moving.

Bob Platt, his chief financial officer—formerly Magnavox's chief executive before Magnavox got caught in an unfriendly takeover—did a superb job of putting the company's finances in order. He was

even able to raise almost half a billion dollars in private sector capital at a time when most lenders just laughed at the idea of financing Conrail. Throughout those first years, Bob, now retired, was a real bulwark. As head of Magnavox, he'd been through all the struggles and made all the decisions. He was a source of strength and wise counsel in many things; having him at Conrail was like having a second CEO. And for that I thank him.

Ed Jordan's vice president of operations was Richard B. Hasselman—now Conrail's senior vice president of Operations. There is no better operating man in the country than Dick, who learned his trade at the New York Central under Alfred Perlman. Dick was the man responsible for rebuilding Conrail's badly deteriorated physical plant. Spending \$3 billion isn't easy under any circumstances. Spending it well is especially difficult; and Dick spent it well. Under his guidance, Conrail went from laying no rail and half a million crossties a year to laying 1,000 miles of rail and 4 million crossties. In five years, Dick and his people turned Conrail from a railroad on its way to rust and ruin into one of the most modern railroads in America—an effort he is continuing to this day.

Robert E. Swert—now Conrail's vice president for Labor Relations—had worked hard to build a strong working relationship with labor. Bob had come up through the brotherhoods, so he understands labor's point of view and knows how to talk the language better than anyone else I know; his credibility with Conrail's unions was—and is—superb. One of the provisions of the 3R Act, which created Conrail, was to reduce the railroad's 278 separate labor agreements into thirty-four single agreements. By 1980, Bob and his people laid the groundwork that cut 247 of them down to twenty, which covered more than 80 percent of our work force; and by the following year, they had reduced all 278 agreements to a total of twenty-three, covering the entire work force. More important, in 1978 Bob got the brotherhoods to agree to a reduction in train crew size that was a landmark for the railroad industry.

It was that way all the way down the line, from our vice presidents all the way down to our general managers and superintendents. I am very proud of the fact that I didn't bring anyone with me from the Southern Railway—not even a secretary. Virtually all of the right people were already in place when I got here, and they were the ones Ed Jordan put there.

Ed also fought the good fight and got Staggers passed—at what I imagine was enormous personal cost. It's not easy to go back to Congress month after month for five years and tell them things didn't work out the way the planners had promised they would—especially when Ed was one of the chief planners.

I don't know the specific reasons behind Ed's decision to tender his resignation, but if I were in his position, I'd have been very tired after those five years—very tired, and very discouraged. Ed had put the railroad in excellent shape—with modern plant and equipment, a strong management team, a well-running, integrated organization. Staggers was a victory of major proportions. I believe that Ed built Conrail to the limits of his strength and considerable organizational ability. With the presidential election coming up and a new Congress, 1980-81 was one of those natural turning points where everyone knew, I think, that it was time to move on to the next phase.

A New Hand on the Throttle

I came into Conrail well-rested and with a set of skills that the railroad needed at the time. Unlike Ed, who came out of the insurance and consulting industry, I'm an engineer by training, and a railroad man by birth and inclination. My father spent his entire career at the Southern Railway. So did I—except for two years 1963-65 as the Pennsylvania Railroad's Director of Industrial Engineering—forty-three years in all. I'd worn a lot of hats in those forty-three years—mechanical officer, engineering vice president, operating vice president, and chief executive. I'd come up in that company and knew how railroads work. There were very few surprises left for me in railroad operations.

The year 1980 was a turning point for me, too, because it marked the end of my career at the Southern Railway. But, I was not ready to retire at age 65. I'd only been CEO of the Southern for three and a half years, and was just starting to have some fun on the job. But the rules said I had to go, and so I went. I wanted to keep on working, but hadn't made any plans. When Conrail came to me, I really wasn't sure the job was what I wanted. I'd like to say I had faith in the company, but I'd been watching Conrail and its predecessors for a long time. I knew what the problems were—and how hard it is to change things.

On the other hand, when you're looking for a job—as I've said many times before—you can't be too choosy. I had some old friends up in Philadelphia, and liked the city. Besides, I wanted to know why a railroad as large as Conrail, with billions in revenue, couldn't hold onto any of it. Conrail had hundreds of locomotives in storage, hundreds of miles of unused track, too much plant and too little traffic. And all that cost money. After forty-three years in the railroad business, I thought I knew what it would take to make Conrail a viable, profitable company.

Equally important, I found out that I could work with USRA. Before I took the Conrail job, I met with Stephen Berger, who now heads the Port Authority of New York and New Jersey, and who had just come in as chairman of USRA. I'd had enough briefing to recognize that he was going to be a very key player in Conrail's future. We discussed the railroad's problems, my background, and the goals we both had for Conrail—not the least of which was finding out whether we could work together. We established an excellent relationship, which I'm proud to say continues today. Conrail produced for Steve and he gave Conrail his unqualified support.

In eight years at Conrail, I worked harder than I ever worked in my life.

Thanks to my predecessors at Southern Railway, Bill Brosnan and W. Graham Claytor, Jr., Southern was a smooth-running money machine. The biggest problem we had at the Southern was figuring out how to make more.

Other than testifying before Congress during the Staggers hearings, I never had to make the rounds in Washington, so I never thought of myself as a politician. Fortunately, in Brosnan and Claytor I had two of the best teachers a man could want. During certain periods of time at Conrail, I probably spent half my time in Washington, using lessons I learned from my mentors at Southern Railway.

