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217133

July 13, 2006

BY HAND DELIVERY

Honorable Vernon Williams
Secretary
Surface Transportation Board
1925 K Street, N.W., Suite 700
Washington, DC 20423-0001



Re: STB Ex Parte No. 575, Review of Rail Access and Competition
Issues -- Renewed Petition of the Western Coal Traffic League

Dear Secretary Williams:

Attached please find the original and ten copies of a summary of the testimony that Rick Webb, Chief Executive Officer of Watco Companies, Inc., intends to present at the public hearing on July 27th.

Please date-stamp the extra copy of this letter and return it with our messenger.

Sincerely,

Karl Morell

Attorney for Watco Companies, Inc.

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Public Record

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BEFORE THE
SURFACE TRANSPORTATION BOARD



STB Ex Parte No. 575

REVIEW OF RAIL ACCESS AND COMPETITION ISSUES – RENEWED PETITION OF
THE WESTERN COAL TRAFFIC LEAGUE

COMMENTS OF WATCO COMPANIES, INC.

PRESENTED BY

RICK WEBB

CHIEF EXECUTIVE OFFICER

WATCO COMPANIES, INC.

Dated: July 13, 2006

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BEFORE THE
SURFACE TRANSPORTATION BOARD

STB Ex Parte No. 575

REVIEW OF RAIL ACCESS AND COMPETITION ISSUES – RENEWED PETITION OF
THE WESTERN COAL TRAFFIC LEAGUE

COMMENTS OF WATCO COMPANIES, INC.

Watco Companies, Inc., and its 16 railroad subsidiaries submit these comments in response to the Surface Transportation Board's ("Board") decisions served February 1, 2006 and March 10, 2006, in this proceeding.

In this proceeding, the Board has called a public hearing to address concerns raised by certain parties about so called "paper barriers" contained in agreements for the sale or lease of rail lines by large railroads to existing short lines or new carriers. More specifically, various parties have requested the Board to adopt rules which would limit the ability of the seller or landlord carrier to restrict the purchaser or tenant carrier from interchanging traffic with other competing carriers.

In the February 1st decision, the Board specifically sought comments that: (1) discuss the Board's statutory authority to address pre-existing paper barriers; (2) identify and describe existing paper barriers; (3) identify and quantify any problems experienced by shippers as a result of paper barriers; (4) address the short and long term economic impacts of paper barriers;

(5) address the effectiveness of the AAR/ASLRRA agreement on paper barriers; and (6) include information about the Railroad Industry Agreement ("RIA").

INTEREST OF WATCO

Watco Companies, Inc., a non-carrier, is a Kansas corporation which currently controls the following sixteen (16) Class III railroads operating in fourteen (14) States: South Kansas and Oklahoma Railroad Company, Palouse River & Coulee City Railroad, Inc., Timber Rock Railroad, Inc., Stillwater Central Railroad, Inc., Eastern Idaho Railroad, Inc., Kansas & Oklahoma Railroad, Inc., Pennsylvania Southwestern Railroad, Inc., Great Northwest Railroad, Inc., Kaw River Railroad, Inc., Mission Mountain Railroad, Inc., Mississippi Southern Railroad, Inc., Yellowstone Valley Railroad, Inc., Louisiana Southern Railroad, Inc., Arkansas Southern Railroad, Inc., Alabama Southern Railroad, Inc., and Vicksburg Southern Railroad, Inc.

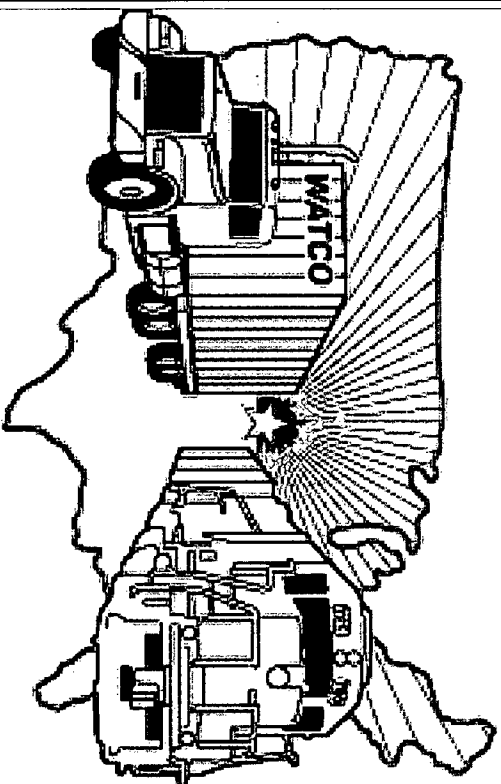
Many of the agreements between Watco's subsidiary railroads and the various Class I railroads contain restrictions that limit the subsidiary railroads' ability to route traffic. Watco, however, does not view the restrictions as anticompetitive or evil as some parties to this proceeding suggest.

