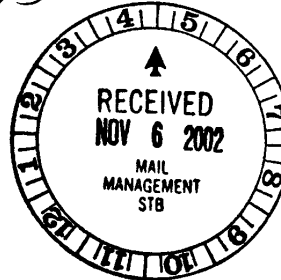


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206573



November 6, 2002

BY HAND DELIVERY

Vernon A. Williams, Secretary
Surface Transportation Board
1925 K Street, 7th Floor
Washington, DC 20423

ENTERED
Office of Proceedings
NOV 6 2002
Part of
Public Record

Re: STB Finance Docket No. 34114, Yolo Shortline Railroad Company – Lease and Operation Exemption – Port of Sacramento

Dear Mr. Williams:

Enclosed for filing in the above-referenced proceeding are an original and 10 copies of Yolo Shortline Railroad Company's Reply to Petition to Revoke Exemption.

Please acknowledge receipt of this filing by date-stamping the enclosed acknowledgment copy and returning it to our messenger.

Sincerely,

Rose-Michele Weinryb

Enclosures

cc: Joseph H. Dettmar, STB Office of Proceedings (by facsimile)
Robert T. Opal (by facsimile)

206573

**BEFORE THE
SURFACE TRANSPORTATION BOARD**



Finance Docket No. 34114

**Yolo Shortline Railroad Company –
Lease and Operation Exemption -
Port of Sacramento**

**REPLY TO PETITION TO
REVOKE EXEMPTION**

ENTERED
Office of Proceedings

NOV 6 2002

Port of
Sacramento

**YOLO SHORTLINE RAILROAD
COMPANY**

By its attorneys,

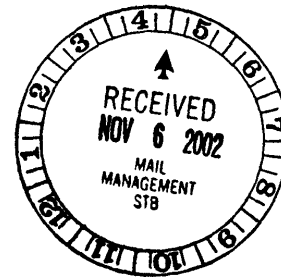
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(202) 628-2000

Dated: November 6, 2002

**BEFORE THE
SURFACE TRANSPORTATION BOARD**

Finance Docket No. 34114

**Yolo Shortline Railroad Company –
Lease and Operation Exemption -
Port of Sacramento**



**REPLY TO PETITION TO
REVOKE EXEMPTION**

On October 21, 2002, Union Pacific Railroad Company (“UP”), pursuant to 49 U.S.C. § 10502(d), filed with the Surface Transportation Board (the “Board”) a petition to revoke (“UP Petition”) the exemption obtained by Yolo Shortline Railroad Company (“YSLR”) in the above-named docket (the “YSLR Exemption”). UP based its Petition on two theories: 1) that the exemption was void *ab initio* because it contained false or misleading information or, 2) the transaction was not of the type contemplated by the class exemption procedures and, therefore, should be revoked to permit greater Board scrutiny.

The Petition is a companion filing to the notice of exemption filed by UP in Finance Docket No. 34252 (“UP Notice”), as part of its effort to prevent YSLR from terminating an agreement pursuant to which UP has provided exempt service in the Port of Sacramento (“Port”). For the reasons set forth in the Petition to Reject or Stay filed by YSLR in Finance Docket No. 34252, on October 28, 2002 (“YSLR Petition”), the Board should reject UP’s efforts to “convert” its exempt operations on track owned by the Port and leased by YSLR into regulated operations, thereby forcing YSLR to commence a discontinuance proceeding in connection with the termination of UP’s rights. The UP Petition filed in this docket appears to be no more than

an effort by UP to force YSLR to fight a two-front war. The notice of exemption filed by YSLR in this finance docket, more than one year ago, contained no false or misleading information and met all of the requirements of the Board's class exemption regulations. There is no basis whatsoever for revoking that exemption.

I. Background.

To understand the facts in this case, it is necessary to go back to the beginning of the Port of Sacramento's ("Port") operation in 1950. At that time, presumably because the Port wanted to attract customers to ship via its port facility, and in order to facilitate that, it arranged for rail service to handle traffic to and from points beyond the Port. In 1950, the Port made an agreement with the Sacramento Northern Railway ("SNR"), which gave the Port the right to terminate SNR's operations on Port track by giving a 20-day notice of termination; similarly, SNR could terminate its obligation to provide service to Port shippers by giving the same 20-day notice (the "1950 Agreement"). In February 1951, the Port entered into an agreement with the Southern Pacific Railroad ("SP") to use the Port track jointly to provide service to Port shippers (the "1951 Agreement"). Unlike the 1950 Agreement, the 1951 Agreement gave the Port the right to terminate SP's operation on its tracks by giving a one-year notice of termination and SP the right to terminate its obligation to provide service to Port shippers by giving the same one-year notice.

Neither SP nor SNR ever had exclusive rights to serve Port shippers; they never had any expectation of perpetual rights to serve Port shippers; and they never undertook a common carrier duty to operate over Port tracks to serve Port shippers. In 1966, SP and SNR constructed the Port Center (or Drill) Track and obtained an agreement from the Port to enable it to operate

over Port trackage to access the Port Center Track until 2016 ("1966 Agreement").¹ Neither carrier obtained regulatory authority for its operation, Petition at 5, apparently concluding that operations on privately-owned Port track were exempt from regulation and were governed only by the terms of the agreements they had made with the Port. All parties retained the flexibility to terminate the arrangement.

Over the years, SNR was acquired by UP in 1983, and in 1996, the Board granted UP's application to acquire and merge the SP into its system.² As a result of those consolidations, UP stepped into the shoes of SNR and SP with respect to the Port agreements. But nothing about those transactions changed either the rights or the responsibilities of the parties under the Agreements. However, the Board did condition its approval of the merger on UP's grant of trackage rights to The Burlington Northern and Santa Fe Railway ("BNSF") to permit BNSF to serve shippers at "2-to-1 Points" where shippers were losing the advantage of two carriers competitively pricing their services. The Port was just such a point.

