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ORIGINAL

AUG 3 2005

RECEIVED

August 3, 2005

BY HAND

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

ENTERED
Office of Proceedings

AUG 03 2005

Part of
Public Record

RE: STB Docket No. AB-441 (Sub-No. 4X), San Pedro
Railroad Operating Company, LLC-Abandonment
Exemption-In Cochise County, AZ,

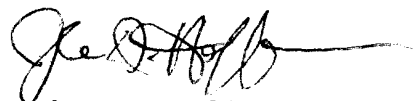
Dear Mr. Williams:

On behalf of San Pedro Railroad Operating Company (SPROC), I am enclosing for filing in the above-captioned proceeding an original and ten copies of its Reply to the "Statement of Chemical Lime Company in Opposition To San Pedro Railroad Operating Company's Petition for Exemption." for abandonment of a rail line

I am also enclosing a copy of this filing on a disk formatted in MS Word.

Please date stamp and return one copy of this letter and Reply.

Sincerely yours,



John D. Heffner
Counsel for SPROC

Enclosures:

cc: Mr. David L. Parkinson
All parties

ORIGINAL

BEFORE THE
SURFACE TRANSPORTATION BOARD

AUG 3 2005
RECEIVED

STB DOCKET NO. AB-441 (Sub-No. 4X)
SAN PEDRO RAILROAD OPERATING
COMPANY, LLC-ABANDONMENT EXEMPTION-
IN COCHISE COUNTY, AZ

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PETITION FOR EXEMPTION
UNDER 49 U.S.C. 10502
FROM 49 U.S.C. 10903

REPLY OF
SAN PEDRO RAILROAD OPERATING COMPANY, LLC
TO CHEMICAL LIME COMPANY'S STATEMENT IN OPPOSITION

John D. Heffner
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Attorney for San Pedro
Railroad Operating
Company, LLC

Dated: August 3, 2005

BEFORE THE
SURFACE TRANSPORTATION BOARD

STB DOCKET NO. AB-441 (Sub-No. 4X)
SAN PEDRO RAILROAD OPERATING
COMPANY, LLC—ABANDONMENT EXEMPTION—
IN COCHISE COUNTY, AZ

PETITION FOR EXEMPTION
UNDER 49 U.S.C. 10502
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REPLY OF
SAN PEDRO RAILROAD OPERATING COMPANY, LLC
TO CHEMICAL LIME COMPANY'S STATEMENT IN OPPOSITION

INTRODUCTION

Pursuant to the Board's decision served July 28, 2004, San Pedro Rail Operating Company ("SPROC") submits this Reply to Chemical Lime's Statement in Opposition dated July 14, 2005. SPROC has shown that its request to abandon the subject rail line meets both the exemption criteria of 49 U.S.C. 10502 and the formal public convenience and necessity standard of 49 U.S.C. 10903 and that the subject abandonment should be granted.

BACKGROUND

On June 6, 2005, SPROC filed a Petition for Exemption with the Board under 49 U.S.C. 10502 to abandon approximately 76.2 miles of railroad track and right of way south of milepost 1040.15 at Curtiss, AZ, and extending

through Paul Spur to Douglas, in Cochise County, AZ.¹

SPROC had acquired these lines from SWKR Operating Company, a short line subsidiary of RailAmerica, Inc., in 2003.

Each of the four segments comprising the subject line had been the subject of Interstate Commerce Commission or Surface Transportation Board decisions approving their abandonment and three had been designated as trails under the National Trails Act. SWKR had obtained abandonment authority for the segment between Charleston and Paul Spur which SWKR had converted the line into a rail trail. SWKR continued to provide limited service to Chemical Lime on a noncommon carrier basis as an industrial spur. As such, SWKR needed no further authority to terminate service and salvage the track. Finally, once RailAmerica acquired SWKR, it sought and obtained but never consummated abandonment authority. Instead, RailAmerica sold this segment along with the other segments to SPROC which asked

¹ The subject line consists of four segments. (1) the segment of railroad designated as the Bisbee Branch, which extends between milepost 1085.0 at Bisbee Junction, AZ, and milepost 1090.6 at Bisbee, AZ, a distance of 5.6 miles (first segment). The remaining line segments are collectively designated as the Douglas Branch and include (2) the segment of railroad extending between milepost 1097.3 near Paul Spur, AZ, and milepost 1106.5 near Douglas, AZ, a distance of 9.2 miles (second segment); (3) the segment of railroad extending between milepost 1055.8 near Charleston, AZ, and milepost 1097.3 near Paul Spur, AZ, a distance of 41.5 miles (third segment); and (4) the segment of railroad extending between milepost 1040.15 near Curtiss, AZ, and milepost 1055.8 near Charleston, AZ, a distance of 19.9 miles (fourth segment).

the Board to vacate SWKR's abandonment authority and dismiss its Petition for Exemption for that abandonment.²

Currently, SPROC continues to operate the line north of MP 1040.15. At present the only customer on the railroad south of MP 1040.15 is the Chemical Lime plant at Paul Spur (Douglas, AZ) (near MP 1097.3), some 60 miles to the South. At the time SPROC acquired the line its Chairman David Parkinson had determined that its success depended, first and foremost, upon the railroad's ability to restore the international connection at Naco with the Mexican rail system (a carrier called Ferromex). Developing business with Chemical Lime and locating new customers to the railroad were also part of his business plan. Reply Verified Statement of David Parkinson ("Parkinson RVS") at 11-12. His analysis also found that the railroad track and right of way and especially the bridges needed substantial attention. After several visits from state and federal track inspectors and receipt of a bridge report from Osmose Railroad Engineering Services, Inc., an engineering firm, he learned that the bridges were in an even worse condition than originally anticipated. Parkinson RVS at 13-14, 16-18. After learning in January 25, 2005, that Ferromex would not

