IN THE SUPREME COURT OF MISSISSIPPI

CANADIAN NATIONAL RAILWAY COMPANY — APPELLANT

VS. — CASE NO. 2011-IA-00951-SCT

KATHLEEN K. WALTMAN, ADMINISTRATRIX OF THE ESTATES OF ROBERT LEE KITCHENS, JR. AND MARY L. KITCHENS, DECEASED, AND INDIVIDUALLY; AND ROBERT LEE KITCHEN, III — APPELLEES

BRIEF OF APPELLANT

On appeal from the Circuit Court of Copiah County, Mississippi

Submitted By:

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COMPANY

Appellant believes this Court has already decided the issues raised herein in Appellant's favor, and therefore, **ORAL ARGUMENT IS NOT REQUESTED.**

CERTIFICATE OF INTERESTED PERSONS

The undersigned counsel of record certifies that the following listed persons have an interest in the outcome of this case. These representations are made in order that the Justices of the Supreme Court and/or Judges of the Court of Appeals may evaluate possible disqualification or recusal:

1. Canadian National Railway Company, a foreign national corporation;
2. Illinois Central Railroad Company;
3. Charles Hodges, employee of Illinois Central Railroad Company;
4. James K. Smith, employee of Illinois Central Railroad Company;
5. Jeff Lewis, employee of Illinois Central Railroad Company;
6. Kevin Douglas, employee of Illinois Central Railroad Company;
7. Charles Cunningham, employee of Illinois Central Railroad Company;
8. Ron Wegers, employee of Illinois Central Railroad Company;
9. Kathleen K. Waltman, Administratrix of the estates of Robert Lee Kitchens, Jr. and Mary L. Kitchens, deceased;
10. Robert Lee Kitchens, III;
11. John W. Kitchens, Kitchens Law Firm, P.A., Crystal Springs, Mississippi, attorney for appellees;
12. Pat M. Barrett, Jr. and Jonathan P. Barrett, Barrett Law Office, P.A., attorneys for appellees;
13. Alexander F. Guidry, Mockbee, Hall & Drake P.A., attorney for appellees;
14. Rodney Entrekin, Ferris Burson & Entrekin, PLLC, attorney for co-defendants Illinois Central Railroad Company and its employee defendants;
15. George H. Ritter and James E. Graves, III, Wise Carter Child & Caraway, P.A., attorneys for appellants;

16. Honorable Lamar Pickard, Circuit Judge, Circuit Court of Copiah County, Mississippi.

James Graves, III

GEORGE H. RITTER
JAMES E. GRAVES, III

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STATEMENT OF ISSUES

The following issues are presented to the Court in this appeal:

1. Whether, on the mere unsubstantiated, conclusory allegations in the pleadings, a trial court may preliminarily pierce the corporate veil of a foreign corporation and thereby circumvent the necessity of establishing personal jurisdiction;

2. Whether the court erred in refusing to dismiss the Complaint for lack of personal jurisdiction and allowing merits discovery based upon the mere allegation that Canadian National Railway Company's indirect subsidiary Illinois Central Railroad Company is its "alter ego" and a "mere instrumentality"; and,

3. Whether the court erred in allowing the Plaintiffs to conduct discovery in order to support their claim for corporate veil piercing where the Plaintiffs have failed to allege the elements of a corporate veil piercing claim under Mississippi law as required by this Court's decision in *Penn Nat'l Gaming, Inc. v. Ratliff*, 954 So. 2d 427 (Miss. 2007).

STATEMENT OF THE CASE

I. Procedural History

Plaintiffs originally filed this wrongful death action on May 8, 2009, against Canadian National Railway Company ("Canadian National Railway"), Illinois Central Railroad Company ("Illinois Central") and several Illinois Central employees to recover damages related to a railroad crossing accident that occurred on May 9, 2008, at Monticello Road in Hazlehurst, Mississippi, which resulted in the death of Robert Lee Kitchens, Jr. and Mary L. Kitchens. On June 24, 2009, Canadian National Railway (a Canadian corporation with its principal place of business in Montreal, Quebec, Canada) filed its first motion to dismiss asserting lack of service, lack of jurisdiction, and failure to state a claim. After the trial court denied this motion, Canadian National Railway petitioned this Court for interlocutory appeal. This Court granted the petition and vacated the order denying the motion to dismiss finding that Plaintiffs had not served process on Canadian National Railway. This Court did not address Canadian National Railway's 12(b)(2) or 12(b)(6) defenses.

Plaintiffs then amended their complaint and served Canadian National Railway pursuant to the Hague Convention. [R at 12-23 – Excerpt No. 3] On December 17, 2010, Canadian National Railway again moved to dismiss pursuant to Miss. R. Civ. P. 12(b)(2) and 12(b)(6). [R at 37-86] Plaintiffs responded to the motion on January 10, 2011. [R at 87-167] After hearing oral arguments, the Court entered an order on June 17, 2011, granting Plaintiffs ninety (90) days to conduct discovery "to justify piercing the corporate veil" and reserved its ruling on the motion to dismiss pending completion of that discovery. [R at 184-188 – Excerpt No. 2] On July 7, 2011, Canadian National Railway timely filed a petition for interlocutory appeal, which was granted by this Court on September 8, 2011. [R at 201] All proceedings in the trial court as to Canadian National Railway have been stayed. [R at 201]

II. Pertinent Factual Background

The undisputed facts show that: (1) Plaintiffs have not met their burden of establishing personal jurisdiction over Canadian National Railway; and, (2) the Plaintiffs failed to state a cognizable claim for piercing the corporate veil against Canadian National Railway in their Amended Complaint.

A. The Allegations of the Amended Complaint

The Plaintiffs, the Administratrix and wrongful death beneficiaries of Robert Lee Kitchens, Jr. and Mary L. Kitchens, deceased, filed their Amended Complaint on September 23, 2010, against Canadian National Railway and Illinois Central.[1] [R at 12-23 – Excerpt No. 3] Plaintiffs allege that Mr. and Mrs. Kitchens were killed in a collision with a freight train at Monticello Road in Hazlehurst, Mississippi on May 9, 2008. [R at 6 – Excerpt No. 3] They further allege that due to previous false activations of the automatic flashing light signals at the crossing, the Kitchens were lulled into a sense of false security by the flashing lights, thus causing the subject accident. [R at 18 – Excerpt No. 3]

The Amended Complaint also names as Defendants Illinois Central's locomotive engineer Charles E. Hodges, conductor David E. Moak, and signal and track department employees–James K. Smith, Jeff Lewis, Kevin Douglas, Charles Cunningham, and Ron Wegers– who were responsible for maintenance of the crossing and warning lights. [R at 13-14 – Excerpt No. 3] These individuals were employees of Illinois Central and not Canadian National Railway. [R at 42-43, 45 – Excerpt Nos. 4, 5]

Plaintiffs do not allege any independent negligence of Canadian National Railway. Rather, they allege that Illinois Central is the "alter ego" and a "mere instrumentality" of its "dominant shareholder" Canadian National Railway. [R at 14 – Excerpt No. 3]

B. Jurisdictional Facts

Illinois Central is a freight railroad operating in the United States, including Mississippi. [R at 43, 45, 47 – Excerpt Nos. 4, 5, 6] Illinois Central owns tracks and has employees in the state of Mississippi. [R at 43, 45, 47, 70-77 – Excerpt Nos. 4, 5, 6, 8] It is an Illinois