BNSF did not immediately exercise its right to serve the Port directly, and UP enjoyed a period of years where it was the only carrier operating on Port trackage. And, as feared, the service received by the shippers and the maintenance provided under the agreements deteriorated. In 2001, discussions were had between YSLR and BNSF concerning YSLR performing service in the Port on its behalf. Concurrently, YSLR and the Port began negotiating the terms of an agreement for YSLR to operate on Port trackage. Ultimately, it was decided between the parties that rather than grant YSLR a mere contract right to operate with a short-

¹ In UP's notice of exemption in related Finance Docket No. 34252, UP includes the mileage of the Port Center Track accessed by the 1966 Agreement in calculating the miles of track covered by its exemption.

² See Union Pacific Corporation, Union Pacific Railroad Company, and Missouri Pacific Railroad Company – Control and Merger – Southern Pacific Rail Corporation, Southern Pacific Transportation Company, St. Louis Southwestern Railway Company, SPCSL Corp., and the Denver and Rio Grande Western Railroad Company, Finance Docket No. 32760 (Decision No. 44), 1 S.T.B. 233, 1996 STB LEXIS 220, served Aug. 12, 1996.

term termination clause, the Port would give YSLR property rights in the form of a leasehold interest for an initial term of 10 years, followed by a year-to-year arrangement thereafter.³

The Port could have given UP notice of termination of the 1950 and 1951 Agreements prior to the lease, but for its own reasons that are not relevant to this proceeding, it did not. Instead, it decided to assign to YSLR these two agreements. This assignment did not change the rights or responsibilities of the parties under the Agreements. UP was notified of these activities on September 10, 2001, at a meeting held in Omaha in conjunction with UP's annual gathering of its short line partners. This was also when YSLR first requested that UP amend the cooperative marketing agreement between YSLR and UP so that UP would absorb YSLR's charges for its services in the Port. This was confirmed in a September 26, 2001, email from Mr. John Speight (YSLR) to Mr. John Miller (UP) (attached as Exhibit A).

On October 10, 2001, the Port and YSLR entered into a Railroad Lease and Operating Agreement (the "Lease Agreement") to extend YSLR's system into new territory accessing shippers it previously had not served. Pursuant to the Lease Agreement, the Port granted YSLR, among other rights, a lease and license to possess and operate certain Port-owned track situated "outside the fence" of the Port facility ("Leased Track"). The Port retained possession of its tracks that access shippers "inside the fence". ("Port Facility"). See map attached as Exhibit B.

At the inception of the Lease, UP was providing exempt service in the Port pursuant to the 1950 Agreement, the 1951 Agreement and the 1966 Agreement. The Lease Agreement provided YSLR with the right to provide exclusive service within the Port (subject to the Agreements for the terms thereof), and accordingly, the Port assigned to YSLR all of its rights and obligations under the 1950 Agreement, the 1951 Agreement and the 1966 Agreement. On

³ Section 9.1 of the Railroad Lease and Operating Agreement between YSLR and Port, dated October 10, 2001, provides that "[t]his Lease Agreement shall be effective when fully executed, shall continue in full force and

November 16, 2001, YSLR provided UP with notice of its termination of the 1950 and 1951 Agreements in accordance with the terms of those agreements. The 1950 Agreement has already terminated. The 1951 Agreement will terminate November 16, 2002. The 1966 Agreement will terminate in 2016.

Upon termination of the 1951 Agreement, UP will no longer have the contractual right or responsibility to perform rail operations on the Leased Track. Under the 1966 Agreement, UP will retain the right to use a portion of the Leased Track to bridge its operations between its West Sacramento yard and the UP-owned track referred to as the Port Center Track.

On October 18, 2001, YSLR filed a verified notice of exemption to acquire by lease and operate additional track pursuant to 49 U.S.C. § 10902, which permits class II or III carriers to acquire or operate extended or additional rail line with Board authority.⁴ YSLR used the class exemption procedures established by the Board for use only by class III railroads. 49 C.F.R. § 1150.41 - § 1150.44. The exemption became effective by its terms on October 25, 2001. YSLR has both the contractual right and the regulatory authority to possess and operate the Leased Tracks. Although not required by the class exemption regulations, YSLR served a copy of its notice on Mr. Charles Penner, Director Industrial Development of UP, Omaha, NE, as it had served its notice when it acquired operating rights in McClellan Park earlier that year.⁵

Almost a full year after the exemption became effective,⁶ the UP filed its Petition seeking revocation of YSLR's exemption.⁷ The Board has held that a party seeking revocation has the

effect for a period of ten (10) years and year to year thereafter, unless otherwise terminated as provided herein."

⁴ See Yolo Shortline Railroad Company – Lease and Operation Exemption – Port of Sacramento, STB Finance Docket No. 34114, 2001 STB LEXIS 884, served Nov. 20, 2001.

⁵ See Yolo Shortline Railroad Company – Acquisition and Operation Exemption – County of Sacramento, CA, STB Finance Docket No. 34018, 2001 STB LEXIS 311, served March 27, 2001.

⁶ See Mount Laurel Railroad Company – Acquisition and Operation Exemption – Consolidated Rail Corporation, Finance Docket No. 31974, 1998 STB LEXIS 131, at * 17, served May 15, 1998 (noting that "[w]hile specific time limits are not applicable to the filing of petitions to reopen and revoke under 49 U.S.C. 10505(d), the time elapsed is relevant, and, depending on the facts of the case, concerns for administrative finality, repose, and

burden of proof and must articulate reasonable, specific concerns under the revocation criteria.

Chicago SouthShore & South Bend Railroad – Operation Exemption – Illinois International Port District, Finance Docket No. 32425, served April 15, 1998, 1998 STB LEXIS 100, at * 6-7.

