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September 8, 2004

VIA HAND DELIVERY

The Honorable Vernon A. Williams
Secretary
Surface Transportation Board
1925 K Street, N.W., Suite 715
Washington, DC 20423-0001

ENTERED
Office of Proceedings

SEP 08 2004

U.S. OF
TRANSPORTATION



**RE: Finance Docket No. 34509, Kaw River Railroad, Inc. -- Lease
Exemption -- The Kansas City Southern Railway Company**

Dear Secretary Williams:

Attached for filing are the original and ten copies of the Reply To Supplemental Petitions To Revoke and Motion To Strike.

Please time and date stamp the extra copy of the Reply and return it with our messenger.

If you have any questions, please contact me.

Sincerely yours,

Karl Morell
Karl Morell

Enclosures

ORIGINAL

BEFORE THE
SURFACE TRANSPORTATION BOARD

FINANCE DOCKET NO. 34509

KAW RIVER RAILROAD, INC.
--LEASE EXEMPTION--
THE KANSAS CITY SOUTHERN RAILWAY COMPANY

REPLY TO SUPPLEMENTAL PETITIONS TO REVOKE
AND MOTION TO STRIKE



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Dated: September 8, 2004

BEFORE THE
SURFACE TRANSPORTATION BOARD

FINANCE DOCKET NO. 34509

KAW RIVER RAILROAD, INC.
--LEASE EXEMPTION--
THE KANSAS CITY SOUTHERN RAILWAY COMPANY

REPLY TO SUPPLEMENTAL PETITIONS TO REVOKE
AND MOTION TO STRIKE



The Kaw River Railroad, Inc. ("KRR"), hereby replies in opposition to the Supplemental Petitions To Revoke ("Supplemental Petitions") filed separately by the Brotherhood of Locomotive Engineers & Trainmen, a Division of the Rail Conference, International Brotherhood of Teamsters ("BLET") and by the United Transportation Union ("UTU"), on August 16, 2004 (collectively, the "Unions"). KRR also moves to strike portions of BLET's Supplemental Petition.

BACKGROUND

On May 25, 2004, KRR filed its Notice of Exemption, pursuant to 49 C.F.R. Part 1150, Subpart D—Exempt Transactions, to permit KRR: (1) to lease from The Kansas City Southern Railway Company ("KCS") and operate approximately 7.5 miles of rail lines in Kansas City, KS; (2) to sublease from KCS and operate approximately 4.5 miles of rail lines in Kansas City, KS and Kansas City, MO, that are owned by Kansas City Terminal Railway Company ("KCT");

and (3) to acquire by assignment from KCS operating authority over approximately 6.2 miles of rail lines owned by KCT.

On May 27, 2004, BLET filed a petition for stay to which KRR and KCS responded. By decision served May 28, 2004, the stay request was denied. In denying the stay request, the Chairman noted that:

[T]he record indicates that some of the trackage over which KRR would operate is KCS main line trackage and, therefore, is a line of railroad subject to the Board's exclusive jurisdiction and regulatory authority.

As proposed by KRR, the transaction would entail a new operation by a new carrier. Because the new operation would constitute KRR's entire line of railroad, and KRR would be holding out service to the public, it must seek authority ... to provide it.

Decision served May 28, 2004, slip op. at 2 ("Stay Decision"). The exemption became effective and KRR commenced operations on June 1, 2004.

On June 4 and 14, 2004, respectively, BLET and UTU filed Petitions to revoke the exemption pursuant to 49 C.F.R. Part 1121. Simultaneously, the Unions requested the production of the following documents: (1) all leases and other written arrangements between KRR, KCS and KCT, including the leases and other arrangements between KCS and KCT that bear upon the KRR leases and operations; (2) the Track Lease and Switching Maintenance Agreement, dated December 15, 1992; and (3) the Operating Agreement, dated June 12, 1909, as amended. KRR replied to the Petitions to revoke on June 24, 2004 and produced the requested documents on July 1, 2004.