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[1] The Amended Complaint also names as Defendants "Canadian National Railway Company, d/b/a Illinois Central Railroad Company; Illinois Central Railroad Company, d/b/a Canadian National Railway Company; and Illinois Central Railroad Company, d/b/a Canadian National/Illinois Central Railroad Company." Appellant's correct name is Canadian National Railway Company. The correct name of its indirect subsidiary is Illinois Central Railroad Company.

corporation, registered to do business in Mississippi, but with its principle place of business in Homewood, Illinois. [R at 43 – Excerpt No. 4] Since May 23, 1997, Illinois Central has been a wholly-owned subsidiary of Illinois Central Corporation, a Delaware corporation. [R at 43 – Excerpt No. 4] Illinois Central Corporation is the sole shareholder of Illinois Central and several other corporations. [R at 43 – Excerpt No. 4] Illinois Central Corporation is a wholly-owned subsidiary of Grand Trunk Corporation, a Delaware corporation, which in turn is a wholly-owned subsidiary of Canadian National Railway. [R at 43 – Excerpt No. 4]

For a period of time after 1998, Illinois Central sometimes did business as "Canadian National/Illinois Central Railroad Company" or "CN/IC." [R at 43 – Excerpt No. 4] By July 2004, Illinois Central no longer did business under either of those names. [R at 43 – Excerpt No. 4] However, Illinois Central does use and operate under the tradename "CN" and the "CN" logo. [R at 43 – Excerpt No. 4] As a result of the similarity between these names, some Illinois Central employees and non-employees have erroneously referred to Illinois Central as "Canadian National" or "Canadian National Railway" instead of the trade name "CN" or the correct legal name "Illinois Central Railroad Company." [R at 43-44] These facts are undisputed in the record.

Canadian National Railway moved to dismiss pursuant to Rule 12(b)(2) for lack of personal jurisdiction. [R at 37-41] It established through affidavit testimony that it does not operate as a railroad in the state of Mississippi, owns no land or tracks in the state of Mississippi, has no employees in the state of Mississippi, is not registered to do business in Mississippi, and has no agent for service in Mississippi. [R at 42-77 – Excerpt Nos. 4, 5, 6, 7, 8] It further established through affidavits and W-2 forms that the co-defendant employees alleged in the

Complaint to have been negligent were at all times employees of Illinois Central and not Canadian National Railway. [R at 43, 45, 70-77 – Excerpt Nos. 4, 5, 8] Canadian National Railway also established through sworn affidavits as well as land records that Illinois Central, and not Canadian National Railway, was the owner and operator of the train involved in the collision and the tracks where the collision occurred. [R at 47-68 – Excerpt No. 6] The evidence also showed that the subject train was powered by two locomotives, each of which had a large "IC" logo on the front and "Illinois Central" printed on the sides. [R at 80, 182, 183 – Excerpt Nos. 10, 12, 13] Plaintiffs submitted no competent evidence to rebut any of these facts.

C. The Trial Court's Order

On June 17, 2011, the learned trial judge issued his order on Canadian National Railway's motion to dismiss and found the following facts to have been established by the record:

- The subject train was operated by Illinois Central Railroad Company, an Illinois corporation with its principal place of business in Homewood, Illinois.
- Illinois Central Railroad Company operates as a railroad in Mississippi, owns land and tracks in Mississippi, including the subject railroad crossing, and files tax returns in Mississippi.
- Illinois Central Railroad Company employed the individuals who allegedly committed the act or omissions in the Plaintiffs' Complaint.
- Illinois Central Railroad Company is a wholly owned subsidiary of Illinois Central Corporation, a Delaware corporation that is a wholly owned subsidiary of Grand Trunk Corporation. Grand Trunk Corporation is a wholly owned subsidiary of

Canadian National Railway, a Canadian corporation with its principal place of business in Montreal, Quebec, Canada.

[R at 184-185 – Excerpt No. 2] The trial judge noted that under Mississippi law, the "corporate veil should not be preliminarily pierced for purposes of exercising long-arm jurisdiction based on mere unsubstantiated allegations of the complaint." [R at 185 – Excerpt No. 2] He further found:

> **The Supreme Court has recently held that in Mississippi, undercapitalization alone is not a basis for disregarding the corporate entity.** *Stanley v. Mississippi State Pilots of Gulfport, Inc.*, 951 So.2d 535, 542 (Miss. 2006). Plaintiffs allege [u]ndercapitalization in the form of negative Net Worth based on an unaudited 2008 Balance Sheet as a basis for fraud, along with consolidated financial statements with the parent corporation and depositions of corporate employees. These assertions alone will not satisfy the heavy burden to disregard the corporate entity to reach the foreign corporation.

[R at 186-187 – Excerpt No. 2 (emphasis added)] Despite its findings that the Plaintiffs had not presented sufficient **evidence** to satisfy their admittedly "heavy burden," the trial court held that the "Plaintiffs have presented sufficient **allegations** to justify limited further discovery into the 'alter ego' or 'mere instrumentality' issue" and granted Plaintiffs ninety (90) days "to provide the court with evidence sufficient to justify piercing the corporate veil." [R at 187 – Excerpt No. 2 (emphasis added)] The Court reserved ruling on the motion to dismiss until the completion of the 90-day discovery period. [R at 187 – Excerpt No. 2]

SUMMARY OF THE ARGUMENT

The trial court's order is clearly erroneous and contrary to law because (1) it allows discovery without first requiring the Plaintiff to plead and prove sufficient facts to establish personal jurisdiction over Canadian National Railway, and (2) it does not dismiss Plaintiffs' claims despite this Court's mandate in *Ratliff* that a plaintiff must allege facts supporting the elements of a corporate veil piercing claim and may not rely solely upon conclusory allegations of dominance and control. Moreover, despite the Circuit Court's acknowledgment that "undercapitalization alone is not a basis for disregarding the corporate entity," it erroneously allowed discovery even though the Plaintiffs' only argument for why the corporate veil should be pierced and/or that discovery should be allowed was their contention that Illinois Central was undercapitalized. For these reasons, and as discussed more fully below, the order of the trial court should be reversed, and Plaintiffs' claims against Canadian National Railway should be dismissed with prejudice.

ARGUMENT

I. Plaintiffs Failed to Establish Personal Jurisdiction over Canadian National Railway

Even though it is undisputed that Canadian National Railway is a foreign corporation that does not do business in Mississippi, Plaintiffs contend personal jurisdiction exists based solely on their unsubstantiated allegation that Illinois Central is the "alter ego" or is a "mere instrumentality" of Canadian National Railway. This theory presupposes that Plaintiffs have alleged or otherwise established a *prima facie* case for corporate veil piercing when, in truth, neither the allegations in the Amended Complaint nor Plaintiffs' response to the motion to dismiss satisfy their burden of establishing *in personam* jurisdiction over Canadian National Railway.