“When, as here, an exemption has become effective a revocation request is treated as a petition to reopen and revoke and, under 49 CFR 1115.3(b), it must state in detail whether revocation is supported by material error, new evidence, or substantially changed circumstances.” Indiana Hi-Rail at * 8. See also GW Switching Services, L.P. – Operation Exemption – Lines of Southern Pacific Transportation Company; Genesee and Wyoming Industries, Inc. – Exemption Continuance in Control of a Nonconnecting Carrier, Finance Docket Nos. 32481 and 32482, 2001 STB LEXIS 656, at * 7-8, served August 7, 2001.

The Petition makes no attempt to argue that UP has any evidence or circumstances that it did not have a year ago, nor has the Petition cited any material error on the part of the Board. Furthermore, the Petition fails to identify a single thing required for a notice of exemption under 49 C.F.R. § 1150.41- 1150.44 that YSLR failed to provide truthfully. All UP did was complain about YSLR’s subsequent exercise of its contract rights. The transaction in this proceeding was not about UP or any of its contract rights, and UP has cited no authority for the proposition that the class exemption regulations require such a discussion. UP has failed to satisfy its burden of proof and, on that basis, YSLR asks the Board to deny the Petition in full.

detrimental reliance must be balanced with those factors that support reopening and revocation, particularly when the challenged exemption pertains to a transaction that cannot readily be undone. . . .” See also Indiana Hi-Rail Corporation – Lease and Operation Exemption – Norfolk and Western Railway Company Line Between Rochester and Argus, IN and – Exemption from 49 U.S.C. 10761, 10762, and 11144; Wilson Fertilizer & Grain Company – Petition for Declaratory Order – Certain Rates and Practices of Indiana Hi-Rail Corporation, Finance Docket Nos. 32162 and 41671, 1998 STB LEXIS 19, at * 8-9, served January 30, 1998 (“Indiana Hi-Rail”) (stating “[w]hen so much time has elapsed, concerns for administrative finally, repose, and detrimental reliance must be balanced against any benefits to be derived from reopening and revocation of the exemption”).

⁷ In a related proceeding, Union Pacific Railroad Company – Operation Exemption – In Yolo County, California, Finance Docket No. 34252, filed Oct. 21, 2002, UP has filed for an exemption to convert its operation on Port tracks that it neither owns nor leases into regulated service.

II. The Verified Notice of Exemption Was Not False or Misleading and, therefore, is Not Void *Ab Initio*.

The Board's regulations at 49 C.F.R. § 1150.43 set forth specific information a rail carrier must provide in a notice of exemption pursuant to 49 U.S.C. §10902 for a transaction such as the lease between YSLR and the Port (*i.e.*, a transaction that will not create a class I or class II railroad). UP does not attempt to argue that YSLR has not provided adequately and truthfully all of the information required for a valid notice of exemption pursuant to section 10902, nor could it: The required information in the notice filed by YSLR is accurate and complete.

Nevertheless, UP claims that YSLR's notice is "materially misleading." Petition at 4. The information characterized by UP as misleading does not relate to the transaction for which YSLR sought authority in its notice *i.e.*, the right to acquire and operate the Leased Track. Rather, the information UP disputes involves matters unrelated to the transaction itself: (1) YSLR's termination of UP's exempt operations over the Leased Track pursuant to the terms of the 1951 Agreement; and (2) YSLR's ability to access the Leased Track. UP Petition at 7-8. The Board's requirements under section 10902 do not extend to the termination of a user's unregulated operations on the line in question or to the issue of whether the additional line is contiguous or requires access via third party carriers. None of the information UP disputes is relevant to a notice of exemption under section 10902. Under these circumstances, the issues raised by UP are not "material" to the validity of YSLR's notice.

A. Board Authority Under the Class Exemption is For the Lease Transaction between the Port and YSLR.

UP concocts an assertion that the YSLR notice was false and misleading based on joint theories of "involuntary discontinuance of service" and "voluntary substitution of carriers."

Neither theory is founded in the law, the regulations or Board precedent. Both reflect UP's narcissistic view of the world.

First, the YSLR Notice involves YSLR's extension of its railroad by leasing the Leased Track from the Port. UP's exempt operations on those tracks were conducted pursuant to a contract that was terminable on one year's notice by either party. UP's rights were no more or less when the property was in the hands of the Port or YSLR. The fact that UP characterizes YSLR's exercise of its rights under the agreement as an "involuntary discontinuance" of service does not bring that action under the Board's jurisdiction or act to preclude YSLR's use of the 10902 exemption.

Nor does UP's "voluntary substitution of carriers" theory change YSLR's right to use the class exemption. But, in fact, the transaction did involve a voluntary substitution of carriers – the Port voluntarily agreed to substitute YSLR for UP to provide service on the Leased Track. The only condition was that the Port and YSLR had to wait a year after giving notice of termination to UP. As UP acknowledged by filing the UP Notice, neither the Port nor YSLR had to obtain regulatory authority to discontinue UP operations. Nothing in the Board's regulations gives a tenant the right to veto the actions of an owner or lessee under their contract.

Second, the Board has no authority under the ICC Termination Act of 1995 ("ICCTA") to regulate the termination of UP's exempt operations over the Leased Track. Right up to its recent death bed conversion, UP has consistently characterized its operations over the Leased Track as exempt pursuant to 49 U.S.C. § 10906. UP Petition at 5; UP Petition, Declaration of Warren C. Wilson ("VS Wilson") at 4. The Board does not exercise jurisdiction over the termination of exempt operating rights under section 10906 or under any other provision of ICCTA. Accordingly, the Board has no authority over YSLR's termination of those UP operating rights.

A notice of exemption that omits future actions over which the Board will have no authority cannot be ruled defective on account of a "material" omission.