MOTION TO STRIKE

Section 1121.3(c), requires a party seeking to revoke a notice of exemption to "provide all of its supporting information at the time it files its petition." A supplemental petition, which

is permitted if discovery is sought under Section 1121.2, may only contain the information obtained through discovery. 49 C.F.R. § 1121.3(c). UTU is in compliance with this rule since its Supplemental Petition is confined to a discussion of the agreements KRR produced to the Unions. BLET's Supplemental Petition, however, virtually ignores the discovery material and consists almost entirely of arguments and factual allegations that were neither contained in its Petition nor have any grounding in the documents produced during discovery. Moreover, except for a brief mention of the discovery documents, virtually all of the facts relied on by BLET in the Supplemental Petition were, or should have been, available to BLET on June 4th, when it filed its Petition to Revoke. For example, BLET attaches a KCS news release dated June 1, 2004, and a KCS Terminal Notice dated May 26, 2004. Similarly, the three Verified Statements attached to the Supplemental Petition rely exclusively on information that predates the filing of the initial Petition.

BLET commenced this revocation proceeding and controlled the timing of its initial filing. More importantly, all of the statutes, case law and factual material (except for the discovery documents) relied on by BLET in the Supplemental Petition existed at the time it filed its initial Petition. By interjecting this preexisting material at the supplemental stage, BLET is flouting the Board's rules governing revocation cases. In the interest of fairness, administrative efficiency, and compliance with the Board's rules, all portions of the Supplemental Petition not addressing the discovery documents should be stricken from the record.

REPLY

The gravamen of the BLET's Supplemental Petition is that the tracks at issue in this proceeding are switching tracks and, therefore, excepted from the Board's entry jurisdiction under Section 10906. The jurisdictional status of the KCT tracks at issue in this proceeding has

already been addressed by the Board's predecessor, the Interstate Commerce Commission ("ICC"). In 1993, Gateway Western Railway Company ("GWR"), which was subsequently acquired by KCS, filed a joint petition with KCT and The Atchison, Topeka and Santa Fe Railway Company ("ATSF"), seeking approval for ATSF to lease certain KCT main line and connecting tracks and for GWR to lease 25.68 miles of KCT's switch and yard tracks. Included in the 25.68 miles of switch and yard tracks are the KCT tracks being subleased by KRR. In granting the joint petition, the ICC considered *sua sponte* whether the trackage now being subleased by KRR was subject to the exception of former Section 10907, now Section 10906. The ICC concluded that the lease of this trackage did not fall within the exception of former Section 10907 and, therefore, was subject to the ICC's licensing jurisdiction. Finance Docket No. 32238, *The Atchison, Topeka and Santa Fe Railway Company and Gateway Western Railway Company – Lease Exemption – Kansas City Terminal Railway Company* (not printed), served February 24, 1994. It logically follows that, since the lease of the KCT switching tracks by GWR in 1994 was a transaction subject to ICC approval, the sublease of a portion of that same trackage by KRR is a transaction now subject to Board approval.

In granting GWR's lease of the tracks, the ICC noted that GWR had agreed "to provide the same switching service currently performed by KCT, without discrimination, to maintain all of covered KCT's switching and yard tracks at their current maintenance levels, and to make upgrades when requested by KCT." *Id.*, slip op., at 4-5. In Article II of the Track Sub-Lease and Switching and Maintenance Agreement KCT Trackage ("Track Sub-Lease Agreement"), KRR agreed to provide the same services KCS assumed from KCT in 1994.¹ In fact, the arrangement

¹ A copy of the Track Sub-Lease Agreement is attached as Exhibit B to UTU's Supplemental Petition.

between KRR and KCS is modeled largely after the arrangement between KCS and KCT that was approved by the ICC in 1994.²

The Unions' requests to revoke the exemption in this proceeding are fundamentally flawed in two respects. First, BLET misconstrues the law governing the Board's jurisdiction over the use of one carrier's track by a new or existing carrier, while UTU simply ignores the governing law. Second, both BLET and UTU misinterpret the transaction between KRR and KCS.

As the Stay Decision points out, KRR obtained operating authority over approximately 6.2 miles of main line track. The other KCT rail lines KRR is subleasing have already been found not to constitute excepted track under Section 10906. Even if some of the trackage being leased from KCS constituted excepted yard or switching trackage for KCS, the appropriate focus is not on KCS's past use, but KRR's intended use. As KRR previously noted, in determining whether a particular track segment is excepted from Board jurisdiction pursuant to Section 10906, the courts, the Board and the ICC focused on the intended use of the track and not on the nomenclature used by a party in describing the track or the use of the track by the prior operator. *Nicholson v. ICC*, 711 F.2d 364 (D.C. Cir. 1983), *cert. denied*, 464 U.S. 1056 (1984) ("Nicholson"); Docket No. 33323, *Chicago Rail Link, L.L.C. – Lease and Operation Exemption – Union Pacific Railroad Company* (not printed), served September 2, 1997 ("CRL-UP"), *aff'd sub nom. United Transportation Union v. STB*, 169 F.3d 474 (7th Cir. 1999) ("CRL"); *Brotherhood of Locomotive Eng'rs v. STB*, 101 F.3d 718 (D.C. Cir. 1996) ("BLE v. STB"); Finance Docket No. 32394, *Brotherhood of Locomotive Engineers v. Union Pacific Railroad*

