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July 9, 2002

ENTERED
Office of Proceedings

JUL 16 2002

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Public Record



Mr. Vernon A. Williams
Secretary
Surface Transportation Board
1925 K Street NW
Washington, DC 20423-0001

RE: Finance Docket 30186 (Sub No. 2), Tongue River
Railroad Co.--Rail Construction and Operation--
Ashland to Decker, Montana

Dear Mr. Williams:

I am submitting, on behalf of the Tongue River Railroad Company, an original and ten copies of our four-month progress report for the latest four-month period, pursuant to the Surface Transportation Board's favorable decision served November 8, 1996 in FD 30186 (Sub-No. 2).

Very truly yours,

Thomas E. Ebzery

Thomas E. Ebzery
Attorney for the
Tongue River Railroad Company

TEE/lms

Enc.

cc: Parties of Record

CERTIFICATE OF SERVICE

I hereby certify that on this 9th day of July, 2002, a copy of the foregoing document was served via first class mail, postage prepaid, to the following Parties of Record:

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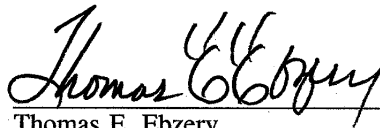
Hon. Judy Martz, Governor
State of Montana
State Capitol
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Catherine Schenk, Chief
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State of Montana
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Helena, MT 59601-4514

General Counsel
Burlington Northern and Santa
Fe Railway Company
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Fort Worth, TX 97161-0039

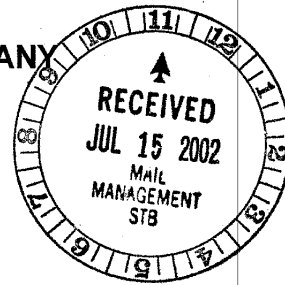
A handwritten signature in dark ink, appearing to read "Thomas E. Ebzery", written over a horizontal line.

Thomas E. Ebzery
1500 Poly Drive, Suite 105
Billings, MT 59102

TONGUE RIVER RAILROAD COMPANY

Four-Month Report to the Surface Transportation Board

July 9, 2002



1. Surface Transportation Board - Regulatory Proceedings

The Surface Transportation Board ("Board") regulatory process relating to the Tongue River Railroad Company's application remains pending. The TRRC application, known as Tongue River III, seeks authority to construct and operate the "Western Alignment" in Rosebud and Big Horn counties. The Western Alignment is proposed as an alternative routing for the southernmost 17.3-mile portion of the 41-mile Ashland to Decker rail line. In addition, the TRRC application includes a request to modify certain portions of the previously approved rail line running between Ashland and Miles City, Montana.

The Tongue River Railroad Company alignment will offer the three surface coal mines located near Decker, Montana, southern Powder River Basin coal traffic moving via Gillette, Sheridan, Huntley and Miles City, as well as new coal mine tonnage originating from the Ashland, Montana area with competitive, efficient and improved rail service to markets in the upper Midwest and the Pacific Northwest.

Recently, the ownership pattern of the coal resources in the Ashland area underwent a significant change. On April 10, 2002, the U.S. Department of the Interior transferred to the State of Montana the federal mineral title to three Otter Creek tracts. (see attached Billings Gazette April 11, 2002 articles) The three Otter Creek Tracts, located southeast of Ashland, Montana, contain 533 million tons of high quality sub-bituminous coal and were received by the State of Montana as payment in lieu of the development of the New World/Crown Butte gold mine near Yellowstone National Park resulting from a 1996 agreement that preempted the construction of the New World/Crown Butte gold mine outside Yellowstone Park.

Under a mandated congressional directive, the Department of the Interior was required to transfer the federal mineral rights to Montana. The 1998 Interior Appropriations Act required that the Department of the Interior convey to Montana, without consideration, all right, title and interest in \$10 million in federal mineral rights, agreed to by the Secretary of Interior and the Governor of Montana through negotiations, or all federal mineral rights in Otter Creek Tracts 1, 2 and 3. The transfer comprises approximately 7,623 acres of federal minerals, including 2,110 acres of federal coal rights, 40 acres of federal coal, oil and gas rights, and 5,473 acres of federal minerals rights that include all minerals. The coal in the Otter Creek Tracts is considered high-quality and exceeds the emission standards established by the 1990 Clean Air Act Amendment. The transfer creates contiguous holdings of private/state coal, offering the possibility of large-scale development of the coal resource.