Third, notwithstanding the consensual relationship of YSLR and the Port, there is no statutory or regulatory requirement that a notice of exemption under section 10902 involve a "voluntary" substitution of an existing carrier. See Indiana Northeastern,⁸ (denying a petition by existing operator to reject stay and/or revoke a notice of exemption under section 10902). In fact, the Board has expressly stated that a notice of exemption under section 10902 need not disclose even the existence of an existing operator. See Lackawanna County,⁹ at *12 ("[The Board's] regulations at 49 CFR 1150.41 et seq. do not require parties to submit information about whether there is an existing operator on the line."); Indiana Northeastern, at *7. However, in spite of the lack of regulatory requirement, YSLR did state in the YSLR Notice that UP was the current operator and YSLR was to become the exclusive operator.¹⁰

Although the class exemption does apply to "a change in operators,"¹¹ it also applies to operations by a carrier that are in addition to, and not in replacement of, an existing carrier's operations.¹² Accordingly, YSLR's operating authority under a section 10902 class exemption is appropriate irrespective of the continued or terminated operations of UP. Because the class exemption would apply to YSLR's operations regardless of whether UP's operations were

⁸ See Indiana Northeastern Railroad Company – Change In Operators – Branch and St. Joseph Counties Rail Users Association, Inc. In Branch County, Michigan, STB Finance Docket No. 33760, 1999 STB LEXIS 520, served Sept. 1, 1999 ("Indiana Northeastern").

⁹ See Lackawanna County Railroad Authority – Acquisition Exemption – F&L Realty, Inc.; Delaware-Lackawanna Railroad Co., Inc. – Operation Exemption – Lackawanna County Railroad Authority, STB Finance Docket Nos. 33905 and 33906, 2002 STB LEXIS 814, served October 22, 2001 ("Lackawanna County").

¹⁰ The exclusivity cannot occur until UP's rights under the 1951 Agreement terminate November 16, 2002.

¹¹ See 49 C.F.R. §1150.41(c).

¹² The Board has previously demonstrated that its authority governing a notice of exemption under a section 10902 does not depend on whether there is a substitution of operators or an addition of a new operator. See Indiana Northeastern, at *2 (stating that "[a]lthough [the owner and new operator] captioned their notice as a notice for 'change in operators' under 49 CFR 1150.41(c), we will treat the notice as an ordinary exemption for the commencement of operations under section 1150.41(b) because the notice does not claim that the authority of any

terminated and regardless of whether such termination was voluntary, any purported confusion with respect to this information cannot provide a sufficient basis to reject the YSLR Notice.

The disconnect between the lease transaction that is the subject of the YSLR Notice, on the one hand, and the termination of UP's exempt operating rights, on the other hand, is perhaps best illustrated in the following way. Assume the YSLR Notice is revoked and either 1) YSLR files a petition for the same exemption, or 2) the lease transaction between YSLR and the Port is unwound, and the 1951 Agreement reassigned to the Port. In either case, UP will be in the exact position it is in today with respect to its exempt operations over the Leased Track: Its operating rights will terminate on November 16, 2002.

UP's attempt to characterize the YSLR notice as false and misleading because it does not discuss UP ignores the fact that the Port would not have leased its track to YSLR if it had not been dissatisfied with UP service and desired to change operators, as was its right. The operating authority YSLR received pursuant to the YSLR Notice is unrelated to UP's exempt operations under the 1951 Agreement, which is terminable in accordance with its terms without prior regulatory authority.

B. Board Authority Under the Class Exemption is For the Lease Transaction between the Port and YSLR.

UP drags another related proceeding into its attempt to create the impression that the YSLR Notice was not proper.¹³ UP claims that the YSLR Notice is materially misleading because YSLR does not have access to the Leased Track without running over a piece of UP

current operator or past operator on the line will be terminated along with [the new operator's] commencement of operations on the line") (footnotes omitted).

¹³ By letter dated October 10, 2002, UP initiated an arbitration proceeding with respect to the 1992 Trackage Rights Agreement between YSLR and UP.

track on which YSLR has trackage rights.¹⁴ UP is taking the position that the trackage rights under which YSLR operates over UP track do not permit it to handle cars to or from the Port, thereby prohibiting the access. Whether or not UP ultimately prevails in this argument, YSLR's contractual right to access the Leased Track from UP track is irrelevant to whether YSLR may obtain authority to provide service on the Leased Track. Section 10902 does not require that the acquiring carrier have either direct physical access or contractual access via another carrier to the additional line being acquired.¹⁵

In Lackawanna County, two class III carriers filed notices of exemption for authority to acquire and operate, respectively, certain track pursuant to 49 U.S.C. § 10902. A third party rail carrier claimed that these notices of exemption were void *ab initio*, based, in part, on the failure of those notices to disclose that the carrier seeking operating authority could not physically serve the track at the time the notices of exemption were filed. The Board rejected the argument, stating that "[w]hether or not [the two class III carriers that had filed the subject notices of exemption] could provide rail service on the...line does not...determine whether either could invoke the Board's class exemption procedures." Lackawanna County, at *12. The Board further explained:

The question of whether a party (or parties) have regulatory authority to operate over a particular segment of track is different from the question of whether that party (or parties) have the necessary property interest or contractual right under applicable agreements to exercise that authority. In exercising our licensing authority, we look to whether the statutory standards are satisfied, not whether the applicant or petitioner will be able to exercise the authority sought.

See Lackawanna County, at *14.

¹⁴ Yolo Shortline Railroad Company – Purchase and Trackage Rights Exemption – Union Pacific Railroad Company, Finance Docket No. 32107, 1992 ICC LEXIS 159, Aug. 3, 1992.

¹⁵ See Sault Ste. Marie Bridge Company – Acquisition and Operation Exemption – Lines of Union Pacific Railroad Company, STB Finance Docket No. 33290, 1997 STB LEXIS 2989, served January 24, 1997.

The Board's statement in Lackawanna County makes it clear that YSLR's ability to access the Leased Track is not relevant to its use of the class exemption procedures under section 10902.¹⁶ In fact, just eight months earlier, YSLR acquired the right to provide service at McClellan Park, a facility to which it does not directly connect. Thus, the fact that UP has noticed a dispute for arbitration under the provisions of the 1992 Agreement concerning YSLR's right to access the Leased Track from UP track cannot be a basis on which to revoke the YSLR Exemption.