Even though he was an operating man, Bill Brosnan was one of the first people in the railroad business to understand that our product had to be marketed—just like steel, VCRs, and frozen peas. He also understood the economics of the business. In the 1960s, when the interstate highway system opened and the trucks started “eating the railroads' lunch,” it was Brosnan who pushed for productivity improvements and focused our attention on the bottom line. He was also



A CONRAIL TRAIN LEAVES BEACON PARK YARD IN BOSTON. A PHILADELPHIA-BASED FREIGHT RAILROAD WITH OPERATIONS IN FOURTEEN STATES IN THE NORTHEAST AND MIDWEST, CONRAIL SERVES SIX OF THE NATION'S TEN LARGEST POPULATION CENTERS AND OPERATES OVER A NETWORK OF APPROXIMATELY 13,300 ROUTE MILES

a consummate politician—a man who loved a fight, a skillful presenter—smooth as could be. And I sat at his feet and learned from him.

Bill Brosnan brought Graham Claytor to the Southern Railway because we were fighting an important rate case in the Supreme Court. The Democrats were in the White House and Brosnan wanted a good Democratic lawyer to plead the case. Besides being a good Democratic lawyer, Claytor was also a good railroad man: he'd studied engineering in college and had a real love for the business. And he, too, was—and still is—a consummate politician, as he demonstrated as chief executive of the Southern Railway, as secretary of the Navy in the Carter administration, and today as CEO of Amtrak. When it comes to handling people and working the political side of things, there's not a better man in the world than Graham Claytor. And I was fortunate that he taught me a great deal of what he knew.

I didn't have a lot of time to settle into my new job at Conrail in the beginning of 1981. Things were happening too fast. In December 1980—before I was even on the payroll—the trainmen threatened to

shut down rail service in the entire Northeast. All of the freight, passenger and commuter service north of Washington and east of Pittsburgh was going to stop on Christmas Eve. At the time, Conrail's financial condition was precarious.

The railroad had nothing to lose. We had \$180 million in the bank and a January payroll of \$165 million coming due. I told the unions to go ahead and strike, but they didn't. On New Year's Eve, we signed the best agreement either side had gotten up to that time. And it gave us more flexibility in assembling and running our trains.

On January 1, 1981, when I took over, the biggest problem I had was in identifying all the things we needed to get from Congress in order to make Conrail profitable. Staggers helped because it enabled us to raise prices, but there were still serious structural problems that had to be addressed.

A Strong Dose of Reagan Reality

It so happened that another chief executive also took office in January 1981. Three weeks after I came in, Ronald Reagan took the oath of office, intent on honoring his pledge to cut federal spending to the bone. Conrail was a prime target. The new administration's Secretary of Transportation Drew Lewis had been a bankruptcy trustee of the Reading Railroad, one of Conrail's predecessors. Robert W. Blanchette, whom Mr. Lewis appointed head of the Federal Railroad Administration, had been counsel to the trustees of Penn Central and then a Penn Central trustee.

Both Mr. Lewis and Mr. Blanchette knew firsthand the problems of the northeastern rail system, and both looked at Conrail's prospects with a good deal of skepticism. It is easy to understand their honest belief that Conrail was beyond rescue and that breakup was the only prudent course.

It is important to understand the relationship between Conrail and the Department of Transportation at that time. On April 1, 1976, the trustees of the bankrupt railroads received 31.7 million shares of Conrail preferred stock and 25 million shares of common stock in exchange for the actual rail properties—until a settlement could be reached. This happened in 1980 and 1981 when the federal government paid the Penn Central \$2.1 billion and lesser amounts to the other predecessor railroads for their common and preferred stock.

Fifteen percent of the stock was then in the Conrail Employee Stock Ownership Plan (ESOP) that had been created on January 1, 1980. The remaining 85 percent reverted to ownership by the taxpayers, through the Congress.

However, there was some disagreement as to which executive branch department should have custody of the stock. The Departments of the Treasury, Labor, Commerce, and Transportation each felt they had a legitimate claim, and each argued its case vigorously. Ultimately, the Department of Transportation prevailed and obtained custody of the common stock. This was a decision of some significance, since whoever held that stock got to elect five of Conrail's eleven outside members of our Board of Directors. On changeover day, April 16, 1981, Mr. Lewis did indeed appoint five new and, if I may say so, well-qualified directors, all of whom held fast to their principles and their best judgment in overseeing Conrail.

As Transportation secretary, Mr. Lewis was a strong and persuasive advocate of the Reagan administration's agenda. Between January and April 1981, he and I met several times—along with Mr. Blanchette and John Fowler, the DOT's general counsel—in the secretary's office. It was a place I learned to know very well. At each meeting, they repeated their intention to liquidate Conrail and scrap what they couldn't sell. And at each meeting, I registered my strong dissent, for I believed that Conrail's prospects were stronger than they may have appeared.

Something happened in early February that gave me great cause for hope. According to our projections, Conrail needed another \$300 million to see us through 1981, until we could turn the corner and—we hoped—become profitable. In terms of the federal budget, \$300 million is a very small amount of money; yet, unless we had it written into the budget, we knew that the chances of getting any more money were very slim.

While Mr. Lewis was working hard to close the federal "tap," I was able to get an after-hours appointment to meet with David Stockman, the chief architect of the administration's fiscal policy, who had just been appointed director of the Office of Management and the Budget. I went to Mr. Stockman's office early one evening, and had half an hour to present my case. I told him what I needed and why; he asked several questions, and then said, "All right. I'm going to

put your \$300 million in the budget, but that's it. You're not getting another dime, so don't come back to see me again." In that way, we obtained our \$300 million—and we never touched a penny; I'm very proud of that.

The Anatomy of a Deal

During this same period, we were working on the document I mentioned earlier, which the Staggers Act required us to submit to Congress by April 1, 1981. In that document—often known as Final System Plan 2—we tried to identify the changes we had to have in order for Conrail to survive.

Not surprisingly, we found the same old problems—for which we offered some concrete solutions. Conrail's responsibility for commuter service, on which we'd lost upwards of \$250 million in five years, was one thing that clearly had to go.