² See SPROC's Petition for Exemption at 3-6.

restore the international connection at Naco, Mr. Parkinson and his staff undertook a review of their options regarding continued service over the line segment. In March 2005 SPROC decided that abandonment of the line segment due to the limited existing freight business and the lack of customer opportunities was necessary. SPROC informed Chemical Lime on March 22, 2005, that the railroad would be seeking abandonment authority and would place this line on its "System Diagram Map" in the event of filing a formal abandonment application. Parkinson RVS at 2, 13; Juszli VS at 2. During the time preceding and immediately after the filing of the abandonment petition SPROC officials maintained a continuing dialog with Chemical Lime officials over the continued status of rail service and alternatives to trail service to their Paul Spur plant. Parkinson RVS at 2, 3, 13, 15.

After SPROC filed its Petition on June 6, an inspector with the Federal Railroad Administration (FRA) reviewed Osmose's inspection report for the bridge at MP 1044.4 and found it in such poor condition that he recommended in a letter to SPROC dated June 10, 2005, that the railroad cease operations over the bridge. Parkinson R.V.S. at 18 and Attachment 9. The FRA's recommendation had the practical effect of embargoing the bridge at MP 1044.4 and

terminating service to Chemical Lime. Upon learning that the FRA was issuing the bridge letter, Mr. Parkinson instructed his counsel to discuss continuation of service with the FRA but the agency was adamant that service stop at MP 1044.4. The FRA orally advised SPROC counsel that if the railroad did not voluntarily terminate service, it would issue an order requiring cessation of service over the bridge.³ Thereafter, SPROC embargoed the line south of MP 1044.4 and advised both the FRA and Chemical Lime of its action. On July 14, 2005, Chemical Lime filed its "Statement in Opposition" along with the verified statement of Mark Juszli, Vice President, Business Development and Logistics. It is to this filing that SPROC now responds.

ARGUMENT

The Board (and the Interstate Commerce Commission before it) applies the public convenience and necessity standard adopted in 49 U.S.C. 10903 in determining whether to permit a railroad to abandon a line. In applying that standard, the Board weighs the evidence supporting the abandonment against customer needs and rural and community impact. Colorado v. United States, 271 U.S. 153 (1926). Specific considerations include the losses the carrier is

³ Telephone call between SPROC counsel John Heffner and FRA official Grady Cothen on June 9, 2005.

experiencing, the financial condition of that carrier, shippers' use of the line, and the transportation alternatives available. However, as the Supreme Court ruled over 85 years ago, "...[A] carrier cannot be compelled to carry on even a branch of business at a loss, much less the whole business of carriage." Brooks-Scanlon Co. v. Railroad Comm'n, 251 U.S. 396 (1920). To do so would be an unconstitutional taking of the carrier's property without due process. In the Matter of Penn Central Transportation Company, 384 F. Supp. 895 (Special Court, Regional Rail Reorganization Act 1974).

The Staggers Act of 1980 gave the ICC the power to exempt railroads from the formal provisions of the Interstate Commerce Act by granting exemptions where appropriate. With the passage of the I.C.C. Termination Act in 1995 repealing the Interstate Commerce Act, Congress continued those exemption powers for the STB. Under 49 U.S.C. 10502(a), the Board has the power to exempt a person, class of persons, transaction or service whenever it finds that the application of a provision of this subtitle - (1) is not necessary to carry out the transportation policy of 10101 of this title, and (2) either (a) the transaction or service is of limited scope, or (b) the application of a provision of this subtitle is

not needed to protect shippers from the abuse of market power. And the legislative history behind section 10502 (and its predecessor section 10505) makes clear Congress' intent that the Board uses its exemption authority liberally to free certain transactions and services from the administrative and financial costs associated with continued regulation.

The simple fact is that Chemical Lime does not show that SPROC's abandonment request fails the formal public convenience and necessity test or that it is not entitled to an exemption from the formal abandonment requirements. In challenging SPROC's abandonment petition, Chemical Lime has misunderstood and/or distorted the applicable case law.

Briefly, SPROC understands Chemical Lime's to say that the Board may grant opposed abandonment exemption requests where the traffic revenues do not cover the marginal costs of operating the line (Chemical Lime Statement at 2) but that SPROC's "marginal" operating costs do not exceed its current revenues (Id. at 2,5); that it depended upon the line to handle coal and coke as a fuel for the manufacturing process and that the plant would have to be shutdown without them (Id. at 3; Verified Statement of Mark Juszli (Juszli VS at 4) or that, alternatively, it could truck these commodities to its plant, albeit at a

significantly higher cost (Id. at 4,7; Juszli VS at 3); and that it invested significant funds in re-opening its plant (which had been closed for some period of time) based upon the representations of SPROC about the prospect of restored rail service (Id. at 4). Chemical Lime even went so far as to craft a new "public convenience and necessity" balancing test weighing SPROC's operating results (consisting just of revenues and marginal costs of operation but excluding any track, right of way, or bridge rehabilitation and maintenance costs and return on investment) against the plant investments it has made, cost increases that it may experience as a result of the abandonment, and the payroll and property taxes it pays at the plant and concluding that SPROC should be compelled to continue a deficit service. (Chemical Lime Statement at 6-8; Juszli VS at 3-5).