C. Service of YSLR Notice on UP.

It should not go unaddressed that UP's attempts to create the appearance of a procedural error have caused it to create a pseudo argument related to service of the YSLR Notice on UP. If anything, this highlights the weakness of UP's case. Neither the law nor the class exemption regulations require service on a user of track in a section 10902 filing. But, in fact, UP was told about the YSLR/Port agreement a month before it was signed. VS Wilson at 9. The YSLR Notice was sent to Charles Penner at UP's headquarters in Omaha. And finally, UP itself acknowledges that it received notice of termination from YSLR, not the Port, on November 16, 2001. UP Petition at 6. In view of these facts, it is unclear why UP thinks this line of argument should support the UP Petition.

¹⁶ The Board has also made clear that it will not interpret contracts. "The interpretation of contracts lies within the purview of the courts, not with [the Board]." See Lackawanna County, at *14. Even UP appears to concede that the Board is not the appropriate forum to resolve UP's dispute regarding YSLR's right to access the Leased Track. As noted above, UP already has initiated an arbitration proceeding to resolve this dispute. See also UP Petition at 9.

III. The Exemption Was Properly Filed Under Section 10902 and Does Not Require Additional Scrutiny.

A. UP's Contention that the Lease Agreement Was Not Properly Brought Under the Class Exemption is Wrong

Section 10902 of ICCTA sets forth a mechanism whereby "[a] class II or class III rail carrier. . . may acquire or operate an extended or additional rail line. . . ." The Board has adopted a class exemption procedure for transactions conducted under section 10902. See 49 C.F.R. § 1150.41-45.

On October 18, 2001, YSLR, which is a class III carrier, filed a notice of exemption pursuant to 49 C.F.R. § 1150.42, in connection with its proposed lease of tracks owned by the Port. The lease would enable YSLR directly to serve the two active rail customers that are located in the Port, along with Farmer's Rice Cooperative and Nov-Cal Beverage that are served from the Leased Track. YSLR sought an exemption from section 10902 in connection with the Lease because it planned to use the Leased Track to extend its territory and serve new shippers. Regulatory authority was appropriate even though, at the time, UP was using the tracks in question for operations exempt from the Board's jurisdiction under 49 U.S.C. § 10906.

The UP would not have to look far for authority on this question, as it has been a party to two previous transactions that generated two Board decisions which clearly set forth the Board's analysis. In Chicago Rail Link, L.L.C. – Lease and Operation Exemption – Union Pacific Railroad Company, Finance Docket No. 33323 (August 18, 1997) ("Chicago Short Line"), the Board addressed this exact question in the context of a lease by a short line railroad of UP yard tracks. The Board ruled that the regulated or nonregulated nature of the lessee's operations is not governed by the status of the subject tracks in the hands of the lessor:

When two carriers involved in a transaction use track in different ways, the question rises as to which carrier's use controls. In a

lease transaction such as this, we focus on the tenant railroad's use as the controlling factor in determining the character of the track as to the lessee.

Chicago Short Line at 5. The ruling in Chicago Short Line is consistent with the holding in Brotherhood of Locomotive Engineers v. STB, 101 F.3d 718, 726-28 (D.C. Cir. 1996), in which a short line railroad's switching operations requiring operation on UP's main line track were considered exempt from STB jurisdiction.

Thus, the fact that UP has conducted exempt operations on the leased track is not dispositive as to whether the Board has jurisdiction over YSLR's lease of those same rail facilities. YSLR's use of the leased track – to access new, potential customers – plainly brought the lease transaction within the scope of section 10902, and YSLR's filing of its notice of exemption was wholly appropriate. This is the case without regard to the nature of UP's operations in the Leased Track.

B. UP's Characterization of the Lease Agreement as Other Than Routine is Incorrect

UP posits that the Lease Agreement “is not, by any means, a ‘routine’ acquisition and operation transaction.” UP Petition at 10. The basis for this assertion is that, according to UP, “[t]he essence of the transaction is YSLR's forced discontinuance of UP's service over the subject trackage.” Id. (emphasis in original). UP's choice of the words “forced discontinuance” to describe YSLR's termination of the 1950 and 1951 Agreements is a transparent attempt to recast a routine transaction as somehow sinister and non-routine. That attempt fails for several reasons.

First, and most important, UP states that the 1950 Agreement and 1951 Agreement were agreements relating to “exempt industrial trackage.” Id. at 5. Moreover, UP plainly states that “UP's predecessors (Sacramento Northern Railway and Southern Pacific Company) never

obtained any ICC authority to operate over it.” *Id.* (footnote omitted). And UP acknowledges that it currently uses the track for exempt operations. UP Notice at 2. The net effect of these three statements is that, by UP’s own characterization, the termination of the 1950 and 1951 Agreements involves matters beyond the jurisdiction of the Board. The termination of non-jurisdictional arrangements is irrelevant to the exemption of a transaction that falls within the scope of the Board’s authority and could not possibly render a regulated transaction “non-routine.”

Second, in light of UP’s position that the 1950 and 1951 Agreements relate to exempt industrial track, and its admission that its predecessors did not obtain regulatory authority in connection therewith, it is ironic that UP would use the term “discontinuance” to describe YSLR’s exercise of the termination rights under the Agreements. As UP well knows, the term “discontinuance” refers to the regulatory procedure under 49 U.S.C. § 10903 that is required when a tenant railroad voluntarily or involuntarily ceases service over a rail line. The 1950 and 1951 Agreements were not regulated tenancies, and the use of the term “discontinuance” to describe their termination is disingenuous, at best.