² The construction, lease and operation of rail lines in the KCT terminal area by KCT and its various owning railroads were found subject to ICC jurisdiction on a number of other occasions. See e.g., *Kansas City Term. Ry. Co. Construction*, 175 I.C.C. 391 (1931); *Chicago, M., St. P. & P.R. Co. Trustees Construction*, 252 I.C.C. 49 (1941).

Company and Iowa Interstate Railroad (not printed), served November 6, 1995; *Effingham RR Co. – Pet. For Declaratory Order*, 2 S.T.B. 606 (1997)(“*Effingham*”), *aff’d sub nom. United Transp. Union v. STB*, 183 F.3d 606 (7th Cir. 1999).

Under the Board’s now well established intended use test, the jurisdictional status of leased track is determined, not by its historic character or use, but by the tenant’s intended use in the context of the larger purpose and effect of the transaction. In *BLE v. STB*, at 728, the intended use test was affirmed, subject to the qualification that the focus on use must not obscure “the larger purpose and effect of the transaction at issue.” As KRR previously explained, it will continue to perform certain switching operations on the involved rail lines. KRR, however, will also utilize the involved rail lines to serve new shippers and interchange traffic with at least three Class I railroads. Thus, the trackage, in KRR’s hands, will constitute “an extended or additional railroad line” under Section 10901 and not switching track excepted from the Board’s licensing jurisdiction under Section 10906. Even if one classifies KRR’s operations as “switching operations”, as BLET repeatedly does, the transaction would still be subject to the Board’s jurisdiction under Section 10901 if KRR were able to reach new territory. *BLE v. STB*, at 728 (“[I]f those switching operations have the effect of substantially extending the tenant railroads’ lines into new territory, then the Commission may not decline jurisdiction”).

The intended use test has its genesis in *Texas & Pac. Ry. Co. v. Gulf, Colo. & S.F. Ry.*, 270 U.S. 266, 278 (1926) (“*Texas & Pacific*”), where the Court held that:

If the purpose and effect of the new trackage is to extend substantially the line of a carrier into new territory, the proposed trackage constitutes an extension of the railroad ... although the line be short and although the character of the service contemplated be that commonly rendered to industries by means of spurs or industrial tracks. (Emphasis added).

BLET apparently does not take issue with the Supreme Court's holding in *Texas & Pacific*. BLET suggests, however, that the Board has misinterpreted the Court's holding in *Texas & Pacific* by adopting an "entire line" theory in *Effingham* and several other cited cases. Contrary to BLET's contentions, the so-called "entire line" theory is a necessary and logical extension of the holding in *Texas & Pacific* when focusing, as in this proceeding, on the lease of trackage by a new carrier. For an existing carrier, the appropriate focus is on the line the carrier is seeking to construct, acquire or lease to determine whether that new line enables the carrier to access new shippers. For a new carrier the focus is identical: namely the line it seeks to construct, acquire or lease, which line, of course, by definition will constitute the new carrier's "entire line".

In *Effingham*, the Board, citing *BLE v. STB*, noted that:

we may not allow the focus on use to obscure the larger purpose and effect of the transaction. According to the court, while we may focus on the tenant railroad's use of the tracks solely for switching operations as the controlling factor in determining the track's character, if those switching operations have the effect of substantially extending the tenant railroad's lines into new territory, then we may not decline jurisdiction.

Effingham, at 609. Even if, as BLET suggests, some of the trackage being leased and subleased can be characterized as switching tracks and KRR's use of those tracks is for switching operations, the Board may not decline jurisdiction because, as in *Effingham*, KRR's operations have the effect of substantially extending its operations into new territory.