We needed the freedom to rapidly abandon unprofitable lines—thousands of miles. We had to do away with the guaranteed salary provisions of the 3R Act, which had kept our labor costs at 60 percent of revenues. And, beyond that, we had to find a way of further reducing our labor costs by \$200 million a year for several years.

According to our information, key members of the House Energy and Commerce Committee, which would consider our recommendations—especially James Florio of New Jersey and John Dingell of Michigan—were favorably disposed toward Conrail. We thought we had a pretty good chance of getting the legislation we needed.

In the middle of April, Mr. Lewis invited me to visit with him at his farm. Once more, we engaged in a spirited debate over Conrail's future—our last, as it turned out—but were not able to resolve our difference of opinion.

Then, at the end of April, a week or so after our meeting, Mr. Lewis phoned me and offered a compromise: he would preserve Conrail as a single entity if we could pass a profitability test in 1982. I liked the idea, but felt that we needed more time, so I said, "That's not fair, Drew. I'm not going to be free of the passenger operation until December 31, 1982, and I've got to have time to run without the financial drag of the passenger operation on me before I can make it."

After some further discussion, we reached a compromise—there would be two profitability tests. Two benchmarks were established: On June 1, 1983, the USRA Board was mandated to determine whether Conrail would become a profitable carrier able to generate sufficient revenues to meet expenses and to borrow capital in the private market. The second test was to assess whether Conrail actually had achieved profitability between June 1 and October 31. If Conrail passed both tests, the secretary of Transportation would try to sell us in one piece. If we failed both or either one, then the original plan to liquidate the company would be adopted.

After that, Mr. Lewis and I had very little contact. He'd done what he set out to do, which was to get Conrail off the federal trough. In the meantime, his strong advocacy of the administration's fiscal agenda woke a lot of people up to a set of new realities. For too many years, too many people—including many at Conrail—had been willing to accept the proposition that Conrail would never be profitable; that we'd always need some form of handout to keep us going.

Drew Lewis turned that point of view around—and for that I thank him and his able rail administrator, Bob Blanchette. I firmly believe that if it had not been for their insistence that Conrail toe the mark, we probably would never have worked so hard, or succeeded in convincing labor to work with management toward our common objective of making the company profitable.

From Adversaries to Partners

Of all the things we needed in Final System Plan 2, getting \$200 million a year from labor would be the most difficult. Even though we'd gotten together on the 1978 crew reduction agreement and were making real progress in consolidating the hundreds of labor agreements we'd inherited from the bankrupt railroads, our relationship was still traditional—that is to say, adversarial.

Our position was firm, however. From the day I arrived, it was clear that Conrail was far too labor-cost-intensive. Conrail's pay levels were set by the national agreements, so our workers got exactly the same wages, working conditions and benefits as the employees of the profitable railroads. However, our labor cost was over 60 percent of revenues; the industry average was under 50 percent. By the time we

finished meeting our payroll, there was no money left for other things, and we ran at a deficit.

We had arrived at the \$200 million-a-year figure through rigorous analysis and a process of elimination that started with the amount of money we knew we had to cut from costs, and then subtracted everything we thought we could realistically cut from each area. Labor's contribution came to \$200 million annually for three years—and that was the number we used when we talked with Mr. Florio and others on Capitol Hill who were in a position to help us.

The man who played the critical role on the labor side was Fred Kroll, president of the Railway Labor Executives' Association and president of the Brotherhood of Railroad, Airline and Steamship Clerks. At the outset, Fred's position was the traditional one. He fought as hard as he could for his members and resisted any attempts on management's part to cut costs at labor's expense.

Two things happened to change his mind, however. The first occurred at a congressional hearing on Conrail. During Kroll's testimony, Senator John Danforth of Missouri interrupted to tell him that Secretary Lewis was absolutely serious about breaking up the railroad and selling it off, at the cost of tens of thousands of jobs. The second occurred when Fred found out for himself that Congress was counting on \$200 million annually from labor, and expected to see \$200 million when the totals were added up.

From that point on, Fred Kroll devoted all his considerable energies toward working with management to turn Conrail into a viable, self-sustaining corporation. Fred helped us work out the approximate 12 percent wage hold-down. Now, it's important to understand that this hold-down was not a reduction in pay, but a deferral of almost 12 percentage points of increases granted in any new national rail contract.

In spite of all Fred Kroll's courageous efforts—and this at a time when he was terminally ill with cancer and in constant pain—we were not sure until the eleventh hour that we actually had an agreement. We had called a press conference for May 5, 1981, where we planned to announce the agreement. The night before, the Railway Labor Executives Association met. Fred was the chief negotiator and was able to get all of the other labor leaders behind the agreement—except one. At that point, the negotiations almost collapsed; there hadn't been



CONRAIL'S PHILADELPHIA-BASED SYSTEM OPERATIONS BUREAU USES COMPUTER TECHNOLOGY TO ASSIGN LOCOMOTIVES TO WHERE THEY ARE NEEDED AND TO TRACK THEIR MOVEMENT AROUND THE SYSTEM. THE BUREAU'S COMPUTERIZED LOCOMOTIVE DISTRIBUTION SYSTEM HELPS CONRAIL TO ENSURE THAT ENOUGH LOCOMOTIVES ARE ON HAND AT EACH TERMINAL FOR THE AVAILABLE TRAFFIC, AND TO USE ITS LOCOMOTIVE FLEET MORE PRODUCTIVELY

any real progress as of 1 A.M. and everyone decided to call it a night. Finally, the parties got back together at 10 the next morning and kept working through lunchtime. They finally reached agreement about fifteen minutes before the press conference. The signing went off without a hitch.

That agreement was a major turning point in labor-management relations at Conrail. From that moment on, labor was no longer our adversary, but our partner. As a result of that understanding, I believe we have the best relationship with labor in the industry. All of us, on both sides, work very hard at improving communications, so each side understands the importance of the part they play in operating the railroad and keeping it profitable. We've established labor-management committees and quality circles for that purpose. Every year, we invite all of the more than 800 local chairmen to meetings throughout the system, where we exchange views openly and honestly.