Prior to the transfer of the federal mineral rights to the State, the Montana State Land Board and the Northern Cheyenne Tribe entered into an agreement that settled a lawsuit previously filed by the Northern Cheyenne Tribe challenging the federal government's authority to make the mineral transfer. The State of Montana - Northern Cheyenne Tribe agreement requires the development and approval of operating plans addressing employment, contracting, environmental monitoring and cultural resource protection concerns of the Northern Cheyenne Tribe prior to development of the state coal resources in the three Otter Creek Tracts. (see attached Billings Gazette Guest Opinion dated March 19, 2002)

As noted in the attached news articles, development of the State of Montana Otter Creek Tract coal resources could generate significant coal royalty and tax revenues for the State and create new high paying coal industry jobs. The State intends to make the coal assets received in the Otter Creek transfer available for commercial development. Coal developed from the Otter Creek Tracts will most certainly utilize the TRRC alignment approved by the Board's predecessor in 1986 in order to reach the marketplace.

Pursuant to the pending TRRC application, the Board's Section of Environmental Analysis will prepare a Draft Supplemental EIS incorporating a focused review of the EIS documents prepared in the previous approvals of Tongue River I and Tongue River II. Tongue River I is in reference to the 89-miles of rail line located between Miles City and Ashland, Montana approved by the Interstate Commerce Commission in 1986. Tongue River II refers to the 41-miles of rail line running south from the approved Miles City to Ashland line to connect with

existing rail lines serving the Decker, Montana coal mines that the Board approved in 1996. The Draft Supplement will advance from Environmental Impact Statements prepared in Tongue River I and Tongue River II and incorporate information independently obtained through a third party environmental contractor. In addition, the Draft Supplemental will include a focused review of the analyses completed in Tongue River I and Tongue River II to address changed circumstances and resulting potential impacts related to the proposed alignment refinements.

2. Secondary Approvals

The Draft Supplement will be developed in consultation with three agencies that have requested cooperating agency status. The three cooperating agencies are the Montana Department of Natural Resources and Conservation, the U.S. Department of Interior, Bureau of Land Management, and the U.S. Army Corps of Engineers. The Montana Department of Natural Resources and Conservation is acting as the lead agency for a number of state agencies, including the Montana Department of Fish, Wildlife & Parks and the Montana Department of Environmental Quality. The cooperating agencies are responsible for granting approvals and easements secondary to the Board's approval in Tongue River III.

As part of the Draft Supplement preparation, the SEA will conduct additional agency consultation in addition to the consultation with the cooperating agencies. The agencies consulted will include EPA, USFWS, SHPO and ACHP.

3. Relationship with Burlington Northern Santa Fe

The Burlington Northern Santa Fe Railroad continues its support of the development and operation of the Tongue River Railroad. The parties have maintained communications during the reporting period and continue discussions relative to the market forecasts, project status and an agreement between the parties.

4. Engineering and Design

Final engineering and design efforts remain on hold pending completion of the Draft Supplemental Environmental Impact Statement and secondary approvals.

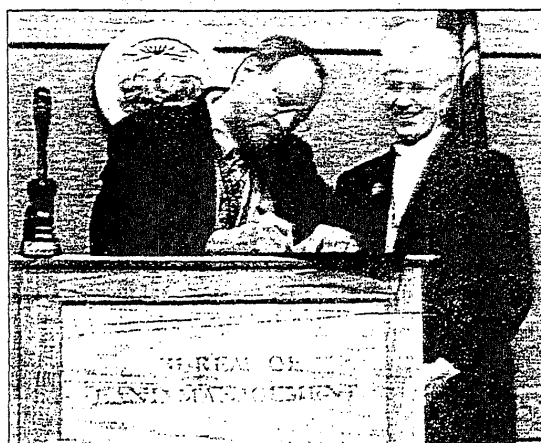
5. TRRC Ownership Structure

As reported previously, Tongue River Railroad Company, Inc. is a Delaware corporation, whose sole shareholder is Tongue River Railroad Company, a Montana limited partnership. Transportation Properties LLP, a limited liability partnership, is the general partner in Tongue River Railroad Company, while Tongue River Holdings Inc., a Montana corporation, is the limited partner. WesRail, Inc., a corporation and wholly owned subsidiary of Wesco Resources, Inc., retains full ownership of Transportation Properties. WesRail continues its efforts with potential investors in the Tongue River Railroad project.

