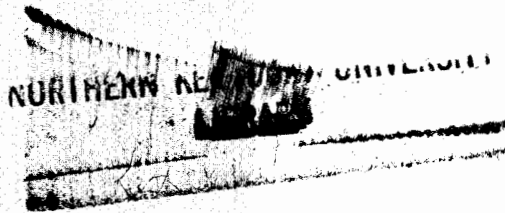


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Issue Brief



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CONRAIL SALE: LABOR ASPECTS

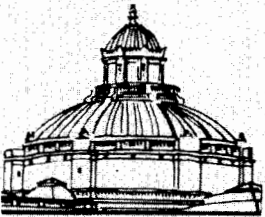
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ISSUE DEFINITION

The Northeast Rail Service Act of 1981 requires the Secretary of Transportation to sell the Federal Government's 85% interest in Conrail. Conrail employees own 15% of Conrail's stock. Conrail's 39,000 employees, through the Rail Labor Executive Association (RLEA), made a proposal to buy Conrail, one of 15 proposals submitted to buy Conrail. RLEA, however, was not among the final three bidders for Conrail selected by the Department of Transportation. These were the Alleghany Corp., the Norfolk Southern Corp., and the Marriott Investment Group, Inc. (Norfolk Southern was ultimately recommended to be the purchaser.) Conrail's management and some Members of Congress favor a public sale of Conrail's stock. Rail labor has been in negotiations with the various bidders over three main concerns -- job protection, employee equity in the company, and payment of wage deferrals. In examining the issues in Conrail's sale, Congress most likely will consider the welfare of Conrail employees as affected by the terms and conditions of the sale. Should negotiations on labor conditions with the final bidder fail, Congress might be asked to include labor conditions as part of any legislation related to the sale of Conrail.

BACKGROUND AND POLICY ANALYSIS

In 1970, the Penn Central Railroad and several other railroads in the Northeast and Midwest went bankrupt. Seeking a solution to the rail transportation problem, Congress passed the Regional Rail Reorganization Act of 1973 (the 3R Act), enacted as P.L. 93-236. The 3R Act provided for the restructuring of the rail system in the Northeast and Midwest, and created the United States Rail Association (USRA) which was instructed to create a financially self-sustaining rail system that would minimize unemployment and adverse impact on communities, preserve existing patterns of rail service, and retain and promote competition. The 3R Act also provided for the establishment of a for-profit corporation, Conrail, to operate the restructured system. The worker protections provided by the 3R Act were paid by the Federal Government.

Under the Northeast Rail Act of 1981, Conrail was to be sold as an entity if USRA determined Conrail would be a profitable carrier by June 1983. If it was determined Conrail would not be profitable by then, it was to be sold piecemeal. Conrail's passenger services were transferred to other authorities leaving Conrail with only freight service.

The Rail Labor Executive's Association (RLEA) is comprised of 19 labor organizations whose members work for the railroads. RLEA made the first bid to purchase Conrail in June 1983. At the same time, RLEA created a five member Special Conrail Task Force to look out for the interest of the employees during the sale.

By July 1984, the Department of Transportation (DOT) had received 15 bids for the purchase of Conrail. The number of bidders receiving active consideration by DOT was narrowed to three -- Alleghany Corporation, Norfolk Southern Corporation, and an investment group headed by J. Willard Marriott. In January 1985, Conrail management submitted to DOT a proposal for the public sale of Conrail's stock. On January 30, 1985, RLEA gave its endorsement to the Alleghany Corp. as the preferred purchaser of Conrail. On

this date also, Representative Edgar introduced in Congress H.R. 787, the Conrail Privatization Act of 1985, which provides that Conrail be sold through a public stock offering.

On Feb. 8, 1985, Secretary of Transportation Elizabeth Dole recommended to Congress that Conrail be sold to the Norfolk Southern Corp.