I'm proud to acknowledge that Conrail's success today owes a great deal to Mr. Kroll's recognition that this wage deferral was in the long term interest of the railroad's employees. Without it, we could not have saved the company.

Fundamental Structural Change

In signing that May 5, 1981, agreement, we'd assembled everything we needed to make our end of the Final System Plan 2 work. Now we had to get all of it through the Congress. To do that, I relied heavily on William B. Newman, Jr., our vice president and Washington counsel. Bill is a young man—he won't reach forty for some time yet—but he's wise beyond his years to Washington and its ways.

I met Bill while I was still at Southern Railway and he was working for the House Energy and Commerce Committee, where he was heavily involved in helping with input for the Staggers Act. I had learned the importance of a good Washington point man during my years at the Southern. In my opinion, Bill was one of the best; when I came over to Conrail, I hired him right away.

Our staunchest ally in the Congress was James Florio, chairman of the House Transportation Subcommittee and a man who has strongly supported the congressional legislation that formed and strengthened Conrail. Prior to officially taking up my new post, Jim and I met at his office in New Jersey on a Saturday morning, where we could talk at length free from weekday pressure. We discussed some of the problems I saw at Conrail and some of the things I hoped to accomplish. He shared my conviction. Jim gave us his support. He played a key role in getting the Northeast Rail Service Act (NERSA) bill through the Energy and Commerce Committee and onto the floor of the House in 1981.

The passage of Northeast Rail Service Act is an interesting story in itself. In the House, NERSA was incorporated into the Democrats' budget reconciliation bill. At the time, however, David Stockman was leading his crusade to cut spending, and so the House Republicans came up with their own budget bill—the Gramm-Latta bill.

The NERSA proposal was already part of the Democratic bill; we were fortunate to get it tacked onto the Republican bill thanks to Congressmen Bud Shuster of Pennsylvania and Norman Lent of New York—two Conrail supporters. So no matter which bill passed—the

Republican version, as it turned out—Conrail obtained legislative help.

The result was different in the Senate, where the Republicans had the majority. Originally, the Senate bill provided for breakup only. My agreement with Drew Lewis on the profitability tests was added later on—but as the original plan for one test in 1982. Our friends were outnumbered. When Senator John Heinz of Pennsylvania tried to change the date of the profitability test, he was soundly defeated. The final Senate bill provided for one test, in 1982; if we failed it, as the bill assumed, we'd be broken up.

So here were two bills, one attractive, one less attractive. The differences were going to be ironed out in conference. When the bills got to conference, we thought we were in good shape. Congressmen Dingell, Florio, Lent, and Ed Madigan of Illinois, and Congresswoman (now Senator) Barbara Mikulski of Maryland represented the House. They were all from our territory, all close to rail labor—and people with whom I had good relations. The Senate side sent Senators Danforth, Robert Packwood of Oregon, Barry Goldwater of Arizona, and some others from outside our territory who had no strong feelings one way or the other.

Congressman Dingell and our other supporters in the House held for the House version. In its final form, NERSA provided for two profitability tests in 1983, both by USRA; transfer of the commuter service to local and regional authorities; elimination of full crew laws; elimination of Conrail's liability for wage guarantees; cash settlements to idle employees in exchange for severance payments to idle employees; exemption from state taxes; and expedited line abandonment procedures.

On August 13, President Reagan signed the Northeast Rail Service Act of 1981. Congress had given us the legislation we asked for. Now it was our turn to show the world—and ourselves—that we could compete successfully in the free and open market. We were on a roll, and we intended to make the most of it.

Fast Track to Profits

It's hard to imagine, thinking back to everything that had happened up to that point, that I'd been on the job only eight months. So much had happened in those eight months.

In retrospect, the ten months between the passage of Staggers, in October 1980, and August 1981, when President Reagan signed NERSA into law, is an amazing period in American railroad history. Seventy-five years of regulation—starting with the Hepburn Act of 1906—had undergone radical change. Labor, as far as Conrail was concerned, had changed from adversaries to partners. We were no longer locked forever into money-losing commuter contracts. We had the \$300 million in additional federal funding, if we needed it. And Conrail could set its own rates, downsize the plant without threat of litigation, and start to produce the kinds of service and marketing innovations we had to produce in order to compete successfully.

With all of those things taken care of, we were able to get to work in earnest. Not that we hadn't been forging ahead in the interim: while Bill Newman and I and a few others were busy down in Washington, many more people kept on running the railroad. Early on, I made it very clear to everyone at Conrail that there was only one gauge for success—the bottom line. No matter how well the railroad was running, no matter how modern the equipment, no matter the trend of traffic volume, if you didn't have something left at the end of the year, you didn't have anything. I'll say this: Everyone heard what I was saying and started tightening up on the expenses.

And it worked. All of a sudden, there was a little black on the bottom line for the second quarter of 1981 and a little positive cash flow. And no one was more surprised than I! We finished 1981 with a profit of \$39 million—the first annual profit in Conrail's history.

We did an awful lot of cutting. By the end of 1983, we managed to reduce our annual labor costs to less than 45 percent of annual revenues, from nearly 54 percent when I came in. We had an Industrial Development Department—which I started calling the “Industrial Abandonment Department”—that identified unprofitable line segments. Under the expedited abandonment procedure provided by NERSA, we were able to shrink the system by about 4,400 route miles—a quarter of our trackage, at a cost of less than 1 percent of the railroad's volume and 2 percent of its revenue.

It wasn't easy, making those cuts. We had to eliminate plant and take away jobs from communities that wanted and needed them—especially during those hard recession years of 1982 and 1983. It's never easy taking away someone's livelihood, but it had to be done.

We had to make an economic judgment about each facility, determine which ones could not make money, and get out. And that created some bad feelings.