In summary, the strict application of the holding in *Texas & Pacific* to the facts of this proceeding inescapably leads to only one conclusion: the lease of the KCS lines, and the sublease of, and acquisition of operating rights over, the KCT lines by KRR is a transaction subject to the Board's jurisdiction under Section 10901. KRR will use these lines collectively to reach into

new territory and deliver freight to or from numerous shippers located along the lines. While some of lines may have constituted excepted track for KCS, in KRR's hands, all of the rail lines are jurisdictional for purposes of Section 10901. KRR's operations are no different than the hundreds of shortline operations the Board and its predecessor have authorized under Section 10901. Like numerous other small railroads, KRR serves as the bridge carrier between the local customers on the KRR lines and three of the Class I carriers that operate in the area.

Ironically, BLET seeks to apply the "intended use" test to the KCT main line over which KRR obtained operating authority arguing that, in KRR's hands, this track is excepted track because KRR has no through trains. Although unclear, it appears that BLET would deem a particular segment of rail line as a main line only if the owning or leasing carrier owned or leased adjoining mainline tracks so that the segment at issue could be used for through movements. If that is BLET's position, it is both logically and legally faulty. KRR utilizes the KCT main line to serve several of the shippers in the area. For example, one of the new shippers KRR was able to locate on the leased tracks, which shipper was not previously served by KCS, receives its shipments in the 12th Street Yard. The inbound traffic is originated by KCS and moved by KCS to the Millstreet Yard. In order to deliver the traffic to the new shipper, KRR must interchange with KCS at Millstreet Yard and then traverse the KCT main line running between the Millstreet Yard and the 12th Street Yard in order to deliver the freight to the customer. In *International-G. N. R. Co. Trustee Trackage Rights*, 275 I.C.C. 27, 37 (1949), the ICC found trackage rights over approximately 1,061 feet of main line track to be jurisdictional, and not switching track, because the tenant carrier's use of the track was an "integral link of a through movement in foreign commerce" even though the cars were handled by a terminal switch engine and the traffic was moved by the tenant for a very short distance. For KRR, the 6.2 miles of KCT main line serves a

similar purpose: providing an integral link for through movements in interstate commerce between the local shippers and KRR's Class I connections.

BLET also argues that the intended use test should not be applied in this proceeding because KRR will not be serving "new" shippers, since the shippers are all former KCS customers. Again, BLET is legally and factually mistaken. In its Notice, KRR specifically identifies some of the new customers KRR will be serving: Procter and Gamble, Meridian Rail, Total Distribution, Ace Pallet, Thomas & Associates Wholesale Lumber, Inland Containers, KC Hardwood, KC Railcar, Colgate Palmolive, Kaw River Shredding, Kansas City Star, Constar Plastics, and Darling. While these shippers were formerly served by KCS, they nevertheless are new customers for KRR. The Board and the courts do not look to see if the customers are new to the rail industry but rather whether they are new to the tenant railroad. The petitioner in *CRL* made the identical argument which was rejected by the court. In so doing, the court upheld the Board's finding that the lease of UP yard track in Chicago was subject to the Board's jurisdiction under Section 10902, and did not constitute excepted track under Section 10906, because the tenant was able to serve two "new" shippers.³ Those two "new" shippers in *CRL* were former customers of UP but, as is the case here, new to the tenant railroad.

Moreover, since it commenced operations, KRR has been successful in attracting two new customers, DaVinci Roofing Materials and Express Sand & Gravel, which were not formerly served by KCS. Consequently, KRR's operations satisfy even BLET's mistaken interpretation of the "intended use" test.

³ In applying the intended use test, the Board found that it was not determinative that the yard track at issue had not been used previously as, or did not otherwise contain, "through lines" for line-haul service. Instead, finding that the tenant carrier would use the track to expand its operations and serve new shippers, the Board determined that, in the tenant's hands, the leased track is "extended or additional rail line" within Section 10902, not yard or switching track excepted from the Board's jurisdiction under Section 10906. *CRL-UP*, slip op. at 5.

UTU argues that KRR's Notice of Exemption is misleading based on its reading of a few selective provisions in the Track Lease between KRR and KCS ("Track Lease"), the Track Sub-Lease Agreement, and the Short Term Locomotive Lease Agreement between KRR and KCS ("Locomotive Lease").⁴ BLET, on the other hand, reads the agreements as substituting KRR for KCS "in the performance of switching in the Kansas City terminal." BLET Supplemental Petition at 11. As explained below, the arrangement between KRR, KCS and KCT is no different than the numerous shortline spin offs that the Board and its predecessor have consistently authorized under either Section 10901 or Section 10902 during the past two decades. The various provisions the Unions cite are quite common in agreements between Class I railroads and their shortline partners, particularly in transactions involving the lease, rather than the sale, of rail lines.