Billings Gazette

THURSDAY, APRIL 11, 2002

The Source



BOB ZELLAR/Gazette staff

BLM State Director Matt Millenbach signs the mineral rights patent for the Otter Creek coal tracts, later presenting it to Gov. Judy Martz, right.

Signed, sealed, delivered: Federal coal in state's hands

By JIM GRANSBERY
Of The Gazette Staff

A joyful Gov. Judy Martz accepted the deed from the federal government Wednesday for 533 million tons of high-quality coal in southeastern Montana.

The Otter Creek Tracts — 11 sections in three blocks — southeast of Ashland, became state property as Matt Millenbach, state director of the U.S. Bureau Of Land Management, signed the federal patent, had it

sealed by Debbie Sorg, land law examiner for the office, and handed it to the governor.

Martz said the state was receiving "the most significant asset since statehood."

"The development of two of the three tracts could result in half a billion dollars in taxes and royalties over the next 10-15 year period," she said.

Martz said she wanted movement on developing the

Please see Coal, 7A

Coal ①

Coal

Continued from 1A

coal tracts "within the next year."

The newly acquired assets come under the purview of the State Land Board, which must prepare a request for bids on a lease.

Martz said at least three parties have expressed interest in developing the coal. One of the interested parties is a budding consortium that includes the construction giant Bechtel Enterprises and the Burlington Northern Santa Fe Railway.

About 50 people attended the signing and transfer at the State BLM Office in Billings, including representatives of the Northern Cheyenne tribe.

Earlier this year, the tribe filed a lawsuit against the Interior Department to delay transfer of the federal coal. The tribe said it wanted employment opportunities and other protections written into the deal.

On Feb. 19, the land board's three Democrats voted to impose some conditions on development of the tracts. In exchange, the tribe withdrew its suit.

"I will work with industry, local governments and the Northern Cheyenne Tribe."

— Gov. Judy Martz

Martz opposed the conditions, calling for more study of the issues and their effects on leasing the coal.

Regardless, the governor Wednesday said she wanted "to move forward."

"I will work with industry, local governments and the Northern Cheyenne Tribe," she said.

Hilda Moss, a Cheyenne and a member of the tribal council, told the governor her tribe is "part of Montana, too," and the day represents accomplishments on behalf of the Cheyenne.

"We will be greatly impacted by this honorable day," she said.

Joe Walks Along Sr., a tribal elder representing President Geri Small, who was unable to attend, said the tribe has the highest number of unemployed in the state. He spoke of the Otter Creek area as being a traditional hunting ground.

Referring to dialogue between Native Americans and the non-Indian population of the state, he said there was a lack of communication and "I wish we could talk better."

As a pastor for the past 40 years, he called for "peace with all the people of the world."

Martz said after the official presentation she would continue to press for continuing action on the development of the sites.

"To wait has no ramifications for the people," she said. "This is also a signal to developers to move forward."

Opening a mine and building a railroad to haul coal to Miles City for use in coal-fired generating plants may cost up to \$4 billion over the next decade, according to some estimates.

The coal in the Otter Creek tracts is considered high-quality and exceeds the standards set by the Clean Air Act. The transfer creates contiguous

holding of private/state coal, offering the possibility of large-scale development of the resource.

The coal is Montana's payment in the 1996 deal that preempted the construction of the New World/Crown Butte gold mine outside Yellowstone Park. Although the 1998 Interior Appropriations Act outlined the transfer of the coal tracts, Secretary of the Interior Bruce Babbitt refused repeated requests by Gov. Marc Racicot that the Otter Creek tracts be turned over.

Early in 2001, Martz asked the new Secretary of the Interior Gale Norton to transfer the tracts.

Former U.S. Rep. Rick Hill, R-Mont., who was instrumental in getting the Otter Creek tracts into the 1998 Interior appropriations bill, estimated the Otter Creek coal had a potential value to Montana of \$600 million in taxes and royalties.

Martz thanked Hill for his efforts and also acknowledged the efforts by the current congressional delegation of Sens. Max Baucus and Conrad Burns and Rep. Dennis Rehberg.