With all of that, morale stayed amazingly high with our people. When we moved all our locomotive maintenance work to Altoona, for example, we decided to close down the old New York Central maintenance shop at Collinwood, Ohio. We had about 350 people working there, so it was a tough thing to do. They were good people, and I hated to lose them. Eventually, we rehired many of them when we expanded the Collinwood terminal. And when the fight came for an independent Conrail, that Collinwood shop committee stood up and carried the banner; they were unbelievable.

At the same time, we continued to invest about \$500 million a year on improving the plant we were going to keep—putting high-speed welded rail on our main line track, fixing up yards and terminals, investing in hi-tech locomotives, computers, and mechanized maintenance equipment.

We also had to refocus on marketing our services in the new environment. Traditionally, railroads had realized a lot of their volume from bulk commodities like coal, steel and chemicals. At one time, we had a great deal of automotive business, but that had fallen off during the 1960s and 1970s. Manufacturing had moved from the Northeast and Midwest out to the Sunbelt and across the Pacific to the Far East. Nevertheless, Conrail still sat on one of the richest and most concentrated consumer markets in the world. We realized that there was a tremendous opportunity in transporting high-value finished consumer goods—no matter where they come from. We also realized that it was a business we knew very little about.

We learned fast. For example, we began to understand that intermodal transportation—where truck trailers and marine freight containers are carried on special railcars—would become more important. So we had to reorient our thinking, and our money, into those areas—the terminals, the lifters that moved the containers and trailers on and off the railcars, and so forth. This was a whole new developing market opportunity for railroads; before deregulation, transporting high-value goods belonged mainly to the truckers. In the new environment, the railroads were starting to become a more important factor. It was an opportunity we could not, and did not, pass up.



LOCOMOTIVES IN FOR HEAVY REPAIRS AT THE JUNIATA LOCOMOTIVE SHOP IN ALTOONA, PA. THE SHOP, WHICH PERFORMS ALL OF THE HEAVY REPAIRS AND MAINTENANCE FOR CONRAIL'S FLEET OF MORE THAN 2,300 LOCOMOTIVES, IS PART OF ONE OF THE LARGEST COMPLEXES IN THE WORLD. DURING THE LATE 1970S AND EARLY 1980S, THE SHOP UNDERWENT AN EXTENSIVE MODERNIZATION PROGRAM TO IMPROVE ITS CAPABILITIES

By mid-1983, things really started looking up. We'd had another profitable year in 1982, with earnings of \$174 million, even though our revenue was off by more than 15 percent. Earnings for the first half of 1983 were \$110 million and revenues were on their way back up. Our performance was good enough for us to raise capital in the private market—a condition of the first USRA profitability test. On April 19, 1983, a consortium of twelve banks, led by Morgan Guaranty, granted us a \$100 million unsecured line of credit—which we never used. And on June 1, USRA announced that Conrail had demonstrated its ability to operate profitably, thus passing the first of the two tests mandated by NERSA. Two weeks later, the Railway Labor Executives' Association, representing Conrail employees, offered to acquire Conrail for \$500 million.

Suitors Come Calling

Despite our continuing improvement performance, at that time I still felt the railroad needed a strong, financially stable parent com-

pany, and so I approached the Santa Fe to discuss their interest in a possible merger. Santa Fe was a strong railroad, with a solid financial base. And unlike the merger with Norfolk Southern proposed by the Secretary of Transportation in 1984, a merger with the Santa Fe would preserve the greatest number of line jobs, since there was no route overlap; only senior management would be adversely affected.

The Santa Fe was very interested and, in mid-July their people announced that they would study the deal. This also pleased the new Secretary of Transportation—Elizabeth Dole had succeeded Drew Lewis a year earlier—since it represented an acceptable way to return Conrail to the private sector.

Then fate intervened. The Santa Fe had been interested in merging with the Southern Pacific for years, but without success. Then, during discussion of a possible Santa Fe-Conrail merger, the Southern Pacific suddenly changed its mind. In an instant, the Santa Fe-Southern Pacific deal was on, and a Santa Fe-Conrail deal was off.

With the Railway Labor Executives Association's \$500 million offer and the talks with the Santa Fe, the ball was rolling on Conrail's return to the private sector. Things speeded up after December 15, 1983, when USRA found, in its second profitability test, that Conrail was profitable during the June-October test period mandated in NERSA. Under those circumstances, the law required the Secretary of Transportation to try to return Conrail to the private sector as a single entity.

In hindsight, few of us expected the process to be so long and, at times, so full of controversy. In fact, there is still considerable disagreement as to the facts and motives of the various parties. In the interest of setting the record straight, what follows is my own recollection, reflecting my own point of view.

Secretary Dole did not really turn her attention to Conrail until mid-1983, when we passed the first of our profitability tests and the Railway Labor Executives Association made its offer. Even then, most of Conrail's dealings were with James Burnley, who since has succeeded Secretary Dole. Whatever differences we may have had—and there were many, no question about it—were principled differences of opinion, based on our understanding of the laws under which Conrail operated and our perceptions of what we thought best for Conrail's future.

As early as January 1984, CSX and Norfolk Southern expressed interest in acquiring Conrail. The first bid, other than that of RLEA, did not come in until April 10, when Alleghany Corp. submitted an offer of \$1 billion to Secretary Dole. A week later, Secretary Dole announced a June 18 deadline for other bids.

In all, she received fourteen formal offers, from a variety of publicly and privately held bidders. The Department of Transportation announced that it would evaluate the bids according to several criteria: (1) leaving the railroad in the strongest financial condition after the sale, (2) protecting service patterns to shippers and communities in the Northeast, and (3) offering the maximum return to the United States, consistent with the preceding criteria. Now, interestingly, the day after the deadline, Federal Railroad Administrator John Riley gave a speech before the National Industrial Transportation League, in which he stated that the secretary would also consider a public stock offering.