KRR's Notice of Exemption complies fully with the governing rules and provides all of the information required under 49 C.F.R. § 1150.33-34. UTU has failed to introduce any evidence to show that KRR's Notice contains false or misleading information. Thus, UTU's request for rejection of the Notice is unwarranted. Contrary to the Unions' contention, the involved transaction is not a sham nor was it entered into with the purpose or effect of harming employees. This transaction is similar to the countless other lease transactions between Class I railroads and new shortline operators. *See e.g.*, STB Finance Docket No. 33960, *Central Illinois Railroad – Lease and Operation Exemption – Lines of The Burlington Northern and Santa Fe Railway Company at Chicago, Cook County, Il* (not printed), served September 12, 2002 ("Central Illinois"); and STB Finance Docket No. 32766, *Portland & Western Railroad, Inc. –*

⁴ The Track Lease and Locomotive Lease are attached to UTU's Supplemental Petition respectively as Exhibit A and Exhibit C.

Lease and Operation Exemption – Lines of Burlington Northern Railroad Company (not printed), served October 15, 1997 (“*Portland & Western*”).

The Unions point out that, under the agreements between KRR and KCS, the cars remain in KCS’s account, that KCS pays car hire,⁵ and that KRR is temporarily leasing a KCS locomotive. The Board was faced with a similar arrangement in *Central Illinois*, but nevertheless concluded that the lease of the tracks was not a sham transaction. In so doing, the Board noted that the tenant carrier was an independent corporate entity that is not affiliated with the landlord and that the lease arrangement was an arm’s-length transaction, as is the case in this proceeding. Moreover, keeping cars in the Class I railroad’s account, providing car-hire relief and inter-carrier locomotive leases are fairly standard practices in the industry and do not detract from KRR’s independence. Rather, keeping the cars in KCS’s account reduces KRR’s operating costs, eliminates an otherwise duplicative function, and retains in KCS a function that KCS is able to provide in a more cost effective manner.

The Unions also cite to provisions in the agreements whereby KRR agreed to minimum service levels⁶ and KCS controls the rates. In STB Finance Docket No. 33561, *Port of Pend Oreille d/b/a Pend Oreille Valley Railroad – Acquisition and Operation Exemption – The Burlington Northern and Santa Fe Railway Company* (not printed), served October 23, 1998, reconsideration denied in decision served May 2, 2000, the Board found an arrangement between a Class I and a shortline carrier to be arm’s length even though the Class I retained the ability to

⁵ If KRR does not deliver a requested car in need of repair to KCS within 48 hours of the request, the car will transfer to KRR’s car hire account and remain in KRR’s account until the car is delivered. Article II (C)(5).

⁶ In the Track Lease, KRR agreed to provide, at a minimum, the level of service previously provided by KCS. The service levels vary from customer to customer and range from an as needed basis to 7-day-a-week service. See Article VI (B) and Attachment B to the Track Lease. It is hardly unusual for a Class I railroad leasing its track to a new carrier to require specified minimum service levels.

set the rates, mandated certain minimum service levels, and supplied all cars. *See also Portland & Western*. The ability of KCS to set the through rates is quite common in the shortline industry and provides substantial benefits to both carriers and their customers. KRR benefits by not having to provide an extensive national marketing department and can rely on KCS's national coverage to market KRR's local services. The local customers on KRR's lines also benefit, since they will have to deal with only a single entity in negotiating rates on traffic moving to and from their facilities.

UTU considers it noteworthy that all inbound traffic will be received by KCS in the same blocking as before the transaction and that KCS retained the right to repair its own signals, grade crossing protections and communications systems. UTU fails to explain, however, why maintaining the status quo as to train blocking and certain repair work renders the transaction a sham. In any event, the Track Lease provides that changes to the blocking will be made over time by mutual agreement of the parties so as to better serve the customers in the area and that KRR has assumed the responsibilities of maintaining the leased and subleased rail lines. Track Lease, at Article II (B)(3) and (4).