As Chemical Lime concedes, the Board does grant opposed abandonment exemption requests where the revenues are insufficient to cover the marginal costs of operating the line. Boston and Maine Corporation - Abandonment Exemption - In Hartford and New Haven Counties, CT (STB Docket No. 32 (Sub-No. 75X, slip op. at 5, served Dec. 31, 1996). As recently as January 2005, the Board granted yet another opposed petition for exemption for abandonment where the economics of the operation overwhelmingly favored

abandonment over the needs of the customers. Norfolk Southern Railway Company-Abandonment Exemption In Nottoway, Prince Edward, Cumberland, and Appomattox Counties, VA STB Docket No. AB-290 (Sub-No. 252X, served January 18, 2005).⁴ SPROC submits its Petition presents just such a case warranting a grant of authority.

Chemical Lime's Statement and the testimony of its witness Mark Juszli present a litany of arguments why the Board should not force SPROC to continue a hopeless deficit operation. SPROC will address each in this Reply and in the testimony of its Chairman David L. Parkinson.

Chemical Lime argument #1: SPROC unilaterally ceased service without regulatory authorization and without agreement from Chemical Lime.

The only entity that can authorize a railroad to abandon service is the Board. However, the Board has consistently held that a railroad may temporarily cease service by embargoing the line where it is physically unable to serve a shipper. An embargo will be reasonable so long as the railroad either restores the line to service within a reasonable amount of time or promptly seeks abandonment authority. See, Decatur County Commissioners,

⁴ There Norfolk Southern Railway handled 158 cars of traffic on 33 miles of track for two customers versus an anticipated 2005 traffic volume of about 500 cars of traffic on 60 miles for one customer.

Et Al. v. The Central Railroad Company of Indiana, STB Finance Docket No. 33386 (served September 29, 2000) and Michael H. Meyer, Trustee in Bankruptcy, et al v. North Coast Railroad Authority, et al, STB Finance Docket No. 34337 (served July 27, 2005). Because the FRA forced SPROC to shut down its line at MP 1044.4 due to bridge conditions and SPROC promptly sought abandonment authority, its embargo and cessation of service were reasonable and lawful. Moreover, under STB precedent, SPROC could not be forced to spend substantial amounts of money it does not have to rebuild a line subject to abandonment. Decatur; Meyer.

Chemical Lime argument #2: The Board will grant abandonment where the revenue is insufficient to cover the marginal cost of operation and there is no showing here that the current revenue is less than SPROC's operating costs. Chemical Lime begins by incorrectly paraphrasing the Board's ruling in Boston and Maine. The Board actually said that it will grant contested abandonment exemptions where "the revenue from traffic is marginal compared to the cost of the operation of the line" not where the revenue is insufficient to cover marginal (i.e. out of pocket) costs of the operation. Id. at 5. That change in wording makes all the difference. Moreover, Chemical Lime ignores a

whole body of Board case law allows the abandoning railroad to include in its operating loss calculation normalized track and right of way maintenance expenses, bridge repair expenses, and return on investment ("opportunity costs"). Camas Prairie RailNet, Inc. - Abandonment - in Lewis, Nez Perce, and Idaho Counties, ID, (slip op. at 8-10, served September 13, 2000); Wisconsin Central LTD. - Abandonment - in Ozaukee, Sheboygan and Manitowoc Counties, WI, (slip op. at 6-7, 10-11 served October 18, 2004).

In the Petition Mr. Parkinson said that for the year to date through March 31, 2005, SPSR (SPROC) incurred \$39,989 in direct operating costs and \$68,815 in operating revenue. Parkinson VS at 2. In response to Chemical Lime's request for more detailed financial information, SPROC submits as an Attachment to Mr. Parkinson's reply its proforma financial statements for 2004 and 2005. The 2005 statement shows the financial results of operations (an "out of pocket" loss of \$520,042) assuming that SPROC paid the "emergency" costs of repairing the bridge (\$136,496), incurred normalized track maintenance costs of \$304,500 computed at \$5,000 per mile per year,⁵ and operated for the entire calendar year. That "out of pocket" loss does not

⁵ The Board has previously found normalized track maintenance costs in the range of \$5,000 per mile per year to be reasonable. Wisconsin Central LTD, supra; Union Pacific Abandonment, STB AB-33 (sub no. 140) (served December 22, 1999).

even cover the long term track and bridge rehabilitation costs or reflect any opportunity costs. SPROC is the only party submitting evidence on these issues to its data represents the best evidence of record. Accordingly, SPROC believes that \$260,101 in 2005 revenues when measured against \$614,324 in total operating expenses represents the sort of "marginal" operation contemplated in Boston and Maine.

Chemical Lime argument #3: The Douglas plant will either be shut down or face increased transportation costs. Shortly after claiming the abandonment will force closure of its recently reopened plant, Chemical Lime effectively rebuts its own argument by acknowledging that it could handle the traffic by truck, albeit at a higher cost. Juszli at 3, 5. The coal and coke that SPROC transports is used to fuel a furnace. Chemical Lime presents no testimony that other sources of fuel such as gas or oil could not be used, albeit at a higher cost. As the Board and the ICC have often stated, increased shipping costs are not a basis for denying an abandonment. Chicago And North Western Transport. Co., 354 I.C.C. 1, 7 (1977).

Chemical Lime argument #4: SPROC has not provided evidence in support of its claim that it will cost \$600,000 to bring the line up to FRA class I track standards, any

breakdown of cost estimates to allow the Board to evaluate the necessity and cost of repair, or any evidence regarding net liquidation value.