Under Mississippi law, once a defendant submits affidavits or other competent evidence disputing the jurisdictional allegations of the complaint, the plaintiff is required to submit evidence "demonstrat[ing] jurisdiction by a preponderance of the evidence." *Hogrobrooks v. Progressive Direct*, 858 So. 2d 913, 919-20 (Miss. 2003). Thus, it was incumbent upon the Plaintiffs to submit competent evidence rebutting Canadian National Railway's sworn affidavits and other evidence. Because the Plaintiffs' jurisdictional argument depends entirely upon piercing Illinois Central's corporate veil, their burden requires competent evidence establishing each element of a corporate veil piercing claim under Mississippi law.[2]

In both contract and tort cases, the Mississippi Supreme Court has stated the following rule with regard to corporate veil piercing:

> [T]he corporate entity will not be disregarded . . . unless the complaining party can demonstrate (1) some frustration of expectations regarding the party to whom he looked for performance; (2) the flagrant disregard of corporate formalities by the defendant corporation and its principals; and (3) a demonstration of fraud or other equivalent misfeasance on the part of the corporate shareholder.[3]

Ratliff, at 431. Plaintiffs submitted no proof of any frustration of an expectation they had of Canadian National Railway, nor did they establish flagrant disregarded for corporate formalities. Most significantly, Plaintiffs failed to argue or even allege anything that would constitute fraud or equivalent misfeasance on the part of Canadian National Railway. In fact, the record was and is undisputed that Canadian National Railway:

- did not own the subject crossing or warning devices;

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[2] The evidence filed by Canadian National Railway was submitted in support of its motion to dismiss pursuant to Rule 12(b)(2). The 12(b)(6) portion of Canadian National Railway's motion is based on the allegations of the complaint alone. *See Horne v. Mobile Water & Sewer Sys.*, 897 So. 2d 972, 975 (Miss. 2004) (consideration of jurisdictional evidence outside the pleadings does not convert Rule 12(b)(2) motion to a Rule 56 summary judgment motion).

[3] This Court has declined to adopt the ten factor test utilized by federal courts in favor of this three-part test. *Buchanan v. Ameristar Casino Vicksburg, Inc.*, 957 So. 2d 969, 977 (Miss. 2007).

- did not maintain the subject crossing or warning devices;
- did not own or operate the train involved in the subject accident;
- did not employ the locomotive crew or other individuals who Plaintiffs allege caused the accident;
- does not own any tracks or operate any trains in the state of Mississippi;
- does not have any employees located in the state of Mississippi; and,
- does not own any property in the state of Mississippi.

The only support Plaintiffs offered for their veil piercing theory was a financial statement showing that Illinois Central had a negative net worth in 2008, which they contend supports a finding that Illinois Central is undercapitalized. [R at 102 – Excerpt No. 11] However, as the Circuit Court expressly held, a showing of negative net worth and/or undercapitalization would be insufficient to "satisfy the heavy burden to disregard the corporate entity to reach the foreign corporation." [R at 186-187 – Excerpt No. 2] And, the Mississippi Supreme Court has expressly held that while other jurisdictions have considered a showing of undercapitalization to be sufficient to pierce the corporate veil, that simply "**is not the rule in Mississippi.**" *Stanley*, 951 So. 2d at 542. To the contrary, the Court in *Buchanan* considered and expressly rejected a test that included undercapitalization as a factor in considering whether to pierce the corporate veil and instead chose to adopt the three-factor test discussed above that does not include such a factor. 957 So. 2d 969, 976-977. Consequently, even if the Plaintiffs' negative net worth evidence was sufficient to establish undercapitalization, under clearly established Mississippi law, that fact alone would not justify piercing the corporate veil.

Furthermore, the 2008 net worth statement submitted by Plaintiffs says nothing about whether Canadian National Railway adequately capitalized Illinois Central at the it became an indirect subsidiary of Canadian National Railway, which is the relevant time period courts in other jurisdictions have looked to when determining whether a corporation is undercapitalized. *Seymour v. Hull & Moreland*, 605 F.2d 1105, 1112-13 (9th Cir. 1979) (rejecting argument that period of poor financial performance was sufficient to pierce the corporate veil where there was no evidence of fraud, that the corporation was not adequately capitalized at the time of formation, or that the corporation owed less than enough assets to carry out its business). In fact, the exact financial statements on which Plaintiffs rely show that Illinois Central has $493 million of paid in capital. [R at 102] In the words of a federal district court that rejected an argument identical to the one Plaintiffs make here: "When a corporation is adequately funded at the outset, bad financial times later do not raise an inference of fraudulent intent." *Whitney v. Wurtz*, 2007 WL 1593221, at *6 (N.D. Cal. Jun. 1, 2007). Plaintiffs have submitted no proof that Illinois Central was not a going business concern when acquired by Canadian National Railway. In other words, not only is undercapitalization of the subsidiary insufficient to establish personal jurisdiction over a parent, but Plaintiffs have not even shown that Illinois Central was undercapitalized. At most, they have shown that Illinois Central went through some tough economic times. Such a showing, however, is not sufficient to establish undercapitalization and definitely is not enough to prove fraud. *Seymour*, 605 F.2d at 1112-13 ("We cannot infer fraud . . . simply on the basis of bad financial times.").

Plaintiffs also contend that the consolidation of Illinois Central's financial reports with those of Canadian National Railway is evidence that Illinois Central is a "mere instrumentality" of Canadian National Railway. "However, consolidating the activities of a subsidiary into the parent's annual reports is a common practice" and "is allowed by both the Internal Revenue Service and the Securities and Exchange Commission." *Calvert v. Huckins*, 875 F.Supp. 674, 678-79 (E.D. Cal. 1995) (citing *Lowell Staats Min. Co. v. Pioneer Uravan, Inc.*, 878 F.2d 1259, 1264 (10th Cir. 1989), and *Volkswagenwerk Aktiengesellschaft v. Beech Aircraft*, 751 F.2d 117, 121 n.3 (2nd Cir. 1984)). In fact, consolidated financial reports are required where the parent owns at least fifty percent of the subsidiary's stock. *Volkswagenwerk*, 751 F.2d at 121 n.3 (citing American Institute of Certified Public Accountants, Consolidating Financial Statements, Accounting Research Bulletin No. 51, at pg. 2 (1959)[4]). *See also* Surface Transp. Bd. Decision, STB Ex Parte No. 634, Nov. 7, 2001 (requiring consolidated financial statements for railroads operating in the United States).[5] Courts addressing these types of consolidated financial statements have uniformly found that they do not establish parental involvement in the subsidiary's day-to-day operations or sufficient minimum contacts on which to predicate *in personam* jurisdiction. *Epps v. Stewart Information Servs. Corp.*, 327 F.3d 642, 650 (8th Cir. 2003) (finding SEC 10-K filings insufficient to prove parent corporation directly does business in the forum state); *Alberto v. Diversified Group, Inc.*, 55 F.3d 201, 207 (5th Cir. 1995) (filing of consolidated income tax returns by parent corporation insufficient to fix liability on parent corporation). *See also Doe v. Unocal Corp.*, 248 F.3d 915, 928 (9th Cir. 2001) (holding that "references in parent's annual report to subsidiaries or chains of subsidiaries as divisions of the parent company do not establish the existence of an alter ego relationship" sufficient to establish general jurisdiction over parent corporation); *Akzona, Inc. v. E.I. DuPont De Nemours & Co.*,

[4] A true and correct copy of this decision is attached hereto as Exhibit A.

[5] A true and correct copy of this decision is attached hereto as Exhibit B.

607 F. Supp. 227, 237 (D. Del. 1984) (finding language of annual report describing subsidiaries as divisions insufficient to establish liability of parent corporation). In considering this evidence, the Circuit Court once again found that these types of consolidated financial records did not "satisfy the heavy burden to disregard the corporate entity to reach the foreign corporation," but it nevertheless failed to grant Canadian National Railway's motion to dismiss. [R at 186-187 – Excerpt No. 2] This was clearly in error.

