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Public Record

Honorable Vernon A. Williams, Secretary
Surface Transportation Board
1925 K Street, N.W.
Washington, DC 20423-0001

Re: Surface Transportation Board Docket No. AB-290 (Sub-No. 259X),
Tennessee Railway Company - Abandonment Exemption - In Anderson
and Campbell Counties, TN - Reply to Notice of Intent to File Offer of
Financial Assistance; Reply to Information Request and Request for
Extension of Time

Dear Mr. Williams:

In a January 28, 2005 letter to the Board, National Coal Corporation ("National Coal") submitted a Notice of Intent to Offer Financial Assistance ("OFA") to Tennessee Railway Company ("TNR"), a wholly owned subsidiary of Norfolk Southern Railway Company ("NSR"), apparently for the acquisition of an approximately 14.04-mile railroad line between Milepost TE-27.96 at Nicks Creek, TN and milepost TE-42.00 at Devonia, TN (the "Line") that is the subject of the notice of exemption for abandonment in this proceeding. In a January 31, 2005 letter to the Board, National Coal requested that NSR, as parent company of TNR, provide National Coal with information related to National Coal's proposed OFA. National Coal further requested that the Board toll the February 18, 2005 due date for its OFA for the Line because it is unlikely that NSR (TNR) will be able to provide National Coal with the requested data by that date.

The Board's regulations governing OFAs at 49 CFR 1152.27(c)(2)(i) provide that an expression or notice of intent to file an OFA with respect to a line for which a railroad has filed a class exemption notice of abandonment must indicate the type of financial assistance the offeror wishes to provide (i.e., subsidy or purchase). National Coal's notice of intent does not clearly express the type of financial assistance that National Coal contemplates offering. We read the two National Coal letters together to indicate that National Coal contemplates an offer to acquire the Line. Since line subsidies are

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limited to one year in the absence of further agreement, the subject Line is out-of-service, the Line is in need of substantial and costly repair to return to service, and National Coal's desire to have the Line available for shipments of coal is based on a plan to resume operation of now inoperative facilities at Devonia, TN this year or in 2006, there is no operation on the Line to subsidize nor will there be any need for such operation for some time, if ever. These facts further support TNR's interpretation of the type of OFA National Coal proposes to submit.

Assuming that the Board accepts National Coal's expression of intent and request for information, which we suggest below the Board should reject, in accordance with the Board's regulation at 49 CFR 1152.27(c)(2)(ii) (D), TNR hereby advises the Board and National Coal that TNR needs additional time to develop the information that TNR is required to produce under the Board regulations upon request of a potential offeror of financial assistance for a rail line that is subject to abandonment. Among other things, National Coal's request will require TNR to obtain an independent appraisal of the land value for the right-of-way of the subject 14.04-mile out-of-service railroad line in order to determine the Line's net liquidation value. Such appraisals commonly take at least 45 to 60 days to obtain and prepare for submission. Therefore, TNR requests that if the Board accepts the Notice of Intent and information request, the Board permit TNR 60 days to provide the requested information to the extent such information is required in this proceeding.

TNR notes that National Coal Corporation's publicly released earnings information shows that the two-year old company operated at a loss in 2003 and 2004. (See e.g., page F-22 of the financial information submitted by National Coal to the Board with its Notice of Intent.) This alone may or may not disprove National Coal's assertion that it is financially capable of consummating acquisition of the subject railroad line and operating it for at least two years. However, we think that these financial results, along with the debt National Coal has assumed to complete the acquisition of new mines and assets and the commencement of new operations, and National Coal's overall financial condition, show that National Coal can not now bear the additional costs of acquisition, rehabilitation and operation of the subject Line.