Third, UP’s use of the phrase “forced discontinuance” incorrectly suggests that YSLR is taking an action not contemplated under the 1950 and 1951 Agreements. That is plainly incorrect. The 1950 Agreement provided both parties with a right to terminate upon 20 days’ notice.¹⁷ Similarly, the 1951 Agreement provided both parties with a right to terminate upon one year’s notice.¹⁸ YSLR, as assignee of the Port’s rights under the 1950 and 1951 Agreements,

¹⁷ Section 9 of the 1950 Agreement provides that “[t]his agreement shall become effective on May 24, 1950, and shall remain in effect for a period of sixty (60) days and thereafter from month to month, but shall be subject to termination at the end of the initial period or at the end of any succeeding month upon twenty (20) days’ written notice by either party to the other.”

¹⁸ Section 8 of the 1951 Agreement provides that “[t]his agreement may be terminated by either party hereto by giving not less than one (1) year’s (sic) advance notice in writing.”

simply exercised its unambiguous rights thereunder. There is nothing "forced" about YSLR's decision to terminate these Agreements. It was simply a garden variety exercise of rights under commercial agreements. Because those agreements were not regulated transactions, UP's sole recourse, if any, in connection with YSLR's termination of the 1950 and 1951 Agreements, is under applicable state law, not under the ICCTA.

Finally, notwithstanding UP's unhappiness with the termination of its non-regulated arrangements with the Port, it is abundantly clear that the Lease Agreement is a routine transaction that is appropriate for handling under the section 10902 class exemption procedures. The transaction involves 3.1 miles of track being added to the YSLR system. The annual traffic level originating or terminating on these tracks is approximately 1,000 carloads. There are three active shippers (counting Farmer's Rice) in the Port today and several former shippers and new shippers that create the potential for additional traffic. By any measure, this transaction is limited in scope and does not present the possibility of abuse of market power by YSLR (a class III short line railroad operating 35 miles of trackage (before the addition of the Leased Track) and handling approximately 2000 carloads per year).

UP's attempt to analogize the YSLR notice of exemption to the situations in Riverview Trenton R. Co. – Acquisition and Operation, Finance Docket Nos. 33980 and 34040, 2002 STB LEXIS 108, served February 15, 2002 ("Riverview"), and SF&L Ry. Co. – Acquisition and Operation – TP&W Ry. Co., 2002 STB LEXIS 602, Finance Docket Nos. 33995 and 33996, served October 17, 2002 ("SF&L") is unavailing. In Riverview, the record indicated that the acquiring entity used the notice of exemption procedures for section 10901 transactions in an effort to avert the condemnation of rail facilities that were not in common carrier service. Numerous governmental entities protested prior to the consummation of the purchase.

Legitimate public interest issues were in play, and the Board determined that the proceeding would be better handled through a petition for exemption.

In this case, UP's motivation is simply that it does not want its exempt operations terminated in accordance with the terms of the agreements that govern those operations. UP sat on its rights for almost a year, and filed the UP Petition only when the effective date of the termination of its operation was imminent. In a desperation move, UP even filed a notice of exemption in Finance Docket No. 34252 in an effort to "convert" its exempt operations into common carrier service (which would force YSLR to bring an adverse discontinuance action in order to exercise its contractual rights). Ironically, this is precisely the type of abuse of the Board's procedure that led to the revocation of the exemption in Riverview.

Similarly, the fact that UP has received support from a single shipper – Farmers' Rice Cooperative ("FRC") – does not form a basis for revoking the Exemption. FRC indicates that it is satisfied with UP's service and that it would prefer not to have UP be replaced by YSLR at Mill No. 1. (UP would continue to serve the FRC facility at Mill No. 2). But, the mere preference of a shipper for one railroad over another is not a basis for revoking an exemption, especially in a case such as this in which the preferred railroad is not providing regulated service.

The fact that UP has refused to absorb YSLR's \$200 switching fee likewise is no basis for revoking YSLR's exemption. Presumably, UP, YSLR and FRC will all make market-driven decisions that will determine the price and volume of rail traffic moving in and out of the FRC facility and the Port of Sacramento. The simple fact is that FRC sited its mill on a rail facility owned by the Port, and not by UP, and FRC has no right to perpetual service by UP without regard to the Port's property rights.

UP's attempt to equate the YSLR lease of the Port tracks with the situation in the recent SF&L decision falls even further from the mark. In SF&L, the Board revoked an exemption when it found that the acquirer of a 71.5-mile rail line intended to scrap the line and not operate it as a common carrier. Among the indicia of the buyer's intent was the fact that it did not acquire the last one-mile of track, which would have given it access to a connecting carrier. There was no apparent business purpose for not including this one-mile segment in the deal, and the Board found that the buyers "appeared to have intentionally structured the purchase in such a way as to make operating the La Harpe Line unprofitable, so as to facilitate the abandonment of the line. . . ." SF&L at 4. The YSLR Lease bears nothing in common with SF&L situation. YSLR intends to provide common carrier service, and UP has not stated otherwise. The fact that YSLR charges a \$200 per carload for its services (which for FRC would involve a one-mile move) is completely unremarkable; all short lines charge for their services and the fee level charged by FRC does not remotely suggest an intent on the part of YSLR to drive off traffic, abandon the line and scrap it. Indeed, as a lessee, YSLR does not have the contractual right to scrap the line. UP's reliance on SF&L is grossly misplaced.