The Senate Committee on Commerce, Science and Transportation held hearings on Feb. 27 and 28, 1985, to review the sale process and all the bids for Conrail. The Committee reported out the bill, S. 638, the Conrail Sale Amendments of 1985, on Apr. 30, 1985.

The House Subcommittee on Transportation of the Committee on Energy and Commerce held hearings on the Conrail sale on Apr. 18 and 30, 1985.

Job Protection

Job loss under any new owner of Conrail is of major concern to the rail unions. Employment effects depend on who purchases Conrail. There were three types of bidders: (1) employees, (2) railroad companies, (3) outside investors. Employee ownership is seen as the most favorable for preserving jobs, i.e., would result in the least displacement of workers. A Conrail sale to another railroad could result in the most displacement of workers.

Major reductions in Conrail's workforce have occurred since it was formed in 1976. In 1976, there were between 95,000 and 97,000 employees. In January of 1985, employment totaled about 38,500 workers.

The rail unions argue that if Conrail is sold to the Norfolk Southern as many as 10,000 to 15,000 Conrail jobs could be in jeopardy because of duplication of Conrail and Norfolk Southern trackage (Daily Labor Report, 10/29/84, p. A6). In addition, the rail union's estimate that the dismantling of Conrail headquarters in Philadelphia could result in 4,800 workers being unemployed because Norfolk Southern is headquartered in Virginia.

Norfolk Southern contends that only about 2,500 jobs would be lost if they bought Conrail. However, Conrail management estimates that more than 8,000 jobs would be eliminated if Conrail were sold to Norfolk Southern (Daily Labor Report, 2/19/85, p. A11).

Senator Heinz, upon introducing S.Res. 72 relating to a public offering of Conrail, stated that "Employee protection is of vital concern in the Conrail sale. No action should be taken in Congress in the absence of sound information on how many jobs will be lost in a Conrail-Norfolk merger."

Senator Hollings believes a sale to Norfolk Southern would be beneficial to rail labor as a whole because the merger would provide more certainty of financial strength and the potential for layoffs seems minimal. In addition, Hollings states, Norfolk Southern's bid guarantees labor protections. [Cong. Rec. Mar. 7, 1985, p. S2718]. However, Senator Spector believes that the covenant requiring Conrail's Philadelphia headquarters be maintained for 5 years is too short in duration and its enforcement impractical. It is obviously inevitable, Spector argues, that Norfolk Southern would eventually consolidate, resulting in loss of jobs. [Cong. Rec., Mar. 7, 1985, p. S2698 and S2700].

The RLEA's Special Conrail Task Force has been involved in job protection talks with each of the bidders and with representatives of DOT. Job protections being sought by rail labor include provisions for continued employment of present employees, reduction in workforce through attrition, severance pay in case of job loss, and other job protections. As a result of the discussions, covenants on the Conrail sale contract relating to job protection are being sought. One such proposed covenant is a requirement to continue full freight service, which would assure employees that their jobs will continue.

"New York Dock" labor protections have also been proposed in some of the bids. Under the New York Dock Railway worker protection agreement, in the event of an employment displacement transaction, a railroad is required to: (1) give at least 90 days advance written notice to labor of the details of the action; (2) negotiate with labor an agreement providing for selection and assignment of forces acceptable to both parties; (3) pay to each employee, whose position is worsened as a result of the change, a "displacement allowance" for as long as 6 years; (4) pay to each employee deprived of employment a monthly "dismissal allowance" equal to 100% of his average monthly compensation during the preceding year, less earnings from other employment or unemployment insurance payments, for as long as 6 years; (5) maintain all employment benefits included in his previous employment such as free transportation, pensions, and hospitalization; (6) pay a lump sum separation allowance of up to 12 months' pay in lieu of all other benefits at the option of the employee; (7) pay moving expenses for each retained employee required to move his residence including losses from home sale; (8) resolve all disputes arising under this agreement by arbitration; and (9) grant a laid-off employee, if he requests, priority for employment for vacant positions for which he is qualified or can become qualified for through an employer provided training program.