On page 30 of the financial statement submitted to the Board with its Notice of Intent, National Coal acknowledges that most of the company's coal production is currently sold on the spot market or under short-term contracts and that the price of coal is volatile. Additionally, National Coal stated: "We do not generate sufficient cash from operations to fund new mine development, and our expansion into new mines therefore depends on our ability to raise the required funds through debt or equity offering." But on page 22 of the statement, National Coal describes its senior secured credit facility. National Coal has borrowed \$16.4 million of the \$21 million available

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under that arrangement at an interest rate of prime rate plus 5.75%. This debt is secured by a lien on all of National Coal's property. On page 23, National Coal admits: "At December 21, 2004, we were not in compliance with our financial covenants related to EBITDA or our minimum monthly sales requirements under the Credit Agreement, and are seeking a waiver from the lender." Moreover, TNR soon will file a petition for exemption to abandon the approximately 27.01-mile Oneida-Nicks Creek line that connects with the subject Line. National Coal will need to be able to acquire this additional line in order to keep the subject Line connected to the national rail system.

On the basis of the information provided by National Coal itself, TNR believes the Board should reject National Coal's Notice of Intent and information request. National Coal's own financial information discloses that National Coal could not fund the acquisition and operation of a line of railroad of the length and condition of the subject Line, much less the subject Line plus the Oneida-Nicks Creek line.

TNR believes that it should not be required to produce information on the repair and rehabilitation of the subject Line. This information was not required for the filing of the notice of exemption. It is not relevant to the calculation of the net liquidation value of the Line for the purpose of determining the price for its acquisition. The proposed OFA, if it is submitted and accepted, apparently will not be for the purpose of subsidizing continued operation of the Line, as explained above. Nonetheless, TNR has recently calculated that the cost of repairing the Line in order to put it back in service under the Board's conservative assumptions for the calculation of rehabilitation costs would be \$2,110,251. We will provide further details if the Board requires them, but again, we suggest that they should not be required in this proceeding.

TNR does not concur with all of the assertions in National Coal Corporation's January 28, 2005 letter to the Board. However, we will focus in this letter only on one erroneous statement of particular concern and one clarification.

Despite serious negotiations between NSR, on behalf of TNR, and U. S. Coal, Inc., before National Coal bought the U. S. Coal properties near TNR's railroad line, NSR (TNR) and U. S. Coal, Inc. did not reach a final agreement on U. S. Coal's acquisition of all or part of TNR's railroad line between approximately Milepost TE-0.0 (or MP TE-0.95) near Oneida, TN and Milepost TE-42.0 near Devonia, TN. National Coal is well aware that NSR and U.S. Coal could not reach an agreement on all of the necessary terms. In addition, NSR has advised National Coal that the purchase price discussed between NSR and U. S. Coal as long as five years ago was based on land and material values at the time and other terms and commercial considerations that are either obsolete or not applicable to any potential agreement between National Coal and TNR for purchase and sale of the subject Line. The former negotiations between NSR

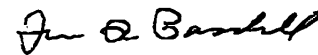
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and U.S. Coal, and the terms discussed, did not result in a contract or other final agreement. They certainly have no bearing on the current purchase price for, or the calculation of the current net liquidation value of, the Line under the Board's regulations.

National Coal asserts that on numerous occasions it contacted NSR (TNR) requesting service "on the line to at least Smoky Junction." This and other more ambiguous phrases could lead to confusion about the locations on the subject Line and about requests for service over the Line. National Coal's operation at Smoky Junction is located at approximately Milepost TE-26.25 in Scott County, TN. Thus, it is not on the segment of the Line in Anderson and Campbell Counties that is the subject of this proceeding. The subject Line segment, starting at Milepost TE-27.96, dead ends near Milepost TE-42.00 at Devonia and is not required to provide rail service to Smoky Junction, TN. National Coal acknowledges that its facility near Devonia, which was purchased from U. S. Coal in 2003, is "presently inoperative." It has been inoperative since long before National Coal purchased it. We wish to make this clarification so that other National Coal statements concerning "the Line," which apparently are meant to refer to the segment of the Line between Oneida and Smoky Junction, are not misinterpreted or taken out of context.

TNR requests that the Board reject National Coal's Notice of Intent to submit an OFA and its information request because of serious questions about National Coal's financial ability to acquire, rehabilitate and operate the Line. In the alternative, TNR requests that it be permitted 60 days to compile the information required to respond to National Coal's request for information concerning the net liquidation value of the subject Line and that TNR not be required to submit further information concerning the repair, rehabilitation or maintenance costs for the Line.

Very truly yours,



James R. Paschall

cc: via fax 865-691-9982 and mail confirmation

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