No Mississippi or federal district court case applying Mississippi law has approved personal jurisdiction over a foreign corporation by piercing the corporate veil of its resident subsidiary. In fact, Mississippi state and federal district court cases addressing this issue have refused to find jurisdiction based upon the actions of the resident subsidiary. *Hogrobrooks*, 858 So. 2d at 921 (dismissibg claims against parent corporation for lack of personal jurisdiction); *Tupelo Mfg. Co. v. Cope Indus., Inc.*, 2006 WL 924036 (N.D. Miss. 2006) (finding no personal jurisdiction over shareholder where "nothing in the record to indicate the type of fraud, malfeasance, or wrongdoing necessary to employ the doctrine of piercing the corporate veil"); *Lifeline Ambulance Servs., Inc. v. Laidlaw, Inc.*, 16 F. Supp. 2d 686, 688 (S.D. Miss. 1998) ("[A]bsent a sufficient allegation of particularized facts, judicial economy requires that the corporate veil should not be preliminarily pierced for long-arm jurisdiction on the mere unsubstantiated allegations in the pleadings."); *North Am. Plastics, Inc. v. Inland Shoe Mfg. Co.*, 592 F. Supp. 875, 879 (N. D. Miss. 1984) ("[T]he corporate veil should not be preliminarily pierced for long-arm jurisdiction on the mere unsubstantiated allegations in the pleadings."). Likewise, courts have rejected plaintiffs' attempts to conduct jurisdictional discovery over a foreign parent corporation. *E.g.*, *Lifeline Ambulance*, 16 F. Supp. 2d at 690 (rejecting request for discovery to establish jurisdiction based upon corporate veil piercing theory); *Brown v. Readwood, Inc.*, 1996 WL 33370666, at *3 (N. D. Miss. 1996) (same). Based on the insufficient allegations in Plaintiffs' Amended Complaint, the lack of evidentiary support, and the applicable case law, Plaintiffs' claims against Canadian National Railway must be dismissed for lack of personal jurisdiction.

II. Plaintiffs Failed to State a Valid Corporate Veil Piercing Claim, and Therefore the Trial Court Erred in Failing to Dismiss the Plaintiffs' Claims Against Canadian National Railway and in Allowing Them to Conduct Additional Discovery

The Plaintiffs' claims should also have been dismissed under Miss. R. Civ. P. 12(b)(6) for failure to state. In its Order on Canadian National Railway's motion to dismiss, the trial court found that Plaintiffs had not presented sufficient **evidence** to pierce the corporate veil but "held that they had "presented sufficient **allegations** to justify limited further discovery into the 'alter ego' or 'mere instrumentality' issue." [R at 187 – Excerpt No. 2 (emphasis added)] Plaintiffs alleged in their complaint merely that Illinois Central was the "alter ego" and a "mere instrumentality" of Canadian National Railway. They did not allege any facts to support this bare legal conclusion much less facts establishing the elements of their corporate veil piercing claim. The Mississippi Supreme Court in *Ratliff* clearly held that a plaintiff is required "to allege all of the material elements necessary to justify disregarding the corporate form." 954 So. 2d at 432. The Court explained that "failure to allege [the] subsidiary was a vehicle for fraud justifies dismissal for failure to state a claim." *Id.* It further held that "conclusory allegations of domination and control . . . are insufficient to withstand [a] motion to dismiss." *Id.* at 433 (citing *RMS Techs. v. Nynex Computer Servs. Co.*, 1993 WL 763469 (N.Y. Misc.1993)). The trial court ignored Plaintiffs' total failure to comply with these strict requirements when it failed to grant Canadian National Railway's motion to dismiss.

The trial court also failed to follow *Buchanan,* in which the Mississippi Supreme Court held that ownership of all corporate stock, commonality of officers and directors, financing by the parent corporation, and the filing of consolidated financial statements and tax returns, even in combination, were insufficient to justify piercing the corporate veil. *Buchanan,* 957 So. 2d at 978-980. These are the very issues on which Plaintiffs seek discovery from Canadian National Railway. In other words, even if Plaintiffs were allowed to conduct the discovery they request, and actually obtained the information they seek, such evidence would not be sufficient to justify the extreme measure of veil piercing. Allowing such discovery therefore would not be just and would simply serve to delay the inevitable dismissal of Plaintiffs' claims.

Plaintiffs have not shown what facts discovery will reveal to establish fraud or similar misfeasance on the part of Canadian National Railway, which is what they would have to show in order to justify piercing the corporate veil. As the Ninth Circuit held in rejecting a similar argument, periods of slow business are "perhaps the most common risk in the business world," and evidence of such periods does not amount to evidence of fraud. *Seymour,* at 1112-13. *See also Wurtz,* 2007 WL 1593221, at *6 (rejecting argument that evidence of corporation's inability to pay some of its creditors was sufficient to show undercapitalization for purposes of corporate veil-piercing). Indeed, "the doctrine of limited liability is intended precisely to protect a parent corporation whose subsidiary goes broke."[6] *Radaszewski v. Telecom Corp.,* 981 F.2d 305, 311 (8th Cir. 1992). Plaintiffs did not allege in their Amended Complaint, nor even attempt to argue

[6] That is not to say that Illinois Central is broke. It is not.

in their Response, that Illinois Central's negative net worth in 2008 was the result of any misconduct by Canadian National Railway. Absent particularized allegations of such misconduct or other evidence of fraud, Plaintiffs negative net worth evidence is of no moment.

In short, the trial court's order preliminarily pierces the corporate veil of a foreign corporation based on the mere unsubstantiated, conclusory allegations of the complaint. Without ever finding that it had personal jurisdiction or that Plaintiffs stated a cognizable claim against Canadian National Railway, the trial judge allowed the Plaintiffs to proceed with discovery on the merits of their corporate veil piercing claim. Significantly, the Court did so even after holding that the discovery the Plaintiffs are seeking (i.e. discovery that they believe will establish a finding of undercapitalization) would not be sufficient to justify ignoring the corporate separateness. For these reasons, this Court should vacate the order of the Circuit Court and order that Plaintiffs' claims against Canadian National Railway be dismissed pursuant to Rule 12(b)(6).

CONCLUSION

The Plaintiffs failed to establish personal jurisdiction over Canadian National Railway and failed to allege a claim upon which relief can be granted against Canadian National Railway. Other than conclusory allegations of the same type rejected by this Court in *Ratliff*, Plaintiffs only argument is that the procedural protections of in personam jurisdiction should be disregarded because Illinois Central in 2008 had a negative net worth. They cite no case law for this proposition and indeed none exists. Under these facts, the exercise of personal jurisdiction would not comport with traditional notions of fair play and substantial justice. Accordingly, Plaintiffs' claims against Canadian National Railway should be dismissed.

Respectfully submitted,

CANADIAN NATIONAL RAILWAY COMPANY

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CERTIFICATE OF SERVICE

I, James E. Graves, III, do hereby certify that I have this date sent via United States mail, postage prepaid, a true and correct copy of the foregoing to the following:

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This the 18th day of November, 2011.

James Graves, III
JAMES E. GRAVES, III

Accounting Research
BULLETINS

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Issued by the
Committee on Accounting Procedure
American Institute of
Certified Public Accountants
270 Madison Avenue, New York 16, N. Y.

August, 1959 No. 51

Consolidated Financial Statements

Purpose of Consolidated Statements

1. The purpose of consolidated statements is to present, primarily for the benefit of the shareholders and creditors of the parent company, the results of operations and the financial position of a parent company and its subsidiaries essentially as if the group were a single company with one or more branches or divisions. There is a presumption that consolidated statements are more meaningful than separate statements and that they are usually necessary for a fair presentation when one of the companies in the group directly or indirectly has a controlling financial interest in the other companies.

