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THE CONRAIL SALE: STILL THE TAXPAYERS' BEST DEAL

(Updating Issue Bulletin No. 113, "Giving Conrail a Green Light," February 15, 1985.)

Item number one on the docket when the Senate reconvenes tomorrow is a long-delayed vote on the sale to the Norfolk-Southern Corporation of Conrail, the federally owned freight railroad. The decision to sell Conrail was made by Congress in 1981. The Department of Transportation (DOT) spent two years evaluating potential buyers before deciding last February to recommend that the bid by Norfolk-Southern be accepted. The offer is a good deal for the taxpayer and those served by the Conrail network. It will ensure that the privatized Conrail will have a healthy future.

In the year since it began considering the Norfolk-Southern bid, Congress has reminded the nation why politicians cannot run a railroad. Rather than acting quickly to slice at least \$1.2 billion from the federal deficit, lawmakers have delayed acceptance of the bid, bowing to pressure from special interests in their districts.

Since Transportation Secretary Elizabeth Dole announced her sensible decision, two additional offers for Conrail have been made. A group of investors (including CSX, Norfolk-Southern's prime competitor) organized by the Morgan Stanley investment banking firm offered \$1.2 billion in May, and last week upped its offer to \$1.4 billion. In December, Allen & Company and the First Boston Corporation offered to pay between \$1.4 and \$1.65 billion for the railroad. But this group, unlike the other two, would not forgo the \$300 million in investment tax credits now held by Conrail. This plan, therefore, would likely leave the U.S. Treasury no better off than the others.

In any event, there are important factors that favor Norfolk-Southern's bid. Most important, Norfolk-Southern will provide

Conrail with essential financial resources. While Conrail is now making a profit, the railroad business in the northeast has been very cyclical. A downturn in business could quickly drain Conrail's financial reserves, again putting the company in jeopardy. Conrail's profits for 1985, in fact, were less than predicted at the beginning of the year. A strong parent corporation, such as Norfolk-Southern, could shield Conrail from temporary earnings downturns. By contrast, the two alternative bids would not add to Conrail's resources. In fact, under the Morgan Stanley proposal, over \$375 million of Conrail cash would be siphoned off immediately after the sale to make payments to employees and to raise part of the purchase cost. It should be stressed that competition in the industry will not be impaired by merging Norfolk-Southern with Conrail. The Antitrust Division of the Department of Justice has conducted a thorough review of this issue and finds that, if some divestitures are made, the acquisition of Conrail by Norfolk-Southern will not harm competition. Norfolk-Southern already has agreed to sell many vital lines to other railroads, under a plan approved by the antitrust enforcers, ensuring that competition will continue and perhaps even increase.

The most important objective of lawmakers should be to see that Conrail is returned to the private sector. This will ensure that commercial factors, rather than politics, will determine its long-range structure. Secretary Dole's plan for Conrail's privatization is sound. If approved by Congress, the U.S. could begin to enjoy both the long-term and immediate benefits of Conrail's sale.

Yet Congress has taught the Administration and the taxpayers a bitter political lesson during the year-long struggle to sell Conrail. Lawmakers have served notice that they are more interested in responding to constituency pressure than in obtaining the best deal for the taxpayer or in cutting the federal deficit. Future attempts to sell federal assets should be planned with this in mind. If a rerun of the delay and frustration associated with the Conrail sale is to be avoided, the Administration should build a wide coalition with a vested interest in each privatization. If a stock offering is proposed, for instance, blocks of shares should be awarded at a discount, or even free of charge, to key constituencies, such as employees.

Gaining the support of politically powerful constituencies in this way admittedly means less revenue from the sale for the taxpayer. But many Congressmen seem prepared to block sensible privatization in order to protect small groups of constituents. That is the political reality Congress has created. Giving such constituents a vested interest in each sale, and creating strong coalitions around future proposals, is thus necessary to smooth the way for further privatization, benefitting all Americans.

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