Employee Equity and Wage Deferral

How much of the new company will the employees own?

At the present time, 15% of Conrail stock is placed in an Employee Stock Ownership Plan (ESOP) that is to be completely transferred to the employees by 1991. Additional employee ownership of stock was included in several proposals for Conrail, often coupled with employee representation on the board of directors.

In a May 1981 agreement, the rail unions accepted deferrals in wage increases in order to keep Conrail viable. The 3 years of wage deferrals (between June 1981 and June 1984) have been estimated to be worth about \$400 million. Labor wants this \$400 million wage deferral to be paid to the workers upon the sale of Conrail. The Special RLEA Conrail Task Force has indicated a preference for receiving this sum in stock rather than cash payment. If given in stock, the workers would own approximately 30% of the new railroad.

The Special RLEA Conrail Task Force is of the opinion that a cash buyout of the employee interest would not be to the employees' advantage. Without employee participation in Conrail ownership, according to the Task Force, the workers' future security would be reduced.

As a consequence of the wage deferrals, Conrail workers have been earning about 12% less than workers on other class I railroads. Since May 1984,

restoration of the wage deferrals has been the subject of negotiations between the rail unions and Conrail. The agreement expired on July 1, 1984. An agreement reached with 10 of its 17 unions in February 1985 restores the 12% in deferred wages to base pay retroactive to July 1, 1984 (Daily Labor Report, 1/15/85, p. A8).

Rail Labor's Bid

In June 1983, the first serious offer to buy Conrail was made by the RLEA in the name of all Conrail's employees, union and nonunion. Although RLEA's bid for Conrail was not among the finalists, some of the other purchase offers contained elements similar to the labor bid.

The RLEA proposal submitted to the Secretary of Transportation would have paid approximately \$2 billion for Conrail (Daily Labor Report, 6/14/83, p. A10). The proposal included cash in the amount of \$500 million, and the return of tax credits to the Government worth about \$1.2 billion. The employees would have also extended the wage increase deferrals for 3 years. Continued wage deferrals, however, were not made available to other buyers. After buying the 85% of Conrail stock held by the Federal Government, RLEA proposed to sell approximately 20-30% of the stock publicly. The board of directors would include management members and labor representatives as well as "outsiders."

In June 1984, a revised bid doubled the original cash payment to \$1 billion. The proposed employee ownership of stock was changed to 40% for employees and 60% public. Three labor-appointed persons were suggested to serve on the board of directors made up of 11 members.

RLEA's interest in purchasing Conrail is to save jobs, continue Conrail as an entity and to protect present employees.

The Reagan Administration and the Department of Transportation have shown no interest in selling Conrail to its employees.

RLEA Endorses Alleghany Corp. Bid

On Jan. 29, 1985, RLEA agreed to conditionally support the Alleghany Corp. in its bid to purchase Conrail. Alleghany was the only one of the three final bidders that all 19 unions of the RLEA could accept.

The proposed labor protection plan in the Alleghany bid would run for 5 years. A fund of \$30 million per year would be set up to pay workers laid off or furloughed. Any unused funds at the end of a year would be carried over to the following years (Daily Labor Report. 1/31/85, p. A9).

Alleghany reportedly was offering to give the employees 35% of Alleghany's stock over a 5-year period and would place three labor members on Conrail's board of directors and one labor representative on the board of the holding company, Alleghany Corp.

RLEA's continuing support for Alleghany depends on reaching agreements on labor protections and on settling the employees' exact stake in the company.

RLEA said it was the best alternative in a situation where there were different opinions. According to a union leader "there was no question

Alleghany's offer was best for Conrail employees. Alleghany would be writing a check for about a billion dollars and they would give the employees about 35% of the company" (Daily Labor Report, 1/31/85, p. A9).

Representatives Edgar and Florio expressed opposition to the Alleghany bid claiming that such a sale would not be fair to the public nor the region Conrail serves.