UP's urgings that the Lease Agreement requires additional scrutiny ring hollow. It does not require additional scrutiny to evaluate the effect of this regulated transaction on UP's unregulated arrangement. This is especially true in light of the fact that UP does not allege that YSLR has done anything but exercise its rights under the 1950 and 1951 Agreements. The Lease certainly does not require additional scrutiny to protect shippers from short line service. The Board and the Commission have strongly supported short line service, even when it is in lieu of class I railroad service.¹⁹

¹⁹ See Louisville & Indiana Railroad Company – Acquisition and Operation Exemption – Consolidated Rail Corporation, Peter A. Gilbertson, et al. – Continuance in Control Exemption – Louisville & Indiana Railroad

Similarly, UP's position that the exemption be revoked because "[t]he service that YSLR intends to provide will not be more 'efficient,'" *id.* at 10, is groundless. There is no requirement under 49 U.S.C. § 10902 or 49 C.F.R. 1150.41 *et seq.* that a purchaser or lessee of a line of railroad demonstrate that it will be more efficient in providing service than the incumbent carrier. If that were the case, and if the mere insertion of an additional carrier were held to render transactions inherently inefficient, there would be no spin-offs of branch lines by class I railroads – like UP's spin-off of YSLR – because those transactions routinely add an additional carrier to a route. The 160 short lines with which UP connects are all "middlemen"²⁰ between UP, as line haul carrier, and the shipper. They are also 160 ways in which service was improved, not harmed. FRC's fears are not based in fact.

UP's assertion that the Lease Agreement will "adversely affect shippers by increasing their shipping costs for no good reason," UP Petition at 10, is likewise disingenuous. UP claims that the \$200 switch charge published by YSLR will be borne by shippers because "UP cannot absorb the YSLR charge because UP will get no saving from the service YSLR will provide." *Id.* at 7, fn. 5. This statement is nonsense. If UP ceases to operate over the Leased Track, serve FRC from that track and drop off and pick up cars at the Port, it will have labor, fuel and equipment savings of some magnitude. If it doesn't, UP needs to look carefully at its operations in West Sacramento.

Company, Finance Docket Nos. 32440 and 32441, 1995 ICC LEXIS 134, at * 15, served June 7, 1995 (stating that "[o]ur experience is that many new short lines provide better service than the class I carriers they succeed"); See also Chicago-Chemung Railroad Corporation – Exemption, Acquisition and Operation – Rail Line of Chicago and North Western Transportation Company Between Harvard and Chemung in McHenry County, IL, Finance Docket No. 31110, 1988 ICC LEXIS 35, at * 11, March 14, 1988, request for reopening denied, 1988 ICC LEXIS 287, September 12, 1988 (rejecting the "generalized challenge to the efficiency and viability of short line railroads" and stating that "[i]t has been [the Commission's] experience that the acquiring firm brings new vitality to the line" and that "[t]ypically, the new operator has closer ties to local communities, will provide better service, and work closely with the line's shippers").

²⁰ VS Wilson at 9.

In addition, UP gives no indication of the margins it earns on Port traffic. If those margins are large, it could simply reduce its net revenue on the traffic. Carriers, including UP, routinely make decisions to reduce their revenue in order to remain competitive for traffic. UP does not provide any explanation of why it would not do so in this case. Indeed, its refusal to absorb any portion of YSLR's fee smacks of bad faith. At a minimum, if UP no longer handles traffic on the Leased Tracks, it will save the per carload fee that UP pays under the 1951 Agreement for use of the Port facility. UP's refusal to adjust its revenue requirements would appear to be exactly why the Board conditioned merger approval on BNSF access at these 2-to-1 points.

Similarly, UP's attempt to cast YSLR's \$200 switching charge as exorbitant does not withstand scrutiny. The charge certainly falls within the range of fees charged by railroads for switching services. But even if UP is correct that the fee is too high, market forces will undoubtedly force YSLR to adjust the fee. Also, UP manages to absorb YSLR charges from \$200 to \$600 for moves of similar or shorter lengths at McClellan Park.

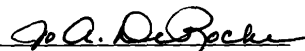
In any event, BNSF has advised YSLR that it is willing to absorb YSLR's \$200 switching fee on traffic to and from the Port. Presumably, BNSF and UP will compete for Port traffic just as they do in other locations. The ultimate charges paid by customers depend on a lot of costs and factors. The charging by YSLR of a \$200 switching charge to all connecting carriers is as reasonable in a UP move as in a BNSF move. UP will find a way to absorb it to compete for the traffic, as it did when it sold the Holland and Woodland branches to YSLR ten years ago. Alternatively, it will refuse to do so and BNSF will handle the traffic. Under any circumstance, UP has cited no authority for its proposition that the amount of a short line's allowance should provide a basis for revocation of its exemption to operate.

After the Lease Agreement was signed, YSLR had obtained its regulatory authority to acquire and operate, and UP had received notice of the termination of the 1950 and 1951 Agreements, UP finally engaged in an effort to work things out with the Port. It was too little too late. In an August 21, 2002 letter to UP (attached as Exhibit C), the Port Director explained why its "contract with YSLR is in [the Port's] best long term business interest." The letter addresses all of the UP arguments and rejects them. The Port's decision to lease its track to YSLR should not be disturbed by the Board.

IV. Conclusion.

For the foregoing reasons, YSLR respectfully requests that the Board deny the Petition in full.

Respectfully submitted,



Mark H. Sidman
Jo A. DeRoche
Rose-Michele Weinryb
Weiner Brodsky Sidman Kider PC
1300 19th Street, NW
Fifth Floor
Washington, DC 20036
(202) 628-2000

Attorneys for:

YOLO SHORTLINE RAILROAD COMPANY

Dated: November 6, 2002

F:\99273\001\tjd\1445FiveReplytoPetitiontoRevoke.doc

EXHIBIT A

Subj: Re: Fwd: Status Update
Date: 10/3/2001 11:08:10 AM Pacific Daylight Time
From: WCMILSON@up.com
To: JJSpeight@aol.com
CC: JJMILLER@UP.COM

John has been out of town since Sept 26. He will get back to you when he returns on 10/8.

JJSpeight@aol.com on 10/03/2001 11:20:03 AM

To: jjmiller@up.com
cc: wcmilson@up.com

Subject: Fwd: Status Update

John,
 Another week has slipped by and we still have not heard from you regarding the status of the below items.
 Any chance we will hear something soon?
 Maintenance is becoming a safety issue on both the Yolo and Sierra railroads!