Consolidation Policy

2. The usual condition for a controlling financial interest is ownership of a majority voting interest, and, therefore, as a general rule ownership by one company, directly or indirectly, of over fifty per cent of the outstanding voting shares of another company is a condition pointing toward consolidation. However, there are exceptions to this general rule. For example, a subsidiary should not be consolidated where control is likely to be temporary, or where it does not rest with the majority owners (as, for instance, where the subsidiary is in legal reorganization or in bankruptcy). There may also be situations where the minority interest in the subsidiary is so large, in relation to the equity of the shareholders of the parent in the consolidated net assets, that the presentation of separate financial statements for the two companies would be more meaningful and useful. However, the fact that

the subsidiary has a relatively large indebtedness to bondholders or others is not in itself a valid argument for exclusion of the subsidiary from consolidation. (Also, see Chapter 12 of Accounting Research Bulletin No. 43 for the treatment of foreign subsidiaries.)

3. In deciding upon consolidation policy, the aim should be to make the financial presentation which is most meaningful in the circumstances. The reader should be given information which is suitable to his needs, but he should not be burdened with unnecessary detail. Thus, even though a group of companies is heterogeneous in character, it may be better to make a full consolidation than to present a large number of separate statements. On the other hand, separate statements or combined statements would be preferable for a subsidiary or group of subsidiaries if the presentation of financial information concerning the particular activities of such subsidiaries would be more informative to shareholders and creditors of the parent company than would the inclusion of such subsidiaries in the consolidation. For example, separate statements may be required for a subsidiary which is a bank or an insurance company and may be preferable for a finance company where the parent and the other subsidiaries are engaged in manufacturing operations.

4. A difference in fiscal periods of a parent and a subsidiary does not of itself justify the exclusion of the subsidiary from consolidation. It ordinarily is feasible for the subsidiary to prepare, for consolidation purposes, statements for a period which corresponds with or closely approaches the fiscal period of the parent. However, where the difference is not more than about three months, it usually is acceptable to use, for consolidation purposes, the subsidiary's statements for its fiscal period; when this is done, recognition should be given by disclosure or otherwise to the effect of intervening events which materially affect the financial position or results of operations.

5. Consolidated statements should disclose the consolidation policy which is being followed. In most cases this can be made apparent by the headings or other information in the statements, but in other cases a footnote is required.

Consolidation Procedure Generally

6. In the preparation of consolidated statements, intercompany balances and transactions should be eliminated. This includes inter-

company open account balances, security holdings, sales and purchases, interest, dividends, etc. As consolidated statements are based on the assumption that they represent the financial position and operating results of a single business enterprise, such statements should not include gain or loss on transactions among the companies in the group. Accordingly, any intercompany profit or loss on assets remaining within the group should be eliminated; the concept usually applied for this purpose is gross profit or loss. (See also paragraph 17.) However, in a regulated industry where a parent or subsidiary manufactures or constructs facilities for other companies in the consolidated group, the foregoing is not intended to require the elimination of intercompany profit to the extent that such profit is substantially equivalent to a reasonable return on investment ordinarily capitalized in accordance with the established practice of the industry.

Elimination of Intercompany Investments

7. Where the cost to the parent of the investment in a purchased[1] subsidiary exceeds the parent's equity in the subsidiary's net assets at the date of acquisition, as shown by the books of the subsidiary, the excess should be dealt with in the consolidated balance sheet according to its nature. In determining the difference, provision should be made for specific costs or losses which are expected to be incurred in the integration of the operations of the subsidiary with those of the parent, or otherwise as a result of the acquisition, if the amount thereof can be reasonably determined. To the extent that the difference is considered to be attributable to tangible assets and specific intangible assets, such as patents, it should be allocated to them. Any difference which cannot be so applied should be shown among the assets in the consolidated balance sheet under one or more appropriately descriptive captions. When the difference is allocated to depreciable or amortizable assets, depreciation and amortization policies should be such as to absorb the excess over the remaining life of related assets. For subsequent treatment of intangibles, see Chapter 5 of Accounting Research Bulletin No. 43.

8. In general, parallel procedures should be followed in the reverse type of case. Where the cost to the parent is less than its equity in the net assets of the purchased subsidiary, as shown by the books

[1] See Accounting Research Bulletin No. 48, *Business Combinations*, for the difference in treatment between a purchase and a pooling of interests.

of the subsidiary at the date of acquisition, the amount at which such net assets are carried in the consolidated statements should not exceed the parent's cost. Accordingly, to the extent that the difference, determined as indicated in paragraph 7, is considered to be attributable to specific assets, it should be allocated to them, with corresponding adjustments of the depreciation or amortization. In unusual circumstances there may be a remaining difference which it would be acceptable to show in a credit account, which ordinarily would be taken into income in future periods on a reasonable and systematic basis. A procedure sometimes followed in the past was to credit capital surplus with the amount of the excess; such a procedure is not now considered acceptable.

9. The earned surplus or deficit of a purchased[1] subsidiary at the date of acquisition by the parent should not be included in consolidated earned surplus.

10. When one company purchases two or more blocks of stock of another company at various dates and eventually obtains control of the other company, the date of acquisition (for the purpose of preparing consolidated statements) depends on the circumstances. If two or more purchases are made over a period of time, the earned surplus of the subsidiary at acquisition should generally be determined on a step-by-step basis; however, if small purchases are made over a period of time and then a purchase is made which results in control, the date of the latest purchase, as a matter of convenience, may be considered as the date of acquisition. Thus there would generally be included in consolidated income for the year in which control is obtained the postacquisition income for that year, and in consolidated earned surplus the postacquisition income of prior years, attributable to each block previously acquired. For example, if a 45% interest was acquired on October 1, 1957 and a further 30% interest was acquired on April 1, 1958, it would be appropriate to include in consolidated income for the year ended December 31, 1958, 45% of the earnings of the subsidiary for the three months ended March 31, and 75% of the earnings for the nine months ended December 31, and to credit consolidated earned surplus in 1958 with 45% of the undistributed earnings of the subsidiary for the three months ended December 31, 1957.

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[1] See Accounting Research Bulletin No. 48, *Business Combinations,* for the difference in treatment between a purchase and a pooling of interests.

11. When a subsidiary is purchased during the year, there are alternative ways of dealing with the results of its operations in the consolidated income statement. One method, which usually is preferable, especially where there are several dates of acquisition of blocks of shares, is to include the subsidiary in the consolidation as though it had been acquired at the beginning of the year, and to deduct at the bottom of the consolidated income statement the preacquisition earnings applicable to each block of stock. This method presents results which are more indicative of the current status of the group, and facilitates future comparison with subsequent years. Another method of prorating income is to include in the consolidated statement only the subsidiary's revenue and expenses subsequent to the date of acquisition.

12. Where the investment in a subsidiary is disposed of during the year, it may be preferable to omit the details of operations of the subsidiary from the consolidated income statement, and to show the equity of the parent in the earnings of the subsidiary prior to disposal as a separate item in the statement.

13. Shares of the parent held by a subsidiary should not be treated as outstanding stock in the consolidated balance sheet.