UTU also cites to Article V of the Track Lease in support of its contention that the transaction is a sham. Article V, however, simply provides the method by which KCS can seek to have an unsafe KRR employee removed from the leased and subleased trackage. This type of provision is contained in virtually all trackage rights and lease agreements in order to enable the landlord carrier to remove unsafe employees of the tenant carrier. *See e.g., Exhibit B, Section 2.15, of the Temporary Trackage Rights Agreement filed with the Board in STB Finance Docket No. 34494, The Burlington Northern and Santa Fe Railway Company – Temporary Trackage Rights – Union Pacific Railroad Company – Kansas City, Mo to Falls City, NE.*

The Unions also find significance in the fact that KRR will maintain records in KCS's MCS System. The purpose of these records is to maintain an accurate count of the cars handled by KRR, since KRR is compensated on a per car basis. KRR's use of KCS's System substantially reduces KRR's information technology and accounting costs.

UTU further notes that KRR is responsible for providing KCS with daily car inspection repair reports pursuant to Article II (C)(4) of the Track Sublease Agreement. Because the cars remain in KCS's account for purposes of car hire, any repairs to the cars by KRR must necessarily be billed through KCS. UTU incorrectly contends that, pursuant to the Track Lease, the arrangement between KRR and KCS was "conditioned upon whether or not it will be necessary to obtain a labor contract agreement from the affected labor crafts...." UTU Supplemental Petition at 3. Article IX of the Track Lease simply provides that, if a labor contract agreement is deemed necessary, the Track Lease Agreement will not become effective until such approval is obtained. As indicated by KCS in its Reply to the Stay Request, no such labor agreement was necessary for this transaction to go forward.

BLET claims that KRR pays no rent⁷ and that instead KCS pays KRR on a per car basis and that KCS retains the right to operate over the leased tracks. These same two arrangements, as well as others cited by the Unions, existed in *Portland & Western*. In reviewing a lease arrangement that was significantly more restrictive than the arrangement between KRR and KCS, the Board noted that:

The lease provisions do for all practical purposes require PWR to route its traffic over BN. But these provisions do not reduce the level of competition that existed in this market before the lease

⁷ The annual rent paid by KRR is contained only in the Highly Confidential version of the documents produced to BLET. BLET's attempt to reveal that information in a public filing before the Board is a violation of the Protective Order issued by the Board in this proceeding on June 18, 2004.

since BN was free to route the traffic it originates over its own lines. The Board and the Interstate Commerce Commission have consistently held that carriers are not obligated to increase the existing level of competition when they undertake sale or lease transactions such as this one.

Portland & Western, slip op. at 6.⁸

The various terms of the agreements between KRR and KCS that the Unions claim are illustrative of a sham transaction have been found by the Board and the ICC to be acceptable in similar transactions. For example, the ICC and the Board have approved transactions which: (1) set the maximum amount of revenues the shortline can assess per car as its charge to the connecting carrier; (2) provide for rail line lease payments calculated on a per car basis; (3) allow a Class I rail carrier to obtain a certain percentage of a shortline's operating revenues; (4) authorize a Class I rail carrier to appear as the only carrier in the route in waybills covering shipments to and from points located on a shoreline when the shoreline is receiving a per car fee from the Class I and not a division of the rate; and (5) allow commercial coordination between the shortline and Class I carrier, where the shortline is not involved in the long-haul. *Minnesota Comm. Ry., Inc. – Trackage Exempt. – BN RR. Co.*, 8 I.C.C.2d 31 (1991)(“*Minnesota Comm.*”).

UTU argues that, under the arrangement between KRR and KCS, nothing changes other than KRR's name replaces that of KCS's and the employees of KRR replace those of KCS. In confronting this identical argument, the ICC explained:

[E]ven if UTU were correct that [the tenant carrier] has replaced [the landlord carrier], this would not show any reduction in

⁸ The lease in *Portland & Western* required only nominal rental payment by the tenant, effectively prohibited the tenant from interlining with another connecting Class I carrier, gave the landlord carrier control over the tenant's rates, retained the right of the landlord to operate certain trains over the leased lines, required the tenant to provide certain minimum service levels, provided for a per car payment by the landlord to the tenant carrier, authorized the landlord carrier to control the interline marketing programs of the tenant, and entitled the landlord carrier to handle all claims for loss and damage.

competition from the situation prior to the agreement. In fact, the number of competitors would be the same, but an aggressive, responsive competitor would have replaced an older, more rigidly stratified one.

Minnesota Comm., at 39.