SPROC responds to Chemical Lime's assertions by noting that there are no specific evidentiary requirements associated with an exemption petition as there are for a formal abandonment. Compare, 49 CFR 1121 and 49 CFR 1152.60 with 49 CFR 1152, 1152.22, and 1152.30-6. The whole purpose of the exemption process is to relieve carriers, particularly smaller railroads, of having to comply with burdensome and expensive regulations.

In that regard, SPROC Chairman David Parkinson originally estimated that the line would require \$600,000 in track repairs to bring most of the track (currently in an "excepted" track condition) up to an FRA class I track standard. Parkinson VS at 3. While Mr. Parkinson did not present specific mile by mile evidence as to the repairs needed and the associated costs, he premised his conclusion on the fact that branch line maintenance costs typically run about \$5,000 per mile per year, a figure accepted by the STB.⁶ He then concluded that \$10,000 per mile of "make up" maintenance would be needed considering the many years

⁶ See footnote 5, supra.

of neglect by other short line owners. Parkinson RVS at 8-9.

Regarding valuation, the Board's regulations do not require an abandonment petitioner to present an appraisal as part of its abandonment request. This is in stark contrast to the formal abandonment application procedures that do require an applicant to furnish some basis for the net liquidation value of the line with its application. 49 CFR 1152.34(c)(iii). A petitioner does not need to go to the very substantial expense of preparing an appraisal until it receives a request from a party contemplating an offer of financial assistance. 49 CFR 1152.27(d).

Chemical Lime argument #5: Chemical Lime spent substantial sums of money bringing its plant back into service and rehabilitating railroad trackage leading to the plant based upon an expectation of continued SPROC rail service.

At no point did SPROC make any rail service commitments other than to maintain the line to Paul Spur through December 31, 2004. Moreover, SPROC offered to make Chemical Lime whole for its track-related improvements by refunding the \$50,000 it spend. Parkinson RVS at 15. In view of the railroad's long history as a light density line subject to numerous sales and abandonment filings, a

sophisticated company such as Chemical Lime knew or should have known the business risks associated with re-opening this plant. It did so for reasons unrelated to rail service availability and now seeks to blame SPROC for a bad business decision.

In the final analysis, Chemical Lime has not shown that SPROC is not entitled to a grant of its abandonment request under either the "public convenience and necessity" test of 49 U.S.C. 10903 or that it is ineligible for an exemption under 49 U.S.C. 10502. The simple fact is that SPROC would incur a large out of pocket operating deficit of \$520,042 handling this traffic in 2005 and did incur a large actual loss of \$304,547 for 2004 excluding any consideration of all but "emergency" bridge repair costs, the cost of track repairs, and opportunity costs. Including these items, SPROC's deficit would run about two million dollars and would threaten the viability of the company and the remaining 7 mile segment it operates between Benson and Curtiss, AZ. Accepting Chemical Lime's cost figures at faith, the adverse impact of the abandonment on this huge corporation would be modest, easily half that of SPROC. Analyzing SPROC's abandonment request by the ICC's historic "34 car per mile" viability test, SPROC's traffic "density" is about 8.33 cars per

mile, well below that threshold. Accordingly, SPROC has shown that the burden of continued operations on it and interstate commerce for outweighs the impact on Chemical Lime or the community. The Board's "PC&N" test weighs in favor of abandonment. Moreover, Chemical Lime has the further option of preserving service by filing an offer of financial assistance under 49 U.S.C. 10904.

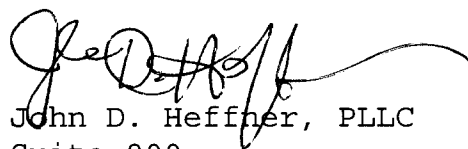
Regarding the Board's exemption criteria, SPROC originally represented in its Petition that it met those criteria. Chemical Lime presents no evidence or argument indicating otherwise.

There is one further matter worthy of mention. Back in its Petition at page 10, SPROC asserted that, but for the various trail use agreements and SPROC's 2003 request to vacate the previously granted abandonment exemption authority, the subject line would already be abandoned. SPROC filed this abandonment petition out of caution unsure as to whether its 2003 filing (submitted by a different counsel) reactivated its common carrier obligation as to the Curtiss to Charleston line. In any event, SPROC believes that the rest of the railroad including that serving Chemical Lime is still an industrial railroad for which no abandonment authority is even needed.

CONCLUSION

Accordingly, SPROC respectfully requests that the Board reject Chemical Lime's specious arguments and promptly grant this abandonment exemption request on September 23, 2005, as indicated in the Board's decision acknowledging its receipt.

Respectfully submitted,

A handwritten signature in black ink, appearing to read "John D. Heffner", with a long, sweeping horizontal line extending to the right.

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1920 N Street, N.W.
Washington, D.C. 20036
(202) 263-4180

Attorney for San Pedro
Railroad Operating
Company, LLC

Dated: August 3, 2005

CERTIFICATE OF SERVICE

I, John D. Heffner, certify that a copy of the foregoing Reply of San Pedro Rail Operating Company was served on August 3, 2005 to the following by first-class mail:

Charles A. Spitulnik
Alex Menendez
McLeod, Watkinson & Miller
One Massachusetts Avenue, NW
Suite 800
Washington, DC 20001

Rusty A. Brewer
Baker Botts LLP
1299 Pennsylvania Avenue, NW
Washington, DC 20004



John D. Heffner

ORIGINAL

David Parkinson, being duly sworn, deposes and states
as follows:

1. My name is David L. Parkinson. I am Chairman and Chief Financial Officer of Arizona Rail Group, owner of the San Pedro Railroad Operating Company (SPROC). I am the individual who initiated the filing of a petition by SPROC seeking the abandonment of SPROC's rail lines which are the subject of an abandonment proceeding in STB Docket AB-441 (Sub-No. 4X). I am also the same individual who submitted testimony appended to that Petition and filed on June 6, 2005.
2. I have read the "Statement of Chemical Lime Company filed in Opposition to San Pedro Railroad Operating Company, LLC's Petition for Exemption" dated and filed July 14, 2005, including the testimony of Chemical Lime Company's (CLC's) witness Mark Juszli. I believe that CLC's statement and the testimony of Mr. Juszli presents a simplistic and distorted view of the facts. Here are my responses presented in a "question and answer" format designed to contrast CLC's strained interpretation of the facts.