I have four points to share with you on the general topic of paper barriers:

- Contracts that are between two consenting parties should not be interfered with by the government.
- The Rail Industry Working Group, while not perfect, is a step in the right direction to promoting a positive problem solving dialogue between the shortlines and Class I railroads.
- Paper barriers are actually a key element of Shortline outsourcing, and as such, are key elements of improving service and capacity in the North American Rail Network.

- To facilitate a better understanding of paper barriers, the Board should consider requiring the reporting of paper barriers in the actual exemption notice that creates a new rail carrier. In this format the carriers would be able to describe upfront the benefit of the paper barrier and the reason why the carriers agreed to the paper barrier in the first place. I think you will find there are good reasons why the barriers are in place, and more importantly a process like this will educate all parties upfront and create an open and honest dialogue.

I plan on elaborating on these four points with the aid of a power point presentation at the July 27th public hearing.



WATCO

COMPANIES, INC.

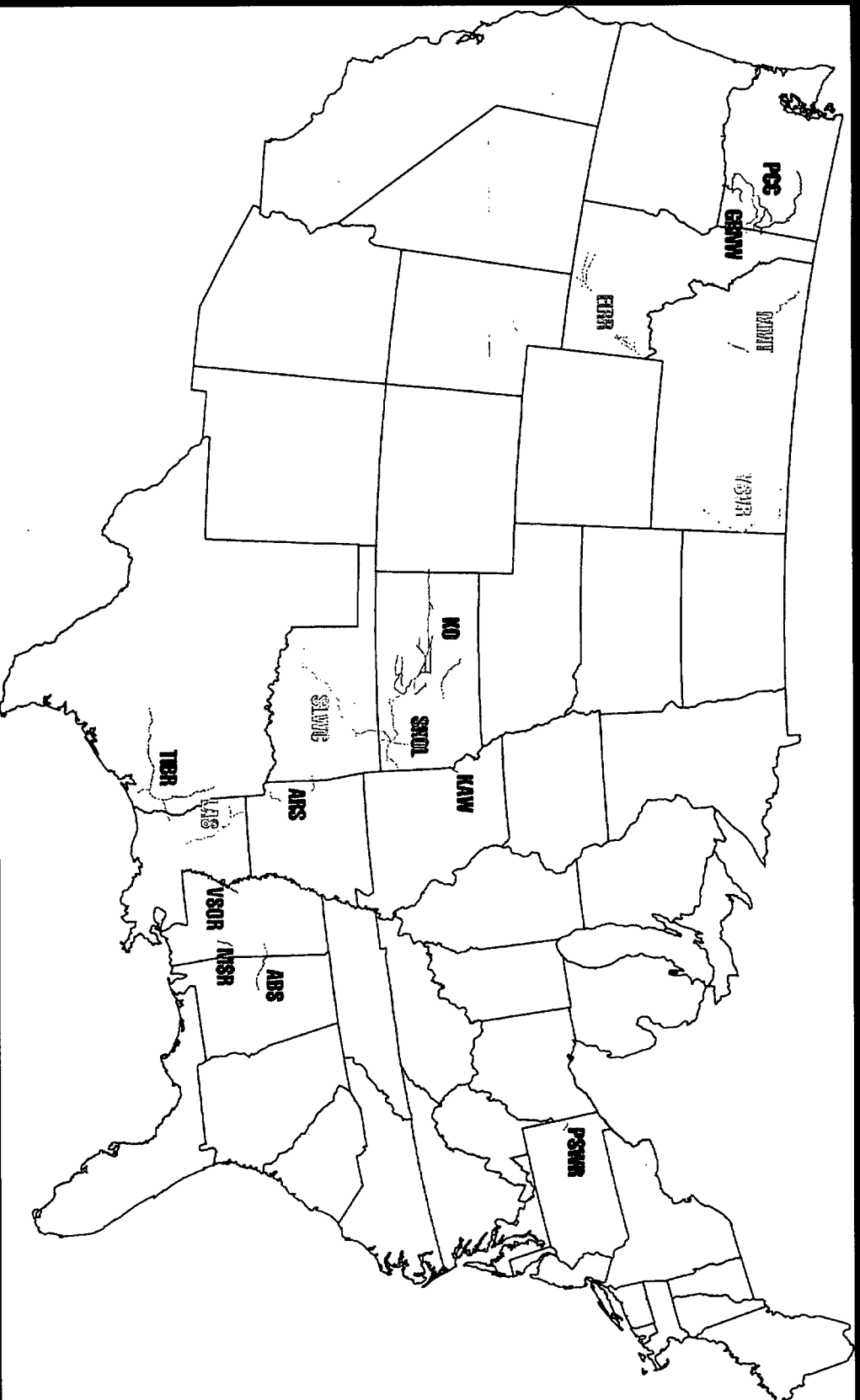
"Your Transportation Specialists"