DOT Picks Norfolk Southern

The Secretary of Transportation recommended to Congress that Conrail be sold to the Norfolk Southern Corp. The proposal included a minimum of \$1.2 billion in cash, and a series of covenants to assure a viable rail service (Daily Labor Report, 2/11/85, p. A8). For instance, one such covenant suggested was that Norfolk Southern must maintain Conrail substantially as it is for 5 years.

Job protections included \$375 million for past wage deferrals and the workers 15% of Conrail's stock. The proposal also included \$124 million annually to be added to employee's current wage scales; and \$15 million to aid employees to participate in the company's stock purchase plan. No provision was offered for labor representatives on the board of directors.

Negotiations with the rail unions would establish the labor conditions. If negotiations failed to produce an agreement, labor conditions might have to be included in legislation. Norfolk Southern has indicated that the New York Dock agreement would be acceptable.

Rail union leaders have questions concerning the continuance of competitive freight service if Norfolk Southern becomes the only railroad in some areas by taking over Conrail. Antitrust problems, according to the Secretary of Transportation, have been resolved.

According to Richard Kilroy, president of the Brotherhood of Railway and Airline Clerks (BRAC), the sale of Norfolk Southern would "create havoc in the northeastern and midwestern United States, devastate the lives of thousands of rail employees, disrupt shippers, and destroy competition" (Daily Labor Report, 2/11/85, p. A8). However, Fred Hardin, president of the United Transportation Union, claims it might be the best plan for Conrail employees (Daily Labor Report, 2/12/85, p. A13). According to Hardin, financial stability of the Norfolk Southern and its proven ability to operate a railroad "probably would insure a Conrail forever" (Daily Labor Report, 1/29/85, p. A9).

Conrail management has expressed opposition to the Norfolk Southern purchase because of the possible impact on employment.

Public Stock Offering

On Jan. 30, 1985, Representative Edgar introduced a bill, H.R. 787, to provide for the sale of the common stock of the Consolidated Rail Corporation by public offering. The proposal in Representative Edgar's bill would give the employees about a 30% interest in the company but would limit to 10% the holdings permitted to any single owner.

Conrail management has been pushing for public stock offering similar to

the original RLEA employees offer to purchase Conrail.

Conrail management submitted to DOT a formal bid for the carrier on Jan. 4, 1985. The offer would generate \$1.4 billion through a public stock offering plan, and includes an eventual 30% ownership of the carrier by its employees. Also, under the management plan two union representatives would serve on the board of directors.

On May 14, 1985, Morgan Stanley & Co., Inc., an investment company, proposed to purchase the Federal Government's 85% interest in Conrail. The proposal, involving about 25 "blue-chip" investors, has been valued at approximately \$1.8 billion [Cong. Rec. May 21, 1985, p. E2303]. The proposal includes public interest covenants equivalent to those negotiated between the DOT and Norfolk Southern. The investor group would resell their stock to the public over a 5-year period. No single investor would own more than 10% of Conrail stock. The present Conrail ESOP would be preserved. Employees, in addition, would be provided the option of participating in the investor group and purchasing common stock. Two labor representatives would serve on Conrail's Board of Directors. Labor protections would be negotiated through the collective bargaining process.

The Reagan Administration, Secretary of Transportation, and Federal Railroad Administrator Riley have fought against selling Conrail on the stock market. They favor a sale to an individual purchaser, claiming that it would leave Conrail in the strongest condition after the sale. Furthermore, they argue, there would be no guarantees that present freight services could be maintained. DOT argues that the covenants which have been included in the bids could not be included in a public sale.

Shearson Lehman Brothers, Inc., an investment advisor for Norfolk Southern, claims that the Morgan Stanley proposal would drain the railroad of cash and weaken the railroad's long-term survival. Furthermore, they argue that the labor protection under the Norfolk Southern proposal is stronger because it offers the New York Dock protections to employees. [Daily Labor Report, 5/22/85, p. A13-14].