Minority Interests

14. The amount of intercompany profit or loss to be eliminated in accordance with paragraph 6 is not affected by the existence of a minority interest. The complete elimination of the intercompany profit or loss is consistent with the underlying assumption that consolidated statements represent the financial position and operating results of a single business enterprise. The elimination of the intercompany profit or loss may be allocated proportionately between the majority and minority interests.

15. In the unusual case in which losses applicable to the minority interest in a subsidiary exceed the minority interest in the equity capital of the subsidiary, such excess and any further losses applicable to the minority interest should be charged against the majority interest, as there is no obligation of the minority interest to make good such losses. However, if future earnings do materialize, the majority interest should be credited to the extent of such losses previously absorbed.

Income Taxes

16. When separate income tax returns are filed, income taxes usually are incurred when earnings of subsidiaries are transferred to the parent. Where it is reasonable to assume that a part or all of the undistributed earnings of a subsidiary will be transferred to the parent in a taxable distribution, provision for related income taxes should be made on an estimated basis at the time the earnings are included in consolidated income, unless these taxes are immaterial in amount when effect is given, for example, to dividend-received deductions or foreign-tax credits. There is no need to provide for income tax to the parent company in cases where the income has been, or there is evidence that it will be, permanently invested by the subsidiaries, or where the only likely distribution would be in the form of a tax-free liquidation.

17. If income taxes have been paid on intercompany profits on assets remaining within the group, such taxes should be deferred or the intercompany profits to be eliminated in consolidation should be appropriately reduced.

Stock Dividends of Subsidiaries

18. Occasionally, subsidiary companies capitalize earned surplus arising since acquisition, by means of a stock dividend or otherwise. This does not require a transfer to capital surplus on consolidation, inasmuch as the retained earnings in the consolidated financial statements should reflect the accumulated earnings of the consolidated group not distributed to the shareholders of, or capitalized by, the parent company.

Unconsolidated Subsidiaries in Consolidated Statements

19. There are two methods of dealing with unconsolidated subsidiaries in consolidated statements. Whichever method is adopted should be used for all unconsolidated subsidiaries, subject to appropriate modification in special circumstances. The preferable method, in the view of the committee, is to adjust the investment through income currently to take up the share of the controlling company or companies in the subsidiaries' net income or net loss,

except where the subsidiary was excluded because of exchange restrictions or other reasons which raise the question of whether the increase in equity has accrued to the credit of the group. (Adjustments of the investment would also be made for "special" debits or credits shown on the income statements of the unconsolidated subsidiaries below the net income for the period, and for similar items shown in the schedule of earned surplus.) The other method, more commonly used at present, is to carry the investment at cost, and to take up income as dividends are received; however, provision should be made for any material impairment of the investment, such as through losses sustained by the subsidiaries, unless it is deemed to be temporary. When the latter method is followed, the consolidated statements should disclose, by footnote or otherwise, the cost of the investment in the unconsolidated subsidiaries, the equity of the consolidated group of companies in their net assets, the dividends received from them in the current period, and the equity of the consolidated group in their earnings for the period; this information may be given in total or by individual subsidiaries or groups of subsidiaries.

20. Whichever method of dealing with unconsolidated subsidiaries is followed, if there is a difference between the cost of the investment and the equity in net assets at the date of acquisition, appropriate recognition should be given to the possibility that, had the subsidiaries been consolidated, part of such difference would have been reflected in adjusted depreciation or amortization. Also, appropriate recognition should be given to the necessity for an adjustment for intercompany gains or losses on transactions with unconsolidated subsidiaries. If sales are made to unconsolidated subsidiaries and the investment in the subsidiaries is carried at cost plus the equity in undistributed earnings, an elimination of unrealized intercompany gains and losses should be made to the same extent as if the subsidiaries were consolidated. The same applies where intercompany sales are made by the unconsolidated subsidiaries. If, however, the investment is carried at cost, it is not necessary to eliminate the intercompany gain on sales to such subsidiaries, if the gain on the sales does not exceed the unrecorded equity in undistributed earnings of the unconsolidated subsidiaries. If such gain is material, it should be appropriately disclosed. Where the sales are made by the unconsolidated subsidiaries to companies included in the consolidated group, the intercompany gains or losses should be eliminated in arriving at the amount of the equity in the undistributed earnings of the un-

consolidated subsidiaries which will be disclosed in a footnote or otherwise. (See paragraph 19.)

21. Where the unconsolidated subsidiaries are, in the aggregate, material in relation to the consolidated financial position or operating results, summarized information as to their assets, liabilities and operating results should be given in the footnotes or separate statements should be presented for such subsidiaries, either individually or in groups, as appropriate.

Combined Statements

22. To justify the preparation of consolidated statements, the controlling financial interest should rest directly or indirectly in one of the companies included in the consolidation. There are circumstances, however, where combined financial statements (as distinguished from consolidated statements) of commonly controlled companies are likely to be more meaningful than their separate statements. For example, combined financial statements would be useful where one individual owns a controlling interest in several corporations which are related in their operations. Combined statements would also be used to present the financial position and the results of operations of a group of unconsolidated subsidiaries. They might also be used to combine the financial statements of companies under common management.

23. Where combined statements are prepared for a group of related companies, such as a group of unconsolidated subsidiaries or a group of commonly controlled companies, intercompany transactions and profits or losses should be eliminated, and if there are problems in connection with such matters as minority interests, foreign operations, different fiscal periods, or income taxes, they should be treated in the same manner as in consolidated statements.

Parent-Company Statements

24. In some cases parent-company statements may be needed, in addition to consolidated statements, to indicate adequately the position of bondholders and other creditors or preferred stockholders of the parent. Consolidating statements, in which one column is used for the parent company and other columns for particular subsidiaries

or groups of subsidiaries, often are an effective means of presenting the pertinent information.

The statement entitled "Consolidated Financial Statements" was unanimously adopted by the twenty-one members of the committee, of whom nine, Messrs. Bedford, Dunn, Graese, Graham, Halvorson, Hoyler, Kent, Powell, and Werntz, assented with qualification.

Mr. Bedford objects to the provision in paragraph 2 that ownership of over fifty per cent of the outstanding voting stock is the general rule governing consolidation policy. He believes the over fifty per cent ownership requirement is at best only one of several criteria evidencing the existence of a consolidated entity.

Messrs. Graese and Hoyler do not agree with the statement made in the last sentence of paragraph 8. Mr. Graese believes there are cases in which the crediting of a capital surplus account with the "excess credit" will result in a more appropriate presentation of consolidated operations and financial position, particularly in (but not limited to) situations where the acquisition of control of the subsidiary has been accomplished over an extended period of time or where there are acquisitions of minority interest at a date considerably after obtaining control. Mr. Hoyler is of the opinion that there have been, and probably will be, circumstances under which credits to capital surplus of the excesses referred to in this paragraph will be appropriate.

Messrs. Halvorson and Werntz object to the relative emphasis given to the recommendations in paragraph 10, which they believe should be reversed. They believe that the date of the purchase which results in control should generally be considered to be the date of acquisition; however, if a limited number of purchases are made over a period of time pursuant to a plan or program which culminates in control, they agree that the earned surplus of the subsidiary at acquisition may be determined on a step-by-step basis.