STB Ex Parte No. 575

**Review of Rail Access and
Competition Issues**

**Comments of Watco Companies
Presented by Rick Webb, CEO**

Watco's shortline railroads



Watco's Family of Railroads

Alabama Southern
KCS, CSX, NS

Mississippi Southern
KCS

Arkansas Southern
KCS, UP

Palouse River & Coulee City
UP, BNSF

Eastern Idaho
UP

Pennsylvania Southwestern
NS

Great Northwest
UP, BNSF

South Kansas & Oklahoma
UP, BNSF, KCS, KO, SS

Kansas & Oklahoma
UP, BNSF, KYLE, SKOL

Stillwater Central
UP, BNSF, GNBC

Kaw River
KCS, BNSF

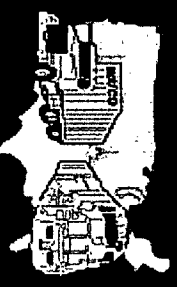
Timber Rock
BNSF, KCS

Louisiana Southern
KCS

Vicksburg Southern
KCS

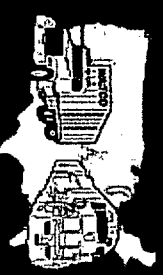
Mission Mountain
BNSF

Yellowstone Valley
BNSF



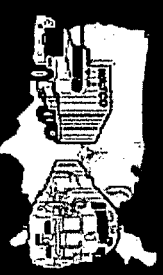
Four points on paper barriers

- Contracts between two consenting parties should not be interfered with by the government.
- The RIWG is a step in the right direction, while not perfect, does create a dialogue for industry driven problem solving.



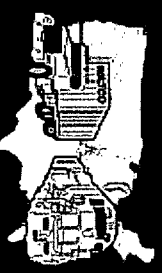
Four points on paper barriers

- Paper barriers are a key element of shortline outsourcing.
- STB should consider requiring the reporting of paper barriers in the initial exemption notice that creates a new rail carrier or allows additional track to be acquired.



Paper barriers are a key element of shortline outsourcing

- Paper barriers lower the cost of acquisition
 - ◇ In many cases avoids full going concern costs of transaction
 - ◇ Lowers barriers for entry
 - ◇ Avoids potential abandonment's because the NLV is greater than the going concern value