Richard Kilroy, president of BRAC, believes that employees would be better protected under the Conrail management plan than by the Norfolk Southern proposal. According to Kilroy, Conrail's plan would best serve the freight shippers and communities served by Conrail and eliminate the antitrust implications of the railroad merger.

The RLEA's Special Conrail Task Force has begun talks on job protection provisions under the Morgan Stanley proposal.

A public offering had been incorporated in the RLEA bid for Conrail.

Supporters for a public stock offering claim that it would raise more money for the Federal Government than a sale to a single buyer.

Several Members of Congress and Conrail management support the Morgan Stanley proposal. Senator Spector, upon introducing the bill, S. 1137, the Conrail Public Offering Act of 1985, claimed that the proposal would provide "taxpayers with a superior return on their investment in Conrail..." and would ensure "long-term employment for Conrail workers...." [Cong. Rec., May 15, 1985, p. S6256].

LEGISLATION

H.R. 787 (Edgar)

Conrail Privatization Act of 1985. Provides for the sale of the common stock of Conrail by public offering. The Secretary of Transportation would be required to sell all common stock shares owned by the United States to Conrail for \$1.4 billion. Conrail would be required to offer for public sale 85% of the shares with 15% of the shares being made available to or for the benefit of Conrail employees. Introduced Jan. 30, 1985; referred to Committee on Energy and Commerce.

H.R. 1455 (Applegate)

Requires that the Secretary of Transportation reopen bidding for Conrail and make a greater effort to maximize the return to the United States upon Conrail's sale. Introduced Mar. 7, 1985; referred to Committee on Energy and Commerce.

S. 464 (Spector)

Railroad Competition Protection Act of 1985. Declares that the Secretary of Transportation may not enter into any agreement with the Norfolk Southern Corporation. Introduced Feb. 19, 1985; referred to Committee on Commerce, Science, and Transportation.

S. 465 (Spector)

Railroad Competition Protection Act of 1985. Declares that the disposition of Conrail shall be by public stock offering and not by private sale. Introduced Feb. 19, 1985; referred to Committee on Commerce, Science, and Transportation.

S. 638 (Danforth) / H.R. 1449 (Broyhill)

Conrail Sale Amendments of 1985. Amends the 3R Act to provide for the transfer of ownership of Conrail to the private sector. Section 108 requires Norfolk Southern Corporation to provide New York Dock labor protections after the sale for employees adversely affected by the merger. Eligible employees adversely affected may receive up to 6 years pay. S. 638 introduced Mar. 7, 1985; referred to Committee on Commerce, Science, and Transportation. Markup session held April 18. Ordered to be reported, favorably and with amendments, Apr. 30, 1985. H.R. 1449 introduced Mar. 6, 1985; referred to Committee on Energy and Commerce.

S. 1137 (Specter)

Conrail Public Offering Act of 1985. Requires that any disposition of the Government's interest in Conrail proceed by public stock offering in accordance with the proposal presented by Morgan Stanley & Co., Inc., on May 14, 1985. Introduced May 15, 1985; referred to Committee on Commerce, Science and Transportation.

HEARINGS

U.S. Congress. Senate. Committee on Commerce, Science, and Transportation. Subcommittee on Surface Transportation. DOT sale of Conrail. Hearing, 98th Congress, 2nd session. June 20, 1984. Washington, U.S. Govt. Print. Off., 1984, 35 p.