Mr. Halvorson disagrees with the recommendation in paragraph 18. In his view, the usual subsidiary is a closely held corporation, and consequently is under no pressure to declare stock dividends and is under no compulsion to follow the "fair value" method of accounting for them if it does. If it does capitalize earned surplus by means of a stock dividend or otherwise, particularly "otherwise," he feels that it must have been done with a purpose relating to its financial position, at the direction of, and with the acquiescence of, the parent company, and that the capitalization should carry through into the consolidated surplus accounts. If the subsidiary is one in which there is a publicly held minority interest, and a stock dividend is issued and accounted for on a fair-value basis in the manner of an independent publicly owned corporation, the accounting for earned surplus in respect of the majority interest would be the same as that for the minority interest, and again he believes that the capitalization should follow through into the consolidated surplus accounts. Mr. Powell also disagrees with the conclusion expressed in this paragraph. He believes that if a parent causes a subsidiary to freeze a part or all of its earned surplus through the payment of a stock dividend or otherwise, thus making such surplus unavailable for ordinary dividends, it should follow a similar procedure on consolidation.

Mr. Kent believes the consolidation policy section is deficient since it fails to restrict the increasing practice of not including certain subsidiaries in consolidated financial statements. He suggests that the bulletin may possibly result in further increasing such practice as a consequence of the preference expressed in paragraph 19 for the inclusion of the equity in earnings of unconsolidated subsidiaries in consolidated statements. It is his belief that in the usual situation a full consolidation policy as implied in paragraph 1 is generally preferable, supplemented by such summarized financial information, in footnotes or otherwise, as may be appropriate.

Messrs. Dunn and Graham believe that the "preferable" method in paragraph 19 should be recognized as the only acceptable method of dealing with unconsolidated subsidiaries in consolidated statements, and that the method which carries the investment in unconsolidated subsidiaries at cost, and takes up as income only the dividends received, should be discontinued as rapidly as is practicable. They feel that the "preferable" method conforms to the purpose of consolidated statements as set forth in paragraph 1 — to present the results of operations and the financial position essentially as if the group were a single company, and that its uniform adoption would increase the comparability of the financial statements of different companies, and would avoid the possibility of manipulation of reported consolidated earnings through the control of dividends received by the parent.

Mr. Dunn believes that paragraph 20 should require the elimination of intercompany gain on sales to unconsolidated subsidiaries if the failure to do so would have a material effect on the reported consolidated income, regardless of whether the gain on intercompany sales exceeds the unrecorded equity in undistributed earnings of the unconsolidated subsidiaries.

NOTES

(See Introduction to *Accounting Research Bulletin No. 43.*)

1. Accounting Research Bulletins represent the considered opinion of at least two-thirds of the members of the committee on accounting procedure, reached on a formal vote after examination of the subject matter by the committee, the technical services department, and the director of research. Except in cases in which formal adoption by the Institute membership has been asked and secured, the authority of the bulletins rests upon the general acceptability of opinions so reached.

2. Opinions of the committee are not intended to be retroactive unless they contain a statement of such intention. They should not be considered applicable to the accounting for transactions arising prior to the publication of the opinions. However, the committee does not wish to discourage the revision of past accounts in an individual case if the accountant thinks it desirable in the circumstances. Opinions of the committee should be considered as applicable only to items which are material and significant in the relative circumstances.

3. It is recognized also that any general rules may be subject to exception; it is felt, however, that the burden of justifying departure from accepted procedures must be assumed by those who adopt other treatment. Except where there is a specific statement of a different intent by the committee, its opinions and recommendations are directed primarily to business enterprises organized for profit.

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SERVICE DATE - NOVEMBER 7, 2001

SURFACE TRANSPORTATION BOARD

DECISION

STB Ex Parte No. 634

PROPOSAL TO REQUIRE CONSOLIDATED REPORTING
BY COMMONLY CONTROLLED RAILROADS

STB EX PARTE NO. 584

WISCONSIN CENTRAL LTD.—PETITION FOR RULEMAKING—
CLASSIFICATION OF CARRIERS

Decided: October 31, 2001

Our accounting and reporting regulations require financial reports to be filed by Class I railroads, that is, railroads with annual operating revenues of at least $250 million (in 1991 dollars).[1] Currently, our regulations do not require commonly owned carriers to report on a consolidated basis. Thus, families of railroads that are operated as an integrated system with cumulative operating revenues well above the $250 million threshold are not required to file financial reports so long as the operating revenues of each individual railroad are less than $250 million.

On September 25, 2000, we proposed, in STB Ex Parte No. 634,[2] that commonly controlled railroads (and their railroad-related affiliates) whose combined annual operating revenues meet the $250 million threshold be required to file consolidated financial reports. Our principal objective was to gather more meaningful and accurate information on the large rail systems operating in the United States by conforming our regulatory reporting requirements as closely as practical to Financial Accounting Standards Board Statement No. 94, Consolidation of All Majority-Owned Subsidiaries (FASB No. 94). On November 15, 2000, partially in response to this proposal, Wisconsin Central Transportation Corporation (WCTC), the parent company of a railroad that was then approaching Class I carrier status,[3] requested (in a petition docketed as

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[1] Class II carriers are those with annual operating revenues (in 1991 dollars) greater than $20 million but less than $250 million, while Class III carriers have annual operating revenues not exceeding $20 million. See 49 CFR Part 1201, General Instruction 1-1.

[2] 65 Fed. Reg. 57650 (2000).

[3] Under our rules, a railroad attains Class I status only after satisfying the revenue requirement for 3 consecutive years. 49 CFR Part 1201, General Instruction 1-1(b)(1). At the
(continued...)

STB Ex Parte No. 584) that we also consider increasing the revenue threshold for Class I status to $500 million.[4]

We now conclude that consolidated reports should be required for each group of railroads (or railroad-related affiliates) that operate as a single, integrated United States rail system whose cumulative operating revenues meet the Class I threshold. We deny the request to institute a rulemaking to consider raising the revenue threshold for Class I railroads.

A. Consolidated Reporting

Comments. In response to our proposal to require consolidated reporting for Class I rail systems, comments were filed by over 20 short line and regional railroad holding companies,[5] the American Short Line and Regional Railroad Association, the Canadian Pacific Railway Company (CP), and the Canadian National Railway Company (CN).[6] Three railroad labor representatives,[7] the Western Coal Traffic League (WCTL), and the United States Department of Agriculture (USDA) also filed comments.

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[3](...continued)
time this rulemaking was instituted, Wisconsin Central Ltd., a subsidiary of WCTC, had satisfied the revenue requirement for the prior year.

[4] For administrative convenience, we address the issues presented in both of these proceedings in this decision. These proceedings have not been consolidated, however.

[5] Genesee & Wyoming, Inc.; Emons Transportation Group; Pinsly Railroad Company; RailAmerica, Inc.; Rail Management Corporation; Transtar, Inc.; Omnitrax, Inc.; StatesRail; Bethlehem Steel Corporation Subsidiary Railroads; and Wisconsin Central Transportation Corporation. Joint comments were filed by Red River Valley & Western Company; Rutland Line, Inc.; Twin Cities & Western Railroad Company; The Monongahela Connecting Railroad Company; Aliquippa & Southern Railroad Company; The Mahoning Valley Railway Company; The Cuyahoga Valley Railway Company; The River Terminal Railway Company; Chicago Shortline Railway Company; ParkSierra Rail Corporation; Montana Rail Link; and I&M Rail Link.

[6] CP is the parent of the Class I railroad the Canadian Pacific Railway (U.S. West) Ltd. (formerly the Soo Line Railroad Company). CN is the parent of two Class I railroads, the Illinois Central Railroad Company and the Grand Trunk Western Railroad Company.