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3. *CLC assertion #1: SPROC unilaterally ceased service on the line in question, without any regulatory authorization, and without agreement by Chemical Lime: CLC Statement at 1.*

SPROC response:

Beginning in late 2004, we diligently pursued every alternative to ceasing service on the line. As noted in more detail in Item 17 below relating to the embargo of the bridge at MP 1044.4, SPROC cooperated fully with Federal and State regulators to maintain service on the line in spite of the bridge safety issue. Even after notifying Chemical Lime in March 2005 of our intent to abandon the line, we intended to maintain service until we obtained appropriate STB authority to abandon the line. In fact, we advised Chemical Lime in that notification that the railroad was experiencing increasing problems related to bridge safety. We had no idea that the FRA was going to take the extreme measure of essentially ordering us to cease operations over the bridge. We were working diligently towards a solution, which would have allowed us to repair

the bridge at MP 1044.4 while maintaining service until such time as we received abandonment authority. On July 13, 2005, we received a letter from the FRA which stated in essence "close the bridge to operations or we will order it closed." The FRA had full regulatory authority to order us to cease operations under their emergency safety enforcement regulations. As soon as it became clear they would accept no other alternative to closing the bridge and ceasing operations over it, we immediately notified Chemical Lime of this situation on July 14 and informed them the line would be embargoed due to FRA safety enforcement actions. We believe that the very few additional months of service that would be required while our abandonment request was pending did not justify the approximately \$136,000 in emergency bridge repairs to restore it to service.

4. *CLC assertion #2: SPROC relies almost entirely on speculation that its abandonment requested will be unopposed: CLC Statement at 2.*

SPROC response:

We did not base our abandonment request on the assumption that our request would be unopposed. Rather, we made the appropriate filing based on the poor physical condition of the line and the financial results of handling fewer than 500 annual carloads over 60 miles of railroad.

5. *CLC assertion #3: SPROC has never provided Chemical Lime with any proposal to build a transloading facility and does not appear to be pursuing the issue actively. SPROC only furnished, in its words, a "token" offer on June 30. CLC Statement at 4.*

SPROC response:

Untrue. In addition to Chemical Lime's so called "token" written proposal June 30, 2005, we provided them with a more detailed transload proposal on July 22, 2005. A copy of that proposal is submitted as Attachment 1.

6. *CLC assertion #4: Relying on SPROC's proposal to provide continued rail service, Chemical Lime invested significant funds in improving the SPROC tracks leading to the Douglas plant as well as in reopening the Douglas plant, and advanced funds to SPROC to maintain the rail line segments while Chemical Lime was reopening the Douglas plant.*
CLC Statement at 4.

SPROC response:

SPROC never provided Chemical Lime with any written or verbal proposal or assurance, let alone commitment, to provide continued rail service over the line. Moreover, as a long time user of this line Chemical Lime is well aware of the fact that the line has a history as a light density line. In fact, each of the two previous owners of this rail line had sought and obtained abandonment authority. In our letter agreement of June 1, 2004 (submitted as Attachment 2) we offered to keep the line in place between Bisbee Junction and Paul Spur, a distance of about 10 miles, for the remainder of 2004 for a "hold in place" fee of \$2500/month. Since Chemical Lime,

prior to that, had refused to give SPROC any commitment or substantive information about the future of their plant at Paul Spur, we took bids to salvage the line since a prior owner of the line had already received abandonment authority for that line segment. It was only at this juncture that Chemical Lime stated that they had plans to reopen the plant in late 2004 and agreed to pay us a fee to keep the line intact. That fee totaled \$22,500 in 2004, essentially all of which went into repairing the line between Bisbee Junction and Paul Spur, so that service could be restored in late 2004.

With regard to the \$32,000 Chemical Lime spent on repairing the track at Paul Spur mill, those were repairs that were necessary to correct track deficiencies that had to be repaired in order for SPROC to switch cars into their plant. Otherwise service could not have been resumed. The plant had been closed for four years.

7. *CLC assertion 5: "that figure [\$68,815], through March 31, 2005, significantly understates the*

annualized revenue for 2005 that SPROC would have realized if it had not unilaterally ceased service without authorization or agreement." CLC Statement at 6.

SPROC response:

Our petition only provided the revenue we received through March 31, 2005, the latest accounting information, which we had when we filed the exemption request. Had service continued through 2005, our revenues on the Paul Spur line segment to Chemical Lime would have approximated \$260,000. See 2004 and 2005 pro forma financial statements, Attachment 3.

8. CLC assertion #6: there is no evidence supporting the \$6 million estimated net liquidation value or the annual opportunity cost of \$840,000. CLC Statement at 7.

SPROC response:

The \$6 million estimate was derived by estimating the value of the track materials (rail and OTM) plus the value of the railroad land holdings.

Due to the recent drop in steel prices, the current value of the rail and OTM is less than that previously estimated. This fact has been verified in consultations with rail salvage companies. The current total value of the track materials and land is estimated at \$5 million. Opportunity costs are computed using STB guidelines.