Provisions of the Track Lease not mentioned by the Unions which demonstrate the independence of KRR include: (1) the requirement that “KRR shall furnish and be responsible for all equipment, switch engines or engines, switch crews and other employees, fuel, water, supplies, and other incidentals in the management, supervision and performance of the [repair] services” (Article II (B)(4)); (2) “KRR shall have the exclusive direction and control of the Switching Services performed on the Leased Trackage and KRR shall be solely responsible for scheduling and overseeing the Switching Services and Switching Maintenance Work, for the degree of care with which the Switching Services and the Switching Maintenance Work is performed, and for the quality of the results of the Switching Services and the Switching Maintenance Work” (Article II (C)); (3) “KRR shall perform the Switching Services and the Switching Maintenance Work in a fair and impartial manner” (Article II (D)); (4) “KRR shall use, for the interchange of cars, those portions of the Leased Trackage currently identified and designated for interchange, and such other portions of the Leased Trackage as KRR and other carriers agree to use for interchange” (Article VI (B)); (5) “Interchange practices will be subject to discussion and review between KRR and other carriers pursuant to an assurance of efficient operating practices and quality service to customers” (Article VI (G)); and (6) “KRR shall be responsible for all losses or damages in any way arising from, growing out of or connected with [the services provided by KRR]” Article X (B).

The above-noted provisions are also contained in the Track Sub-Lease Agreement. That Agreement also provides that “KRR shall ... [p]erform transfer services between Mill Street

Yard and KCS, [BNSF], [UP] and other railroads as required from time to time, and supply at its cost and be responsible for all equipment, switch engine or engines, switch crews and other employees, fuel, water [and] supplies” Article II (B)(2).

These and other provisions of the agreements demonstrate that KRR is not an agent or lackey of KCS nor is the arrangement among KRR, KCS and KCT a sham.

Unlike the situations in *Burlington Northern R. Co. v. United Transp. Union*, 862 F.2d 1266 (7th Cir. 1988); and Finance Docket No. 32523, *Sagamore National Corporation – Acquisition and Operation Exemption – Lines of Indiana Hi-Rail Corporation* (not printed), served October 28, 1994, KRR is a company independent of KCS and has no affiliation or relationship to KCS, operating under its own name and utilizing its own employees, management and equipment. KRR is responsible for its day-to-day operations on the leased and sub-leased rail lines and any resulting profit or loss. While BLET is correct that the shippers in the area look to KCS and the other Class I connections for car supply and rates for the overall movements, these same customers now view KRR as the originating or terminating carrier for their traffic. KRR meets independently with the existing local customers to discuss service needs and markets new customers in its own name. Moreover, virtually all shortline railroads are dependent on their Class I connections for car supply. BLET is also correct in noting that KRR makes up the trains for KCS. KRR, however, also makes up the trains for UP and is permitted under the agreements to make up trains for BNSF.

BLET argues, alternatively, that, if KRR’s Notice of Exemption is not rejected, the exemption should be revoked to carry out the rail transportation policy. The standard for revoking an exemption is whether regulation is needed to carry out the rail transportation policy of Section 10101. 49 U.S.C. § 10502(d). Petitions to revoke must be based on reasonable,

specific concerns demonstrating that reconsideration of the exemption is warranted. *Minnesota Comm.*, at 35-36; *Portland & Western*; Finance Docket No. 31617, *Chesapeake & Albemarle R. Co. – Lease, Acq. & Oper. Exemp. – Southern Ry. Co.* (not printed), served September 19, 1991; Finance Docket No. 31102, *Wisconsin Central Ltd. – Exemp. Acq. & Oper. – Certain Lines of Soo L.R. Co.* (not printed), served July 28, 1988.

The party seeking revocation of an exemption has the burden of proving that regulation of the transaction is necessary. *Id.* Here, BLET has simply come forward with unsupported and unsupportable assertions that revocation is necessary to carry out the national transportation policy. Because BLET has submitted no evidence in support of its assertions, it has failed to meet its burden of proof and its Petition, as supplemented, must be denied.

Where, as here, an exemption has become effective, a revocation request is treated as a petition to reopen and revoke and, under 49 C.F.R. § 1115.3(b), must state in detail whether revocation is supported by material error, new evidence, or substantially changed circumstances. BLET has failed to address these standards much less introduce any evidence to warrant a finding favorable to BLET under these standards.

Moreover, the Board's analysis focuses on the sections of the rail transportation policy that are related to the underlying statutory section from which the exemption was granted. *Minnesota Comm.*, at 36. The Board does not revoke exemptions "because a section of the [rail transportation policy] *unrelated* to the underlying section of the statute requires revocation." *Id.*, at 37. In addition, the Board does not extend its analysis beyond the issues that it would address in an application proceeding. *Id.*, at 36-37.