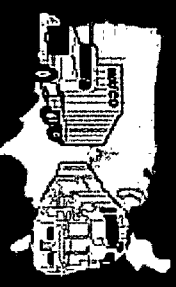
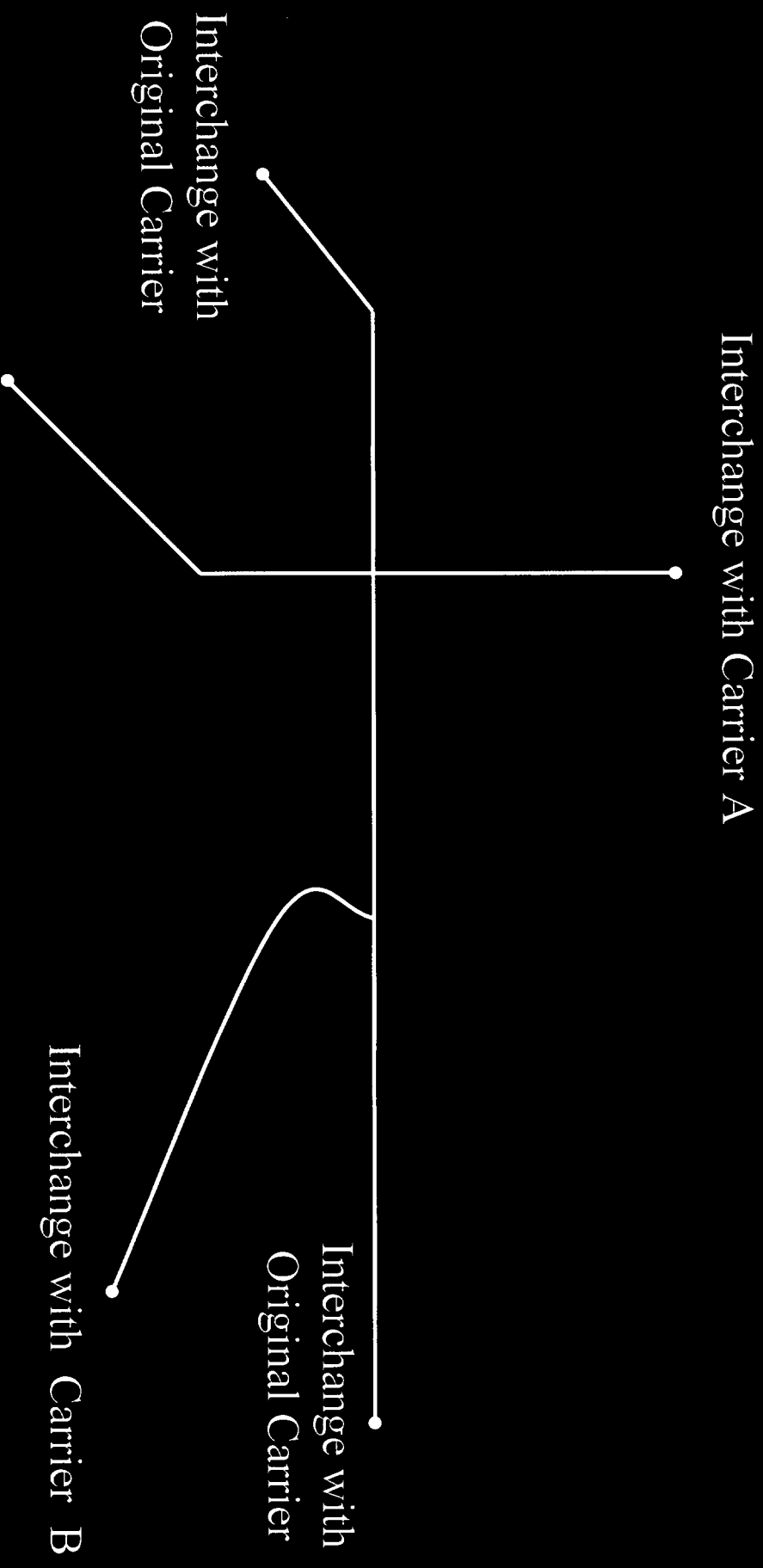


Paper barriers are a key element of shortline outsourcing

- Paper barriers allow larger regional networks to be created
 - ◇ This allows local short haul traffic to be developed
 - ◇ Additional value for Customers
 - ◇ Additional value for communities
 - ◇ Grows the shortline industry