Two steps followed. On July 18, 1984, Secretary Dole announced six semi-finalists in the Conrail bidding—Alleghany Corp., Citicorp, Guilford Transportation Industries, an investor group headed by J. W. Marriott, Jr., the Railway Labor Executives Association, and Norfolk Southern. On September 11, she narrowed this group to three finalists—Alleghany, the Marriott group, and Norfolk Southern. Recognizing that there might be antitrust problems, she also submitted the Norfolk Southern offer to the Justice Department for review, as well as to the Treasury Department for further analysis.

Eventually, as we all know, she selected Norfolk Southern. They were a very solid bidder, and Secretary Dole's selection of Norfolk Southern was entirely proper; they were an excellent choice. They had more cash than anybody else, and there was no question they had the management to run the railroad profitably. The issue for us at Conrail revolved around the fact that this acquisition would cost many jobs. And it would give Norfolk Southern something approaching a monopoly in rail transportation in the eastern half of the United States.

A Justice Department study—carried out by the office of the Deputy Attorney General in the Antitrust Division—also concluded that the Norfolk Southern merger would raise some serious antitrust questions. However, the Justice Department decided that the merger

would not violate the antitrust statutes—providing certain other actions were taken to enhance competition.

We were not so sure. For more than a year, Conrail's legal department, under Bruce Wilson, then our general counsel and vice president of Law, and himself a former deputy attorney general at the Antitrust Division, carried out its own exhaustive analyses of the Department of Transportation plan.

"Let Conrail Be Conrail"

By mid-1984, sentiment was starting to build for an independent Conrail that would be sold through a public stock offering. I had first floated that idea a year earlier, in an interview with Agis Salpukas of the *New York Times*, to which Secretary Dole took strong exception. An independent Conrail was not something that we had given much discussion to, but certainly one approach that seemed more and more attractive, considering Conrail's performance.

Others obviously felt the same way. In June 1984, as I noted, the Federal Rail Administrator, Mr. Riley, had stated publicly that Secretary Dole would consider a public offering. In the early fall, Senators Heinz and Arlen Specter urged the administration to toss out the bids, halt the auction process, and sell Conrail to the public.

We made our first public declaration for a public offering in October 1984. Senator Specter called hearings to consider the impact of the Conrail sale on the Pennsylvania economy. We decided that Bob Platt was our most eloquent and persuasive spokesman, and was most familiar with the numbers. Now once we'd turned our full attention to how we wanted to enter the private sector, every one of us concluded that a public offering was really the only idea that made sense. We'd had earnings of \$313 million in 1983, and were projecting 1984 income of nearly \$500 million; we had more than \$800 million in cash. We were a going concern that didn't need any more protection—corporate or otherwise.

The hearing before Senator Specter was extremely important to us because he was a Republican and a valued administration ally in the Senate. If we could convince him to support us, that would carry a lot of weight at the White House and on Capitol Hill.

Mr. Riley preceded Bob Platt at the witness stand and launched

into a scathing attack on Conrail's viability and a public offering. Then, as forcefully as he could, Bob Platt delivered the message that, in our view, the sale to Norfolk Southern would be a disaster for the state of Pennsylvania—not to mention the employees of the company, who had sacrificed a great deal, and who had lived in uncertainty since the Penn Central collapse. It was clear that a lot of people would lose their jobs in the merger. It would have taken a terrible human cost.

Further, the economics of the deal did not make sense—unless you happened to be Norfolk Southern. They were offering \$1.2 billion for a company whose book value was \$3.4 billion—a quarter of which was in cash—plus tax benefits worth another \$1 billion. Moreover, such a merger would present the shippers with one less option for shipping their rail freight and would create serious disadvantages for CSX, which competed with Norfolk Southern in many important markets.

At that point, the lines were drawn. Secretary Dole and Mr. Burnley grew more insistent on their position, and we grew more insistent on ours. In December 1984 Bob Platt and Thomas Saunders, managing director of the investment banker Morgan Stanley, presented our own plan to the Conrail Board. This plan met all of Secretary Dole's conditions, including cash up front. It provided for a public offering of equity stock only, that would net the government \$1.2 billion. The Board agreed that we ought to forward the proposal to the Department of Transportation, which we did on January 4, 1985. Nevertheless, a month later Secretary Dole formally recommended to Congress that it approve the sale of Conrail to Norfolk Southern.

The only way I can describe the next twelve months is "trench warfare." Both sides—Conrail and the Department of Transportation—used whatever legitimate means we had to convince the Congress that ours was the right solution. We spent hours and hours giving testimony before Congressional committees, made the rounds in Washington and out across America, trying to build a base of support from labor, shippers and opinion leaders.

Every member of our senior management team put in time and energy far beyond the call of duty. Bill Newman routinely put in eighty-hour weeks seeking congressional support in Washington. Bob Platt—and his successor after retirement, Bill Brown—kept in close

touch with Wall Street, building support in the financial community. Bob Swert was in constant contact with our unions. Charlie Marshall, our senior vice president of Marketing and Sales and one of our brightest stars, met with shippers and asked for their support. Bruce Wilson and his gifted legal staff pored over every document the other side put out, finding flaws in their arguments and rebutting them brilliantly, and testified before Congress when I didn't. Saul Resnick, our vice president for Public Affairs, stayed up nights writing editorial columns under my name, letters to editors by the hundreds, and getting numerous editorials favorable to Conrail run in newspapers in key congressional districts across the country. Dick Hasselman and his people kept the railroad moving. In all, it was a team effort that brought out the very finest in an extraordinarily talented, committed and hard-working group of people.

The support grew—slowly, at first, then faster and faster.