John J. Speight
 Director of Marketing
 Sierra Railroad Company
 Yolo Shortline Railroad
 Return-path: <JJSpeight@aol.com>
 From: JJSpeight@aol.com
 Full-name: JJSpeight
 Message-ID: <13c.2095548.28e357c3@aol.com>
 Date: Wed, 26 Sep 2001 12:09:39 EDT
 Subject: Status Update
 To: jjmiller@UP.COM
 CC: wcmilson@up.com
 MIME-Version: 1.0
 Content-Type: multipart/alternative; boundary
 ="part2_125.54ac7a8.28e357c3_boundary"
 X-Mailer: AOL 6.0 for Windows US sub 10536

John,
 Can you advise status of these things we discussed at the Shortline Meeting?

YSLR

1. Micon to Washington Transfer maintenance
2. Status of CMA addition to cover locomotives and maintenance of way equipment between McClellan Park and West Sacramento
3. Status of CMA amendment to include setback charges (we have been holding charges pending your change)
4. Status of CMA amendment to include TOFC of hazmat at McClellan Park
5. Status of CMA amendment to cover Port of Sacramento traffic
6. Status of change in interchange agreement (4) above

Sierra

Wednesday, October 23, 2002 America Online: JJSneight

1. Status of bill for \$1400+ for maintenance of switch in Oakdale
2. Status of ongoing repairs and maintenance for Oakdale trackage
3. Status of sale of Oakdale property to local farmer

John J. Speight
Director of Marketing
Yolo Shortline Railroad

Headers

Return-Path: <WCWILSON@up.com>
Received: from rly-xa05.mx.aol.com (rly-xa05.mail.aol.com [172.20.105.74]) by air-xa04.mail.aol.com (v80.17) with ESMTP Id MAILINXA48-1003140810; Wed, 03 Oct 2001 14:08:10 -0400
Received: from uprrsmtp2.notes.up.com (uprrsmtp2.notes.up.com [167.132.252.103]) by rly-xa05.mx.aol.com (v80.21) with ESMTP Id MAILRELAYINXA51-1003140745; Wed, 03 Oct 2001 14:07:45 -0400
Subject: Re: Fwd: Status Update
To: JJSpeight@aol.com
Cc: JJMILLER@UP.COM
From: WCWILSON@up.com
Date: Wed, 3 Oct 2001 13:07:25 -0500
Message-ID: <OFBB04B41E.41C19A98-ON86258ADA.008356EA@notes.up.com>
X-MIMETrack: Serialize by Router on UPRRSMTP2/INTERNET(Release 5.0.7 [March 21, 2001]) at 10/03/2001 01:07:55 PM
MIME-Version: 1.0
Content-type: text/plain; charset=iso-8859-1
Content-transfer-encoding: quoted-printable

[illegible]

EXHIBIT B

PORT OF
Sacramento

August 21, 2002

Mr. Warren C. Wilson
Senior Manager, Rail Line Planning
Union Pacific Railroad Company
1416 Dodge Street
Omaha, NE 68179

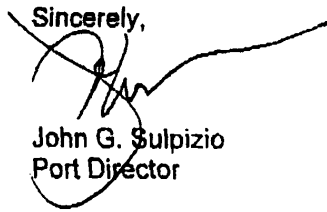
Dear Mr. Wilson:

Your July 19, 2002 letter is appreciated; however, the Port of Sacramento has determined to honor its agreement with Yolo Shortline. The Port maintains that our contract with YSLR is in our best long-term business interest. Moreover, the Port believes that neighboring businesses, and the community at large, will be better served by consolidating all rail shuttle service from the mainline with one short line carrier. This would allow Class "A" carriers to concentrate upon that which they do best, long hauls.

Of course, the Port is concerned that UPRR does not currently intend to adjust rates to accommodate YSLR's agreement with the Port, arguing that it will have no savings with which to offset the reduction. I would respectfully recommend that UPRR consider a consolidation of all its services in West Sacramento with Yolo Shortline, much like I've described above. Such an action plan would seemingly reduce UPRR costs and at the risk of being presumptuous, perhaps even advance the economics for UPRR. The recent agreement between the BNSF and the Yolo Shortline would appear to corroborate this thinking.

Current market dynamics compel the Port to concentrate on our core business. Rail issues have diverted our attention and thus, have motivated our agreement with Yolo Shortline. The Port continues to believe that our intermodal service to our area will improve if the Port stays focused on the waterfront, Yolo concentrates on the short shuttle and UPRR optimizes its performance on the long haul. I sincerely hope UPRR will take another look at their role in this system.

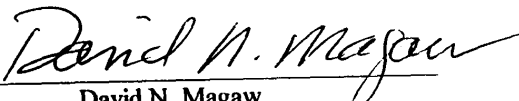
Sincerely,



John G. Sulpizio
Port Director

VERIFICATION

I, David N. Magaw, am the general manager of the Yolo Shortline Railroad Company. I have read the foregoing Reply to Petition to Revoke Exemption under penalty of perjury that the facts contained in the petition are true and correct to the best of my knowledge, information and belief.


David N. Magaw

Dated: November 6, 2002

CERTIFICATE OF SERVICE

I hereby certify that on this 6th day of November, 2002, a copy of the foregoing Reply to the Petition to Revoke the Exemption ("Reply") filed in STB Finance Docket No. 34114 was served overnight by Federal Express, postage prepaid, upon:

Robert T. Opal
General Commerce Counsel
Union Pacific Railroad Company
1416 Dodge Street, Room 830
Omaha, Nebraska 68179

John G. Sulpizio
Port Director
Port of Sacramento
3251 Beacon Blvd., Suite 210
West Sacramento, CA 95798-0070

Curt Graham
Farmers Rice Cooperative
2525 Natomos Park Drive
Sacramento, CA 95833-2927

With respect to Mr. Opal, service was also made by faxing him the Reply at 402-271-5610.


Rose-Michele Weinryb