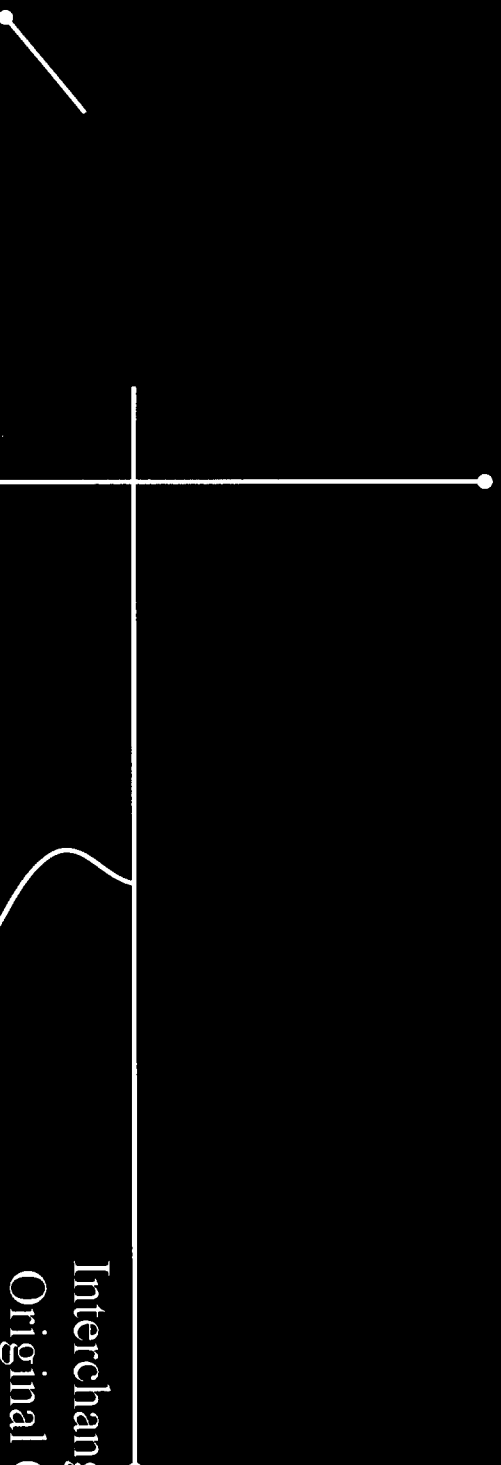


Sample Network



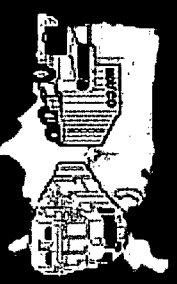
Initial Abandonment

Interchange with Carrier A

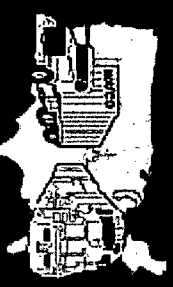
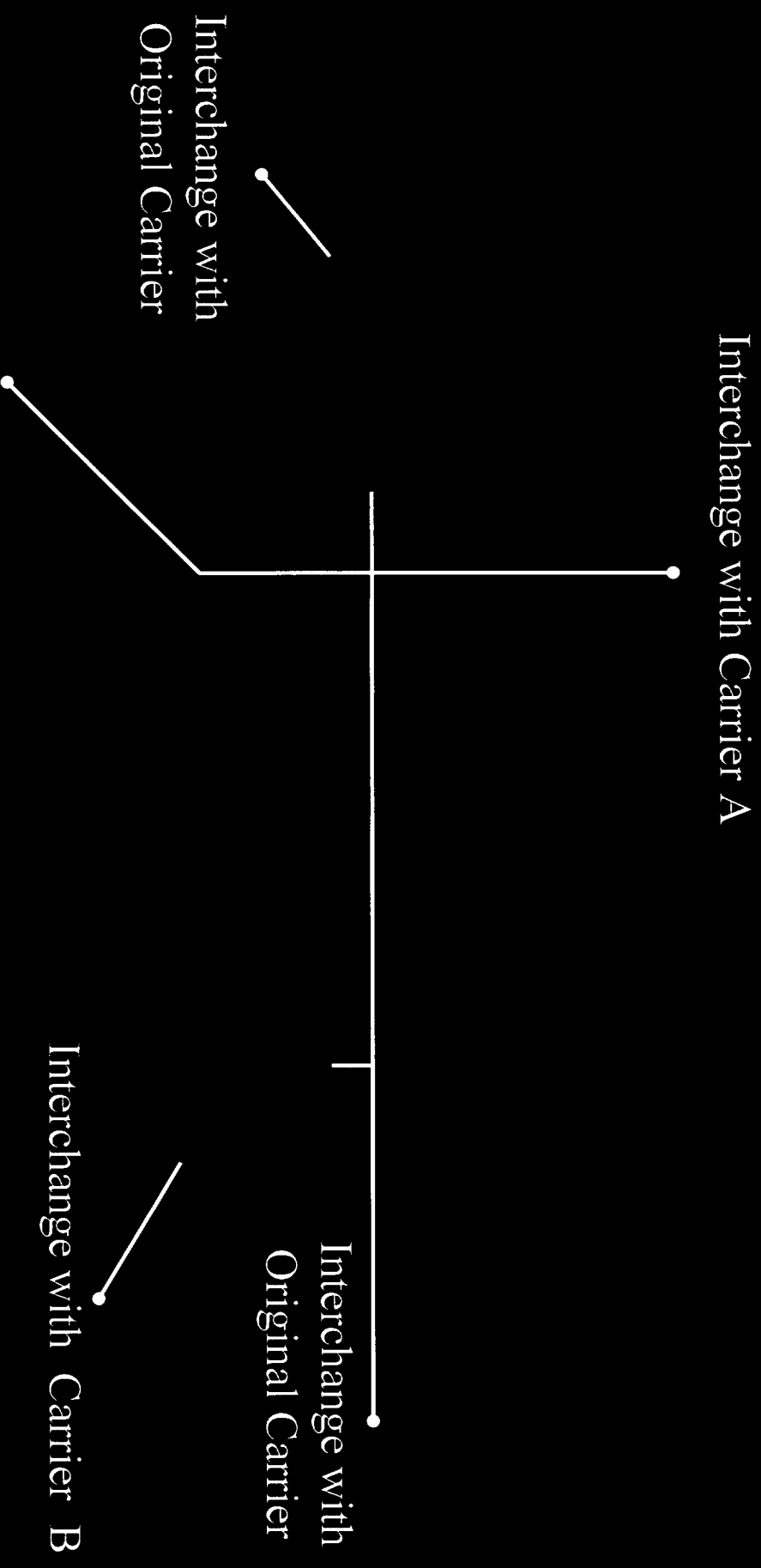


Interchange with
Original Carrier

Interchange with Carrier B



Secondary Abandonment

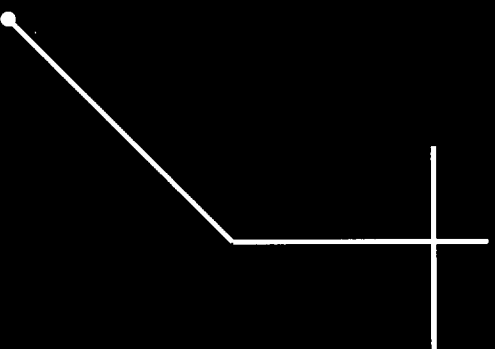


Final Network

Interchange with Carrier A



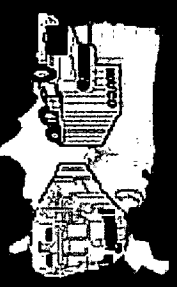
Interchange with
Original Carrier



Interchange with
Original Carrier



Interchange with Carrier B



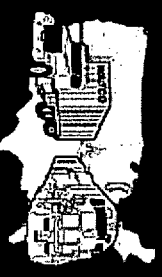
Sample network

- This example shows a smaller network that:
 - ◇ Is reduced over time eliminating real opportunities for OFA's
 - ◇ Cannot offer value for short haul traffic



Reporting paper barriers in filings could mitigate future questions

- STB should consider requiring the reporting of paper barriers in the initial exemption notice that creates a new rail carrier or allows additional track to be acquired.
- ◇ Information could be gathered to understand the value of entire transaction
- ◇ Further study and a specific STB hearing is warranted for this concept



Summary

- Government should let the market work
- Paper barriers are an important part of our industry
- Paper barriers are evolving with the help of the RIWG
- Good and accurate information is what is needed on future transactions