9. *CLC assertion #7: Mr. Parkinson also fails to provide any evidence supporting CLC's claim that it will cost \$600,000 to bring segments of the railroad up to FRA Class I standards or provide any breakdown of its cost estimate that would allow the Board to evaluate the necessity and cost of repair. CLC statement at 7.*

SPROC response:

Based on our reconnaissance of the line between MP 1040.15 and 1097.3, a distance of about 60 miles, we estimated that it would require an expenditure of about \$10,000/mile to bring the track up to an FRA class 1 standard. This expense was primarily for ties, ballast and

surfacing. Normalized maintenance on a shortline of this nature should run about \$5000/mile/year. Since the line had been idle for four years, we again felt this was about the level of funding required to bring the line into full FRA Class 1 compliance. Also this number does not include necessary bridge repairs (see item 14).

10. *CLC assertion #8: SPROC makes little attempt to support its assertions about revenue from the line; because no breakdown of these revenues is given, it is impossible to tell whether the 2004 figure includes the \$22,500 that Chemical Lime advanced SPROC for track maintenance; SPROC provides no evidence that would allow the Board to conclude that SPROC's costs of operating the relevant segments of the line are so high as to exceed the expected 2005 revenue. CLC statement at 7-8.*

SPROC response:

I am submitting as Attachment 3 proforma financial statements for 2004 and 2005 as well as consolidated financial statements.

11. *CLC assertion #9: SPROC insisted that Chemical Lime improve the SPROC tracks leading to the plant and provide monthly payments totaling \$22,500 to SPROC during 2004 to maintain the track. CLC Statement at 8.*

SPROC response:

See Question 4. The \$2500/month fee was an alternative to our scraping the line from Bisbee Junction to Paul Spur. We believed that this fee would cover the cost of keeping that line segment in operation for the balance of 2004. The fee Chemical Lime paid to the track contractor for in-plant repairs was necessitated by the deteriorated condition of the plant tracks due to four years of disuse and was the absolute minimum necessary to provide safe rail service into the plant.

12. *CLC assertion #10: SPROC did not indicate until June 15, 2005, a week after it filed its Petition that \$500,000 to \$600,000 in additional repairs*

would be needed to bring the line up to operating condition. CLC Statement at 9; Juszli at 1-2.

SPROC response:

This is false. SPROC's Petition for Exemption and my accompanying supporting testimony submitted on June 6, 2005, both clearly note that the need to invest approximately \$600,000 in track, right of way, and bridge repairs to maintain the line. Petition for Exemption at 7; Parkinson V.S. at 3. These pages are appended here as Attachments 4 and 5.

13. CLC assertion #11: SPROC's failure to secure an agreement with Ferromex [the Mexican railroad on the other side of the border] does not mean that such an agreement could never be reached. CLC statement at 9.

SPROC response:

Our strategy for keeping the line segment from MP 1040.15 to MP 1097.3 open was based on a threefold approach: 1.) Continued operation and service to Chemical Lime's Paul Spur mill, 2.)

Reestablishing an international rail connection near Naco, AZ/Sonora with the Mexican rail carrier, Ferromex,¹ and, 3.) Developing new industrial rail customers on the line segment. After a year and a half of aggressive negotiations and marketing efforts with Ferromex, it became clear in early 2005, that they were unwilling to reconnect our two railroads at Naco. See email correspondence with Ferromex submitted as Attachment 6. Without the Mexico connection, which we were originally optimistic about when we acquired the railroad in 2003, there was little hope the line segment could remain economically viable. Also our efforts to locate additional rail served customers on the line segment were unsuccessful and we had no realistic prospects for such customers.

14. *CLC assertion #12 that at the time SPROC requested these commitments from Chemical Lime*

¹ I should note that both Kyle Railways and its successor, States Rail had unsuccessfully attempted to restore the international rail connection at Naco. We were unsuccessful because, we discovered, that Ferromex and its part-owner the Union Pacific Railroad wanted to maintain only one international gateway, at Nogales. I doubt that any other rail operator would have any more success in obtaining Ferromex's agreement than SPROC or any of its predecessors would have had.

that it did not indicate that any bridge repairs were necessary, that the railroad was contemplating a request for abandonment, or that the railroad's continued existence was contingent on SPROC reaching a deal with Ferromex. Juszli at 2-3.

SPROC response:

As I noted above, we notified Chemical Lime in March 2005 that bridge conditions were contributing to our decision to seek abandonment. Bridge repair costs for line segment MP 1040.15 to MP 1097.3 are now estimated at \$731,500 based on a recent quote for the high priority work (Priority 2 and 3) from Osmose, a leading bridge contractor. Prior to that, we had known for sometime that the bridges would require significant attention but it was shortly after June 6, the very day we filed this abandonment request, that we received a full report from Osmose based upon the inspection it conducted during the week of May 9. A summary of that report and Osmose's repair estimates are appended here as Attachment 7. SPROC will make the full

report available to the Board and to any other party requesting it.

Regarding abandonment, Chemical Lime has been a long time customer on this railroad going back to the time that it was owned and operated by the Southern Pacific Railroad. Subsequently, the line was acquired by Kyle Railways, Inc., which sought to abandon the railroad south of Charleston, AZ. During the pendency of that abandonment, another short line carrier [States Rail] acquired Kyle's portfolio of railroads. Then RailAmerica acquired the States Rail system and obtained STB authority to abandon the line from Curtiss to Charleston. It was at that point that I stepped in to acquire the railroad believing that I could reestablish the international connection and "make a go" of it. Unfortunately, subsequent events have proved me wrong. But for Chemical Lime to suggest that abandonment comes as a surprise is disingenuous at best.