REPORTS AND CONGRESSIONAL DOCUMENTS

- Congress must carefully examine alternatives in Conrail sale.
In Extension of Remarks of James J. Florio. Congressional record [daily ed.] v. 131, Feb. 6, 1985: E371-E372.
- Conrail Public Offering Act. In Remarks of Arlen Spector.
Congressional record [daily ed.] v. 131, May 15, 1985: S6255-6256.
- The Conrail sale. In Remarks of John Heinz. Congressional record [daily ed.] v. 131, Mar. 14, 1985: S2996-2997.
- The Conrail Sale Amendments of 1985. In Remarks of John C. Danforth, Congressional record [daily ed.] v. 131, Mar. 7, 1985: S 2711-2717.
- Conrail sale question. In Extension of Remarks of Thomas M. Foglietta.
Congressional record [daily ed.] v. 131, May 21, 1985: E2303-2304.
- The Conrail Privatization Act of 1985. In Extension of Remarks of Bob Edgar. Congressional record [daily ed.] v. 131, Jan. 30, 1985: E250-E251.
- DOT obstructs congressional review of Conrail sale. In Remarks of Robert G. Torricelli. Congressional record [daily ed.] v. 131, Mar. 27, 1985: E1165.
- Introduction of H.R. 1930, legislation providing for the sale of Conrail. In Remarks of Dan Rostenkowski.
Congressional record [daily ed.] v. 131, Apr. 4, 1985: E1354.
- Introduction of the Sale of Conrail Act of 1985.
In Remarks of James T. Broyhill. Congressional record [daily ed.] v. 131, Mar. 6, 1985: H1067-1068.
- Let's not derail the Conrail deal. In Remarks of James T. Broyhill. Congressional record [daily ed.] v. 131, Mar. 26, 1985: E1107.
- Pennsylvania House Resolution 31. In Remarks of Bob Edgar.
Congressional record [daily ed.] v. 131, Mar. 26, 1985: E1110.
- Proposed sale of Conrail to Norfolk Southern.
In Remarks of Ernest Hollings. Congressional record [daily ed.] v. 131, Mar. 28, 1985: S3745-3748.
- S. 464 - Relating to the Sale of Conrail. In Remarks of Arlen Spector. Congressional record [daily ed.] v. 131, Feb. 19, 1985: S1381-1383.
- S. 683 - Conrail Sale Amendments of 1985. In

Remarks of Arlen Specter, Congressional record [daily ed.] v. 131, Mar. 7, 1985: 2697-2711.

The sale of Conrail. In Remarks of Ernest Hollings. Congressional record [daily ed.] v. 131, Feb. 19, 1985: S1394-S1395.

Senate Resolution 72 - Relating to a public offering of Conrail. John Heinz. Congressional record [daily ed.] v. 131, Feb. 19, 1985: S1444-S1446.

CHRONOLOGY OF EVENTS

- 05/14/85 -- Morgan Stanley & Co., Inc., an investment firm, submitted a public stock offering proposal for the purchase of Conrail to DOT and Congress.
- 05/01/85 -- House Committee on Ways and Means held a hearing on the tax aspects of the Conrail sale proposal.
- 04/30/85 -- House Committee on Energy and Commerce Subcommittee on Commerce, Transportation, and Tourism held a hearing on Conrail.
- 04/18/85 -- Hearings were held by the House Subcommittee on Transportation of the Committee on Energy and Commerce.
- 04/04/85 -- Hearings were held by the Senate Committee on Commerce and by the Senate Subcommittee on Transportation of the Committee on Appropriations.
- 02/27-28/85 -- Hearings were held by the Senate Committee on Commerce.
- 04/04/85 -- Senate Committee on Commerce held a hearing on DOT's proposed sale of Conrail.
- 02/08/85 -- Secretary of Transportation recommended Conrail be sold to Norfolk Southern.
- 01/30/85 -- RLEA announced its endorsement of the Alleghany Corp. bid for Conrail.
- 09/11/84 -- Secretary of Transportation announced the three most likely bidders for Conrail -- Alleghany Corp., Norfolk Southern, and the Marriott Investment Group.
- 06/20/84 -- Senate Subcommittee on Surface Transportation of the Committee on Commerce, Science and Transportation held hearing on the sale of Conrail by DOT.
- 06/18/84 -- The deadline for receiving bids was set by DOT.
- 06/00/83 -- RLEA submitted first bid for Conrail to the DOT.