[7] The United Transportation Union; John Fitzgerald for the UTU General Committee of Adjustment GO-386 (UTU/GO-386); and the Rail Labor Division of the Transportation Trades Department, AFL-CIO (AFL-CIO).

The short line and regional railroad industry, along with USDA, expressed concern that the viability of small rail operations could be adversely affected if the proposal is used as a means to group together, for classification purposes, all commonly controlled carriers without regard to operational and marketing integration. They point out that Class III carriers are not subject to certain potentially costly labor protection provisions (see 49 U.S.C. 10902); that Class III carriers can lease older "grandfathered" boxcars at reduced rates; and that rail industry agreements provide special incentives to Class III carriers. If Class III carriers that are members of larger corporate families (even those that have no physical or marketing connection) were reclassified as Class II, they would no longer be able to take advantage of these special provisions or benefits, which the small carriers say were established precisely so that small railroads will be able to survive to provide continued rail service over lines that might otherwise be abandoned.

Arguing that combined financial results would more accurately reflect carrier classification, the three rail labor organizations and WCTL favor consolidated reporting for all commonly controlled carriers, regardless of how the carriers operate or market their services. UTU/GO-386 would expand the proposed new reporting requirements so that all railroads, regardless of size, would have to file financial reports with the Board, while AFL-CIO suggests that railroads also be required to report data on rail operations outside of the United States.

While neither CP nor CN opposes consolidated reporting, CP urges that a consolidated reporting requirement be limited to commonly controlled railroads that operate as a single integrated rail system.[8] CN suggests that we retain our current practice that carriers with non-domestic operations need to report data only on their United States rail operations.

Discussion. Although grouping together families of carriers could conceivably change the classification status of Class II or III carriers, the main purpose of the consolidated reporting proposal was to gather better data, for use in our oversight of the rail industry, on the operations of rail systems that are Class I in size. We did not intend to reimpose recordkeeping or reporting requirements on non-Class I railroads[9] that do not function as a larger system, or otherwise to change the classification status of individual carriers simply because they have corporate relationships with other carriers. As our predecessor, the Interstate Commerce Commission explained, "common control should not be the sole criterion for consolidation [for reporting purposes]. It is also important to consider the nature and the extent of the operating and

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[8] We note that the majority of the Class I carriers already voluntarily file consolidated reports for their systems.

[9] See Elimination of Accounting & Reporting Requirements of Class II Railroads, No. 37614 (ICC served Feb. 25, 1982) (relieving Class II railroads from the accounting and reporting requirements); Reduction of Accounting & Reporting Requirements, No. 37523 (ICC served Dec. 15, 1980) (relieving Class III railroads from the accounting and reporting requirements). UTU/GO386 has not adequately supported its request that we effectively reverse these actions relaxing the burdensome reporting previously required of smaller carriers.

management relationship between the commonly controlled . . . railroads." Standards for Railroad Revenue Adequacy, 3 I.C.C.2d 261, 301-302 (1986). Nothing on this record persuades us to alter that approach. Thus, we believe that consolidated reporting makes sense except where the commonly controlled railroads or related affiliates do not operate as a single integrated rail system in the United States. Indeed, even WCTL—which advocates consolidated reporting "even when individual railroads (or railroad-related affiliates) have no connection with one another except for a common parent" (WCTL comments at 2-3) —recognizes that consolidating reports of non-integrated carriers would be of limited value and suggests that carriers also maintain information on an unconsolidated basis.

When a group of commonly controlled railroads is operated as a single integrated system, that system should be recognized and treated as such for classification purposes. It is not practical, however, for us to attempt to determine, in the abstract, how particular families of small carriers are operated and which, if any, might be sufficiently integrated to require that they be classified as a single entity. Moreover, this proceeding is not the place to examine classifications for individual carriers or groups of carriers. Rather, carriers are expected to notify us when their classification status has changed, see 49 CFR 1241.15—whether the change results from this new consolidation requirement or from growth in operating revenues. If any party believes that a carrier has not done so, or that a carrier is incorrectly classified, it may bring a proceeding before us. We will be in a position to address specific carrier classification issues only on a case-by-case basis where a record has been developed with information on how the related carriers operate.[10]

Finally, we will not require carriers to report on their non-United States operations. FASB No. 94 generally requires consolidated reporting for all commonly controlled companies to ensure that the financial reports provide investors (whose principal interest is in the financial results of the combined companies) and general users of the reports a complete picture of the overall operations of the parent corporation. In contrast, we seek information primarily to assist us in the regulation of the matters within our jurisdiction, which is rail transportation in the United States. As CN points out, Canadian rail operations are "governed by different regulatory and labor regimes," which can affect the cost structure and earnings of the carriers. So as not to distort the results of those United States rail operations that we regulate, we will continue to require reporting only on rail operations within the United States.

Conclusion. We conclude that Class I rail systems should file consolidated reports that combine the operations of all their commonly controlled railroads or railroad-related affiliates functioning as an integrated rail system within the United States. The reporting requirement will take effect for the reporting year beginning January 1, 2002. To effectuate this new requirement, 49 CFR Part 1201, General Instruction 1-1 (b)(1) will be amended to read as follows:

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[10] In determining what operations to include in a consolidated report, we will presume that all commonly controlled, interconnected rail lines in the United States form an integrated rail system for reporting purposes. However, carriers are free to explain why in individual circumstances this presumption should not be applied.

(b)(1) The class to which any carrier belongs shall be determined by annual carrier operating revenues after the railroad revenue deflator adjustment. Families of railroads operating within the United States as a single, integrated rail system will be treated as a single carrier for classification purposes. Upward and downward reclassification will be effected as of January 1 in the year immediately following the third consecutive year of revenue qualification.

B. Revenue Threshold

Prior to its acquisition by CN,[11] WCTC requested that we consider raising the Class I revenue threshold to $500 million. However, now that WCTC has been integrated into CN's United States operations, increasing the Class I revenue threshold to $500 million would have no impact on its reporting obligations,[12] as WCTC's rail operations are interconnected with CN's other United States rail operations and should be included in CN's consolidated reports under our ruling in Ex Parte No. 634. In any event, because railroads with operating revenues of more than $250 million are clearly large entities for which financial reporting is reasonable and not unduly burdensome, we decline to institute a rulemaking to consider increasing the Class I revenue threshold.

We certify that this action will not have a substantial adverse impact upon a significant number of small entities. We are not here reclassifying any railroads, and the consolidated reporting that we are requiring applies only to large railroads.

This action will not significantly affect either the quality of the human environment or the conservation of energy resources.

It is ordered:

(1) The Board will require consolidated reporting for all Class I carriers for the reporting year beginning January 1, 2002.

(2) The request to institute a rulemaking in Ex Parte No. 584 is denied.

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[11] See Canadian National Railway Co., Grand Trunk Corp., and WC Merger Sub, Inc.—Control—Wisconsin Central Transportation Corp., Wisconsin Central Ltd., Fox Valley & Western, Ltd., Sault Ste. Marie Bridge Co., and Wisconsin Chicago Link Ltd., STB Finance Docket 34000, Decision No. 10 (STB served Sept. 7, 2001) (approving acquisition of WCTC by CN).

[12] Likewise, Kansas City Southern Railway Company (KCS), which supported the request that we revisit the Class I threshold, would not be affected by WCTC's proposal as KCS' annual operating revenues already exceed $500 million.

(3) This decision will be effective December 30, 2001.

By the Board, Chairman Morgan, Vice Chairman Clyburn and Commissioner Burkes.

Vernon A. Williams
Secretary