15. *Chemical Lime assertion #13: Chemical Lime requested SPROC's proposal as to how it would offset Chemical Lime's financial damages and keep it whole as to the increase in the delivered cost of coal and coke. Juszli at 3.*

SPROC response:

In my telephone discussions with Mark Juszli on June 30, 2005 we discussed what the alternatives were to Chemical Lime opposing an abandonment exemption request. I stated that we would be willing to refund the funds we had collected for the track agreement (June 1, 2004) plus their costs to repair the plant track, a total of approximately \$50,000. Beyond that I made no reference to or any suggestion that we would be willing to reimburse any of their added transportation costs due to the railroad embargo or abandonment. A copy of my June 30, letter to Chemical Lime is submitted as Attachment 8.

16. *Chemical Lime assertion #14: SPROC was optimistic about SPROC's health as confirmed by*

my comments in *Progressive Railroad* magazine.
Juszli at 2.

SPROC response:

The *Progressive Railroad* article was merely a discussion of some of the issues we faced in renewing or keeping service to the border area. Dated December 14, 2004, this article appeared before Ferromex rejected our request to re-establish the border connection and before we fully recognized the seriousness of the emerging bridge problems. I believe the article is irrelevant to the abandonment petition since no commitments were made or suggested regarding the continuation of service on the line.

17. In closing, I would like to set the record straight on the chronology of events that forced SPROC to cease service south of MP 1044.4.

On November 30, 2004, an Arizona Corporation Commission (ACC) track inspector performed a track and bridge inspection of the SPROC and voiced

concern about the safety status of certain bridges. ACC's inspector then returned with Federal Railroad Administration (FRA) inspectors to review the November 2004 bridge and track survey. The FRA issued a bridge inspection report with specific concerns about the bridge at MP 11044.4. On February 11, SPROC retained a qualified bridge engineering firm [Osmose] to inspect and prepare a work program to repair the bridge and on February 17, Osmose inspected the bridge with federal and state inspectors. After Osmose provided SPROC with a letter report of its inspection with repair priorities, SPROC provided a copy of same to the FRA. SPROC advised the FRA that all Priority 1 items (Urgent repairs) had been completed. Between March 10 and June 6, 2005, SPROC contracted with Osmose to undertake and Osmose completed a full bridge inspection of the railroad including a full engineering evaluation of the bridge at MP 1044.4; Osmose met with federal and state inspectors to debrief them on their inspection of the line including the bridge at MP 1044.4. Osmose advised SPROC that the bridge needs major work but that all conditions are priority 2 or higher, meaning that

SPROC can continue to operate over the bridge. After Osmose issued and forwarded to the FRA its formal report on June 6, 2005, the FRA bridge engineer contacted Osmose stating that its repair program was unsatisfactory.

On June 10, 2005, the FRA sent a letter to SPROC recommending that operations cease over the bridge at MP 1044.4 until bridge conditions could be corrected. SPROC then asked Osmose to repair the bridge while it remains in service. After counsel for SPROC contacted the FRA to persuade the agency to let it continue train operations over the bridge at restricted speeds, FRA's Office of Safety strongly urged SPROC to cease service over the bridge immediately. Subsequently, on or about June 15, SPROC advised Chemical Lime and the FRA that it would embargo service over and south of the bridge. Copies of relevant correspondence are submitted here as Attachment 9.

ATTACHMENT 1



JOHN H. DUGAN
Chief Executive Officer and
Chief Marketing Officer

14301 North 87th St., Suite 105
Scottsdale, AZ 85260
Phone: 480-607-2848
Fax: 480-607-1709
Cell: 602-538-4915
Email: john@arizonarr.com

July 22, 2005

Mr. Thomas Hughes
Distribution Manager
Chemical Lime Company
15333 North Pima, Suite 200
Scottsdale, AZ 85260

Dear Tom:

Referring to our recent conversation regarding the possibility of transloading coal and coke at Curtiss, Arizona from a transload location served by the San Pedro and Southwestern Railroad (SPSR).

As we discussed SPSR does not have a ready-made transload facility on property and would need to construct a facility. There are two (2) possibilities with each one of the two requiring a minimum of 90 plus days to construct. The 2 locations that might be developed are as follows:

- (1) Track located on Apache Nitrogen Products property accessed off Apache Powder Road, Curtiss, AZ.
- (2) Constructing a new track and transload facility at Curtiss, AZ on SPSR land.

The estimated cost associated with (1) The Apache Nitrogen site is as follows:

Installation of a Conveyor, Car-Shaker system, Concrete Pad, Environmental containment and run electrical. - # \$90,000.00. (estimated)

(PROJECTED PER TON COST)

SPSR Rail Service - Benson to Curtiss, AZ.	\$378.96 = \$ 3.79 ton
Use of Apache Nitrogen Products track and land -	\$ 4.00 long ton.
@ Unloading from rail car to truck -	\$ 2.25 long ton.
@ Truck Rate - Curtiss to Paul Spur, AZ.-	\$10.00 long ton.
*(Based on back haul)	
Total cost per ton - Benson to Paul Spur, AZ from Apache site.	<u>\$20.04</u>

Page (2)

The estimated cost associated with (2) – constructing a new track and transload facility on SPSR land at Curtis, AZ. is as follows:

Installation of a Conveyor, Car-Shaker system, Concrete Pad, Environmental containment and run electrical. # \$ 90,000.00 (estimated)
% Constructing a new track at Curtis, AZ. \$141,000.00 plus grading & utility relocation.