Jim Gransbery can be reached at 657-1288 or at jgransbery@billingsgazette.com

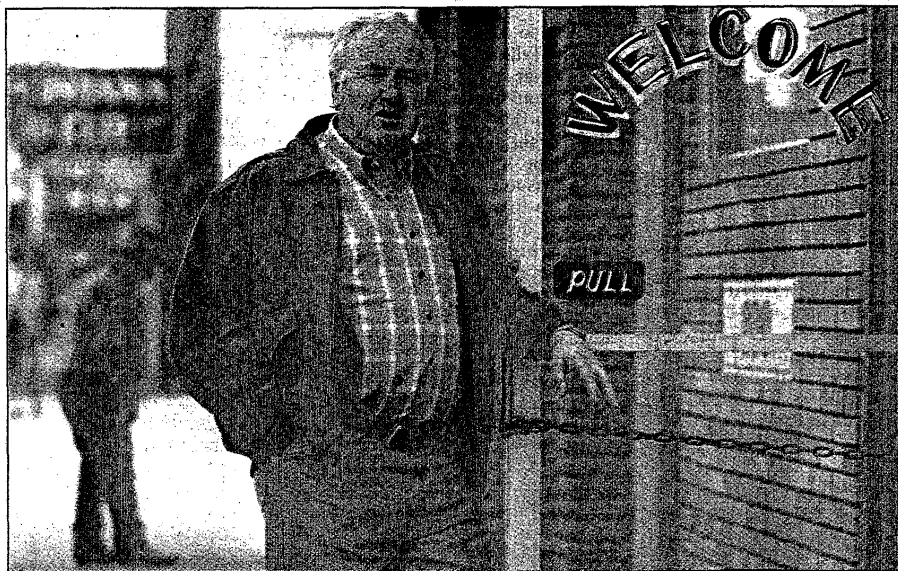
Coal (2)

Billings Gazette

THURSDAY, APRIL 11, 2002

The Source

Otter Creek news spurs high hopes in Miles City



JAMES WOODCOCK/Gazette staff

Tom McKerlick, executive director of the Miles City Area Economic Development Council, says development of the Otter Creek coal tracts could be a tremendous boon to Miles City and Eastern Montana.

miles city -

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Area officials worry red tape could sink \$4.5 billion project

By JAMES HAGENGRUBER
Of The Gazette Staff

MILES CITY — Jack Regan has a hard time not thinking about the mountains of black coal buried 89 miles south of his office.

It's especially tough at the end of the school year when teachers in his district retire. Regan, the superintendent of schools, knows there is no money to replace the two, three or four who leave each year.

The coal also comes to mind when the school year starts and Regan sees more empty desks in Miles City classrooms. In the last four years, the high school has dropped from about 720 students to 600.

The jobs, young people and hope continue to flow out of Eastern Montana. Like most others in Miles City, Regan holds his breath for the day when railroad cars spilling over with Otter Creek coal come rolling up shiny new tracks, stopping at the boilers of a new power plant outside of town.

"Could we build a new high school? Yeah. Could we pay our employees? Yeah. Could we maintain our streets? Yeah. Would the property taxes on my house go down? Yeah," Regan said. "It would just turn everything around."

The prospect of a \$4.5 billion energy project in southeastern Montana has people in these parts positively giddy, said Tom McKerlick executive director of the Miles City Economic Development Council.

"It's mind-boggling," he said Tuesday.

If everything goes smoothly, the first bucket of coal could be scooped in two or three years, McKerlick said. In the best case, it will be hauled over new railroad tracks to a massive power-generating plant outside Miles City. The electricity will be zapped directly to big cities.

Unthinkable amounts of money will be shipped back to Montana. Hundreds of miners, railroad workers and power plant operators will spend their fat paychecks in small towns across Eastern Montana. Their children will attend new schools. The economic ailments of Eastern Montana will be cured.

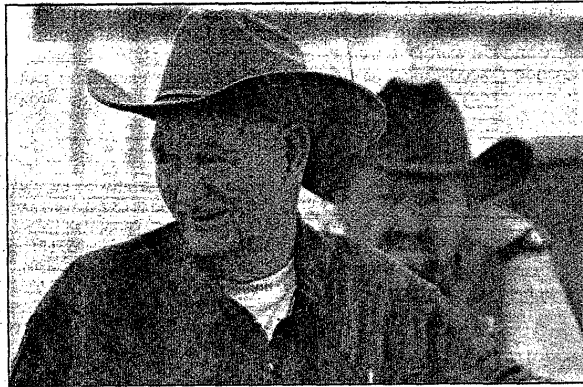
"We're hopeful," McKerlick said, smiling.