BLET quotes one section of the rail transportation policy, 49 U.S.C. § 10101(11), which encourages fair wages and safe and suitable working conditions in the railroad industry. BLET,

however, fails to explain: (1) why that section compels the revocation of the exemption in this proceeding; (2) the relevance of that section to Section 10901, the underlying section of the statute; and (3) the manner in which the involved transaction produces unfair wages or unsafe working conditions. BLET asserts that the involved transaction has resulted in a loss of 18 jobs on the KCS. KRR understands that no employee of KCS is unemployed as a result of this transaction. Moreover, BLET neglects to address, and appears unsympathetic to, the impact revocation would have on KRR employees.

Granting BLET's request would require KRR to file an individual petition for exemption under Section 10502 or an application for the lease and sublease of the rail lines under Section 10901. Under Section 10901, the Board would be required to grant the application unless it finds that the lease and sublease of the KCS and KCT lines by KRR is inconsistent with the public convenience and necessity. Transactions initiated under Section 10901 were deemed by Congress to be consistent with the public convenience and necessity unless shown to be otherwise. In any event, BLET fails to explain the manner in which this transaction is inconsistent with the public convenience and necessity. Moreover, the Board may not impose labor protection in a Section 10901 transaction. 49 U.S.C. § 10901(c). Consequently, granting BLET's request would serve no useful purpose. KRR would be forced to incur the significant expense of filing a petition for exemption or application. In all other respects, however, the parties and the Board would simply come full circle to the same result. It is inconceivable that the Unions could demonstrate that this transaction is inconsistent with the public convenience and necessity and the Board is powerless to impose labor protection in a filing under Section 10901.

The transaction involved in this proceeding is the very type of procompetitive transaction that the Board and the ICC have repeatedly endorsed and affirmed. As the ICC noted:

[I]t has been our experience with transactions of this type that the acquiring firm will bring new vitality to the line. Typically, the new operator has closer ties to local communities and will provide better service, often at lower rates, and will work closely with shippers on the line.

Finance Docket No. 31089, *Montana Rail Link, Inc. - Exemption Acquisition and Operation - Certain Lines of Burlington Northern Railroad Company* (not printed), slip op. at 21, served May 26, 1988. As a locally based carrier, KRR will be able to provide more efficient, economical and attentive service to the customers on the leased and subleased lines. To the extent KRR's services are more efficient and economical, the transaction will lead to improved service at lower rates for existing and potential shippers.

CONCLUSION

KRR respectfully urges the Board to deny the Petitions, as supplemented, for failing to meet the revocation standards set forth in 49 U.S.C. § 10502(d). The Unions have presented no facts or arguments that meet the Board's revocation standard or that otherwise warrant the revocation of the exemption in this proceeding.

Respectfully submitted,



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Dated: September 8, 2004

CERTIFICATE OF SERVICE

I hereby certify that on this 8th day of September, 2004, I have caused a copy of the foregoing Reply to Supplemental Petitions To Revoke And Motion To Strike to be served on all parties of record in this proceeding.

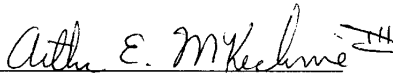
A handwritten signature in cursive script, reading "Karl Morell", is written over a horizontal line.

Karl Morell

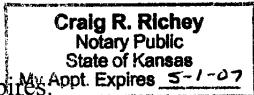
VERIFICATION

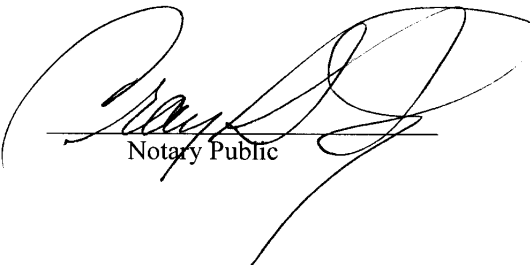
STATE OF KANSAS)
)
COUNTY OF CRAWFORD) ss.

I, Arthur E. McKechnie III, being duly sworn depose and state that I am Assistant Secretary of Kaw River Railroad, Inc., that I am authorized to make this verification, and that I have read the foregoing Reply To Supplemental Petitions and know the facts asserted therein are true and accurate to the best of my knowledge, information, and belief.


Arthur E. McKechnie III

SUBSCRIBED AND SWORN TO before me this 24 day of September, 2004, in the County of Crawford, State of Kansas.

My Commission Expires 


Notary Public