- On April 1, 1985, USRA reported that, according to its figures, Conrail would earn about \$1.4 billion in the 1985-1988 period, as an independent company, paying industry-scale wages, federal and state taxes, and labor protection expenses—just like other railroads.
- In May 1985, Morgan Stanley announced that it had formed an investor group, representing some of the most prestigious institutions in America, to acquire the government's 85 percent interest in Conrail, for subsequent resale through one or more public stock offerings.
- In July, the Railway Labor Executives Association came out in support of a public offering and an independent Conrail.
- On August 1, the Coalition for a Competitive Conrail (CCC), a group of more than 150 public officials, farm organizations, shippers and labor unions, banded together to oppose the sale of Conrail to Norfolk Southern.
- On August 16, the Executive Council of the AFL-CIO issued a statement supporting Conrail.
- On November 24, the National Industrial Transportation League, representing hundreds of shippers nationwide, endorsed the public offering.

In the meantime, questions were being raised within the administration about the viability of the DOT plan. In September 1985, the ICC released a staff study which concluded that both Guilford Transportation Industries and the Pittsburgh & Lake Erie Railroad—two small regional lines that the DOT claimed would compete effectively with the combined Norfolk Southern-Conrail—were likely to be driven out of business instead. Rather than easing shippers' concerns about a rail monopoly, the study only intensified them.

The Department of Transportation was not standing still, however. It, too, argued its case widely and persuasively—to shippers, other railroads, politicians, newspaper editors and the financial community. And their efforts, too, were rewarded with support from a host of key figures in the Northeast and elsewhere. Obviously, there were those who would benefit from a Norfolk Southern-Conrail combination.

To complicate things, another offer was made on December 18, when Allen & Co. and First Boston Corp. formed the Conrail Acquisition Corp., and offered at least \$1.4 billion for the government's Conrail stock. The Morgan Stanley group matched the price on January 16, 1986.

The Moments of Truth

The time for a decision was fast approaching. At the end of January 1986, the question came to the floor of the Senate. There, the then Majority Leader, Senator Robert Dole, used his considerable skills and influence to gather support for the DOT plan. Senator Specter's amendment offering the Morgan Stanley plan as a substitute was defeated 54-39—the same margin by which the DOT plan passed on February 4. I think we all knew, deep down, that we were going to lose in the Senate. Even so, it was a bitter pill for all of us, who'd fought long and hard. But the House still had to consider the issue, and we had a lot of friends there.

In fact, even before I came to Conrail, during the time that Staggers was passed, there was a very dedicated group of eastern and midwestern congressmen who were strong supporters of Conrail. One of those strong allies was Michigan Representative John Dingell, chairman of the House Energy and Commerce Committee and a fierce

defender of competition. Early on, Mr. Dingell and I used to meet together to discuss Conrail and its future.

Mr. Dingell had been watching the DOT's efforts with great interest and had some serious reservations about the antitrust aspects of the Norfolk Southern merger. Nor were his reservations allayed when the DOT and Justice Department were not as responsive as he would have liked to his repeated requests for information and clarification. A public statement by the Congressional Budget Office, on February 26, that the sale to Norfolk Southern would cost the government \$250 million in revenue and tax income between 1987 and 1991 only added fuel to his doubts.

On April 29, 1986, Mr. Dingell publicly expressed these concerns. "The administration's proposal to sell Conrail to Norfolk Southern," he said, "is mired in a hopeless swamp of confusion and controversy. If Conrail is to be returned to the private sector, a new plan must be devised. . . . Any new plan should preserve Conrail as an independent entity and afford the public a fair opportunity to participate in the ownership of the railroad."

Secretary Dole responded by saying, "I believe we can address all his concerns." A week later, on May 6, she advised Norfolk Southern to raise its bid from \$1.2 billion to \$1.9 billion, including \$500 million of Conrail's cash. The higher offer, she maintained, was justified by the economy's strong recovery and lower interest rates since 1984, when the auction was held.

On May 8, Mr. Dingell repeated his earlier statement that "any plan to merge Conrail with Norfolk Southern remains unacceptable," and called upon Secretary Dole to move forward with him in a bipartisan public offering plan. The next day, after Norfolk Southern raised its offer to \$1.9 billion, Mr. Dingell said, "As far as I'm concerned, the notion of selling Conrail to Norfolk Southern is dead."

The House Energy and Commerce Committee then proceeded to formulate guidelines for the legislation that would permit the federal government to sell its Conrail stock to the public. On August 19, Norfolk Southern Corp. conceded that its offer was all but dead, adding that it would not "alienate Congress on a futile kamikaze mission." Secretary Dole endorsed a public offering plan in August, as long as Conrail's viability could be ensured.

On October 8, the House and Senate reached final agreement on a bill authorizing the federal government to sell Conrail through a public stock offering; on October 21, President Reagan signed the Conrail Privatization Act into law. The act authorized the public offering, with a goal of \$2 billion to be raised from the stock sale and cash transfers totaling \$300 million from Conrail.

On March 26, 1987—a little more than a year ago—Conrail returned to the private sector. The initial public offering of 58,750,000 shares at \$28 per share was the largest in U.S. history, raising \$1.645 billion before underwriting fees. That day, Conrail was the most active issue on the New York Stock Exchange, with volume of 18.2 million shares.

It was a long road, but we made it.

The Track Ahead

In the year since, Conrail has proven itself as a viable, competitive private-sector transportation company. In the dozen years of our existence, we lived out 100 years of railroad history—moving from the restrictive regulation and capital-starvation of the past into the market-driven, innovative and successful company of today and tomorrow. We are leaders in the intermodal market—the fastest growing transportation market in the world. We have a well-balanced mix of business, with no single business segment contributing less than 10 percent or more than 18 percent of our revenues. We have some of the most progressive agreements and labor relations in the industry. Our physical plant is among the most modern in the industry, with high-speed continuous welded rail on nearly 100 percent of our mainline track. We have invested heavily in computerized communications, train dispatching, engineering and customer service systems. Our service innovations, such as the high-speed interregional through trains that we run with CSX, Union Pacific and Santa Fe, set the new standards by which rail transportation is judged in the deregulated environment.