But the optimism is cautious. Business leaders in Miles City think there's too much potential red tape from state regulators. They worry investors will be scared away by an agreement between the state and the Northern Cheyenne Tribe, which owns land three miles west of the coal tracts. The tribe threatened a lawsuit to preserve cultural sites near the tracts. The

Please see Miles City, 7A



JAMES WOODCOCK/Gazette staff
Jack Regan, superintendent of the Miles City Schools, thinks that development of the Otter Creek coal reserves could be one of the biggest economic events ever in Montana.



JAMES WOODCOCK/Gazette staff
Rancher Frank Wootan is all for development of the Otter Creek coal reserves and says "Montana needs all the damned economy it can muster."

Miles City (2)

Miles City

Continued from 1A

tribe also has a 70 percent unemployment rate and would like a share of the new jobs.

Mark Hungerford, president of the Billings-based Ozora Corp., told state officials the agreement could derail the project. Hungerford is a backer of the 89-mile railroad spur, which is needed to transport the coal out of the hills southeast of Ashland.

"If you put on these stipulations... the real money will not come," he told state officials Feb. 19 after they agreed to the conditions set by the Northern Cheyenne.

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Apart from new fast food restaurants and hotels huddled next to Interstate 94, Miles City has more businesses leaving than starting. But compared with the rest of Eastern Montana, the city is doing relatively well, McKerlick said.

Miles City isn't growing but it is hanging on, he said. There's few vacancies along the town's historic main street. The annual Bucking Horse Sale continues to draw tourists from around the world. The city's population of about 9,000 hasn't changed much in 50 years. "Then again, neither have cattle prices," McKerlick added dryly.

Many of the farmers and ranchers who haven't been forced out of business in recent decades are deep in debt. Miles City is the regional hub of southeastern Montana. If people in Jordan, Terry and Broadus don't have money, neither do the businesses in Miles City.

"The people have stopped coming in," McKerlick said. "We have seen a deterioration of the whole region. There's just not a



JAMES WOODCOCK/Gazette staff

Miles City cab dispatcher Joe Scanlan came back to live in Miles City after leaving 36 years ago and says it seems like a ghost town from what he remembers during better economic times.

lot of good happening."

Just outside of downtown, near the remnants of Fort Keough, Frank Wootan was attending a horse sale Tuesday afternoon. Wootan ranches 45 miles southeast of town. The 73-year-old said he's angry that the state isn't trying to make the coal project more attractive to outside investors.

"Montana needs all the damned economy it can muster," he said.

The mine project, railroad and coal-fired power plant would bring about \$600 million in taxes to the entire state, McKerlick said. The project would also return Miles City to its previous economic might, back when it was larger than Billings, when steamers full of buffalo hides and beaver pelts chugged away from its docks.

"It's always been a Western town," McKerlick said. "I think natural resource development is what we should be looking at to sustain us."

Without high-paying jobs, young people leave.

Next year, Tony Montoya hopes to transfer from Miles Community College to Montana

"This is the chance of a lifetime."

— Jack Regan,
Superintendent
of the Miles City Schools

State University, where he will finish his business degree. The 20-year-old Colstrip native then hopes to open a snowboard and bicycle shop.

Montoya said he can't even find a part-time job in Miles City and he doubts he will have much success returning here to make a living after college.

"I doubt I'll be back," he said while eating lunch in the two-year college's cafeteria. "There's just not much to do here. It's a good place to grow up, though."

No matter where they live, young people get the itch to leave their hometown, said Darrel Hammon, president of Miles Community College. But towns die without new blood. The coal development would "provide opportunities for kids

to stay," he said.

"If you are not progressing, you are retrogressing," Hammon said. "You cannot stand still."

In fall, Miles Community College will restart a power plant technology program in Colstrip, where a new generation of trained employees is needed to run the plant. The program could easily expand to train workers for a new facility in Miles City, Hammon said.

"This town is more than backing a power plant, more than backing a railroad," he said.

Discussions about coalbed methane development tend to send people to opposite corners of the room. But the prospect of coal mining is less divisive because there's less impact to water supplies, McKerlick said.

Even without a power plant, the project would create about 220 permanent mining jobs and about 70 railroad jobs, McKerlick said. With a power plant, the jobs and economic growth reach "unimaginable" numbers, he said.

Everything depends on private investors willing to pay for the project. Exploration costs alone will exceed \$10 million. The railroad would be about a \$200 million investment. A power plant would cost billions of dollars.

School superintendent Regan said there's too much red tape for him to be confident that Otter Creek coal will be rolling into town anytime soon. He's doubtful about being able to hire new teachers, or budget for major repairs for 80-year-old school buildings.

"I hope we're wrong," he said.

With new power sources on the horizon — such as hydrogen and fuel-cell technology — delay could be deadly for coal, and it certainly wouldn't help Eastern Montana, Regan said.

"We're just afraid that the window of opportunity is going to pass. This is the chance of a lifetime."

miles city

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Guest opinion

Tribe sees role in development of Otter Creek coal

By GERI SMALL
Tribal President

On Feb. 19, the Northern Cheyenne Tribe and the Montana State Land Board entered into an agreement that enables the transfer of 533 million tons of federal coal to the state which lie about three miles east of our reservation. The tribe wants the Feb. 19 agreement and the tribe's position to be fairly represented to the public.

Transfer of the Otter Creek tracts will be a windfall to Montana. The state predicts massive development and state and local governmental revenues of \$700 million in the first 13 years (dwarfing the \$10 million in losses from termination of the gold project near Yellowstone that the Otter Creek transfer was intended to mitigate).

None of the Otter Creek revenues will reach our reservation, even though we will be heavily impacted. We are hopeful that the Montana congressional delegation will deliver on its commitment to seek federal impact funding to offset tribal impact costs. The Feb. 19 agreement does not call upon the state or industry to bear such costs.



SMALL

The Otter Creek coal mines and related projects will employ hundreds of people. The Northern Cheyenne are the largest, most needy and most available indigenous work force in the area. Our unemployment rate is 70 percent. Some assume our people will receive Otter Creek jobs, but this is contradicted by history. The major coal mines and power plants just across our borders have provided little or no employment to our people. The few exceptions have been where a project has been legally compelled to do otherwise.

Providing job opportunities

Consequently, the agreement calls for an operating plan addressing employment. The operating plan is aimed at providing employment opportunity to local residents living on and off the reservation — Indian and non-Indian alike — who are qualified and available, without any preferences or quotas for Indians. When an operator decides to move forward with an Otter Creek project, it must fashion an operating plan in consultation with the tribe and submit it to the Land Board for approval.

The agreement also calls for operating plans aimed at: contracting opportunities for Northern Cheyenne firms that are qualified and available without preferences, quotas or bidding margins; encouraging work force, while on our reservation, to observe reasonable standards of conduct; environmental monitoring; and protection of cultural resources.

BILLINGS GAZETTE MARCH 19, 2002

The Land Board, not the tribe, approves the operating plans. This safeguard should make industry and other stakeholders comfortable. The tribe puts its trust in the Land Board to fairly meet all of its responsibilities under the agreement and to the school trust. If the tribe can trust the Land Board, why can't industry and everybody else?

The tribe initiated its effort to resolve its Otter Creek concerns quite some time ago. It explained its concerns, proposed solutions and made many accommodations in extensive discussions and negotiations with Gov. Martz, Lt. Gov. Ohs, the Land Board, the Secretary of the Interior, regional BLM officials and Great Northern Properties LC (the principal owner of the vast privately-held Otter Creek coal). We did our best to be responsive to input from all these sources, especially state officials and private industry.

State has much to gain

Sens. Conrad Burns and Max Baucus encouraged us to proceed in this way, to arrive at an agreement that would clear the way for the transfer and provide our community with some of the benefits, rather than just the burdens, of development.

On their part, the congressional delegation committed to pursue federal legislation that would provide impact funding and would remedy a 100-year-old federal error that deprived the tribe of ownership of 8-1/2 sections of valuable coal within its reservation. The state and southeast Montana have everything to gain and nothing to lose from such legislation, as it will bring federal funds to the region and make additional federal coal available for regional development, with resulting jobs and revenues.

A few have irresponsibly speculated that the tribe is really laying plans for litigation to block development. This is totally false. As required by the Feb. 19 agreement, we have given up our legal claims against the transfer. The tribe hopes the agreement will produce a positive tribal relationship with Otter Creek development, and also relies on the Montana delegation to follow up on its commitments. For the first time, this will give the tribe a positive stake in, and induce tribal support for, off-reservation development.

Everybody from the governor on down supported the tribe's goals here, but opinions differed on how best to achieve them. A balanced and moderate agreement is now in place. It is completely compatible with development. If everyone will give the agreement a chance, it will prove beneficial to all.

Geri Small is the president of the Northern Cheyenne Tribe.