In all, I believe we are well-positioned to expand our market share and move toward the twenty-first century as one of the most modern and innovative transportation and distribution companies in the world.

But the track ahead is not totally clear, for our industry today is confronting an effort to reregulate the railroads that threatens to return us to the dark ages we so recently left behind.

This effort has been going on for some time—since the passage of Staggers, in fact. A small group of special interests—primarily coal companies and utilities operating under the misnomer “Consumers United for Rail Equity” (CURE)—is seeking to legislate lower rail rates for themselves, irrespective of the costs to other consumers and the impact on competition in the U.S. transportation sector. In this battle, I might add, we, the Administration and the Department of Transportation are fighting on the same team.

In 1986, CURE attempted to use the sale of Conrail as a vehicle to change Staggers; the White House and DOT worked diligently to see that such language was not included in the Conrail Privatization Act. Late in 1987, however, CURE successfully lobbied the House Subcommittee on Transportation, Tourism and Hazardous Materials to recommend a bill that would eliminate many of the benefits of the Staggers Act. Ironically, CURE’s members are among the prime beneficiaries of deregulation: Between 1981 and 1987, average freight revenue per ton decreased by 3.7 percent a year; between 1981 and 1985, coal rates declined by more than 10 percent. During the same period, electric utility profits have more than doubled.

If enacted, this CURE-sponsored legislation threatens to plunge America’s railroads back into the morass of legislated unprofitability by forcing them to:

- establish joint rates, terminal access and reciprocal switching arrangements at the request of any shipper or competing carrier, at rates that would preclude an economic return on investment;
- prove, upon shipper request, that their rates for a substantial portion of traffic are reasonable, vastly increasing rate litigation and inhibiting the implementation of economically justified rate increases; and
- pass through to shippers, in the form of lower regulated rates, all gains in efficiency retroactive to 1980.

The scenario is all too familiar. By crippling the railroads' ability to respond effectively to competition from other modes of transportation, such legislation would endanger the long-term viability of America's railroads—just as similar regulation did earlier in this century. Over time, railroads would fade as a competitive force in freight transportation. And all consumers—including the coal and utility interests behind CURE—would end up paying the price.

It is a serious threat but at the age of 72, going on 73, I'm not sure I want to think about it. It will be just one of the challenges my successor—Mr. Richard D. Sanborn, whom our board elected president and chief operating officer on February 29 this year—will have to contend with. Equally important, he, and the generations of Conrail leadership to come, will have to decide where this company will be going in the next twenty or thirty years and how it will get there. Mr. Sanborn is a man of broad background and experience in railroading, and I have a high degree of confidence that he is the right man to lead Conrail into the future.

At the end of 1988, I will leave with some regrets over things left undone—not because of oversight, but because there just hasn't been enough time. For the last eight years, I've been, as the old Baptist minister used to say, "so taken up tending to the needs of my flock, that I ain't had time to prepare a proper sermon." Perhaps Mr. Sanborn will have the time and vision to prepare the sermon.

In the meantime, at this turning point, I look back on my career at Conrail and consider that I've been given a great gift. I've had the chance to apply everything I learned in one lifetime of railroading—plus some new lessons in things I never imagined. I've had the chance to live through some of the most exciting times a railroad man could ever hope to live through. I've had the chance to work hard, make friends, and make a difference. And I've had the priceless opportunity to leave one piece of the world in better shape than I found it.

And isn't that what life is all about?

THE END



"Actorum Memores simul affectamus Agenda!"



THE NEWCOMEN SOCIETY OF THE UNITED STATES

IN APRIL 1923, the late L. F. Loree (1858-1940) of New York, then dean of American railroad presidents, established a group now known as "American Newcomen" and interested in Business History, as distinguished from political history. Its objectives center in the beginnings, growth, development, contributions, and influence of Industry, Transportation, Communication, the Utilities, Mining, Agriculture, Banking, Finance, Economics, Insurance, Education, Invention, and the Law—these and correlated historical fields. In short, the background of those factors which have contributed or are contributing to the progress of Mankind.

The Newcomen Society of the United States is a nonprofit membership corporation chartered in 1961 under the Charitable Law of the State of Maine, with headquarters at 412 Newcomen Road, Exton, Pennsylvania 19341, some five miles east of Downingtown, Pennsylvania, and 32 miles west of the City of Philadelphia. Here also is located The Thomas Newcomen Memorial Library and Museum in Steam Technology and Industrial History, a reference collection, including microfilm, open to the public for research and dealing with the subjects to which the Society devotes attention.

Meetings are held throughout the United States of America and across Canada at which Newcomen Addresses are presented by leaders in their respective fields.

The approach in most cases has been a life-story of corporate organizations, interpreted through the ambitions, the successes and failures, and the ultimate achievements of those pioneers whose efforts laid the foundations of the particular enterprise.

The Society's name perpetuates the life and work of Thomas Newcomen (1663-1729), the British pioneer, whose valuable contributions in improvements to the newly invented Steam Engine brought him lasting fame in the field of the Mechanic Arts. The Newcomen Engines, whose period of use was from 1712 to 1775, paved a way for the Industrial Revolution, Newcomen's inventive genius preceded by more than 50 years the brilliant work in Steam by the world-famous James Watt.

The Newcomen Society of the United States is affiliated with The Newcomen Society for the Study of the History of Engineering and Technology, with offices at The Science Museum, South Kensington, London, S.W. 7, England. The Society is also associated in union with the Royal Society for the Encouragement of Arts, Manufactures and Commerce, whose offices are at 6 John Adam Street, London, W.C. 2, England.

Members of American Newcomen, when in Europe, are invited to visit the home of Thomas Newcomen at Dartmouth in South Devonshire, England, and to see the Dartmouth Newcomen Engine working.