(PROJECTED PER TON COST)

SPSR Rail Service – Benson to Curtiss, AZ. \$378.96 = \$ 3.79 ton
@ Unloading from rail car to truck - \$ 2.25 long ton
@ Truck Rate – Curtiss to Paul Spur, AZ.- \$10.00 long ton
 *(Based on back-haul)
Total projected cost per ton – Benson to Paul Spur, AZ from
 proposed SPSR site. \$16.04

@ Cost/Rates quoted by CTI Trucking Company, Rillito, AZ.

Conveyor, car-shaker (relocated from Paul Spur),
Construction of concrete pad, environmental containment, permitting
and electrical installation estimated quote from CTI Trucking. Build-out
time is projected to be 90 + days.

% Estimated construction time for track installation 90 – 120 days.

* CTI quote - \$14.00 long ton for non-back haul move, Curtiss to Paul Spur, AZ.

I look forward to discussing this subject further and should you have any questions please
phone me at 480-607-2848 or my cell phone 602-538-4915.

Sincerely,


John H. Dugan

Cc: David L. Parkinson – Napa, CA. ✓

ATTACHMENT 2

**SAN PEDRO & SOUTHWESTERN RAILROAD**

P.O. BOX 1420
796 EAST COUNTRY CLUB DRIVE
BENSON, AZ 85602
520-586-2266 FAX: 520-586-2999

June 1, 2004

Via Federal Express

Mr. Don Robinson
Vice President - Operations
Chemical Lime Company
3700 Hulen Street
Ft. Worth, Texas 76150

Dear Don:

This letter authorizes a short-term agreement between Chemical Lime Company and the San Pedro & Southwestern Railroad (SPSR) concerning our rail line between Bisbee Junction, Arizona and Paul Spur, Arizona, a distance of approximately 11.5 miles.

In consideration for maintaining this rail segment in place without benefit of rail freight traffic, Chemical Lime agrees to pay the San Pedro & Southwestern Railroad a fee of \$2,500.00/month for the period from March 1, 2004 through December 31, 2004, a period of ten months. San Pedro & Southwestern agrees to keep the line intact in its present status during that period.

Assuming that Chemical Lime will reopen the Paul Spur mill and that the mill will use solid fuel in the form of rail transported coal and coke, we agree to negotiate a mutually acceptable new rail transportation agreement similar to the one between Chemical Lime and the San Pedro & Southwestern Railroad dated October 20, 1998.

An invoice for the period of March 1 through May 31, 2004 for the maintenance fee is enclosed. The SPSR will invoice you monthly hereafter for the balance through December 31, 2004.

If you concur with this agreement, please sign and return one copy of it along with the March- May fee.

We look forward to a productive and mutually beneficial business relationship. Thank you for your assistance.

Sincerely,



David L. Parkinson
Chairman

cc: John Dugan, ARG

Accepted and agreed to this 4th day of June, 2004.

Chemical Lime Company

By: Don Robinson

Title: V. P. Operations

ATTACHMENT 3

Memorandum

To: John Heffner

From: Dave Parkinson 

Subject: SPSR Financials and Line Segment Proformas

Date: July 29, 2005

1. The response to your queries are forwarded via separate cover.
2. Enclosed with this memo are the SPSR financial statements for 2003, 2004 and 2005. Only 2004 was audited for bank purposes. Please note that except for a gain on the sale of some land in June 2005, the SPSR sustained operating losses after interest expenses in all three periods.
3. 2004 Proforma Financial for Line Segment to be Abandoned (MP 7.0-67.9)

Revenue

Freight (Chem Lime)	\$56,640
Line Maintenance (Chem Lime)	22,500
Total Revenue	\$79,140

Expenses

Train Operations(2 persons 2days/wk, 3mon Plus 45% benefits	\$ 6,496
Fuel (one loco, 2days/wk, 20gph, 8hr @1.40gal)	5,376
Loco Cost(one loco @ @\$1000/mon lease)	3,000
Loco Maintenance (one loco @ \$15,000/yr 3 mon)	3,750
Maintenance of Way	
Rehab line for operations to Paul Spur	228,500
Prorata portion of 2004 MoW expenses (prorate on revenue basis- 13%)	4,090
Overhead/G&A(prorate on revenue basis)	36,335
Depreciation/Amortization(prorate on mileage (basis)	104,948
Total Operating Expenses	\$392,495
Interest (prorate on revenue basis)	\$8,808
Net Income	(\$304,547)

4. 2005 Proforma Financial for Line Segment to be Abandoned (MP 7.0-67.9)

Revenue	
Freight	\$260,101
Expenses	
Train Operations	42,240
Fuel (\$2.00/gal- 2005)	33,280
Loco Cost	15,000
Loco Maintenance	15,000
Maintenance of Way (\$5,000/mile/year – normalized)	304,500
Overhead/G&A (prorate on revenue-32%)	97,948
Depreciation/Amortization(prorate on mileage)	106,356
Total Operating Expenses	\$614,324
Interest (prorate on revenue basis)	\$29,323
Net Income (without repair to Bridge 11,3)	(\$383,546)
Repair Costs to Bridge 11.3	136,496
Net Income (with Bridge 11,3 repairs)	(\$520,042)

ARIZONA RAILROAD GROUP LLC
CONSOLIDATED BALANCE SHEET
AS OF DECEMBER 31, 2003

ASSETS	Dec 31, 03
Current Assets	
Checking/Savings	148,376.50
Accounts Receivable	60,879.66
Notes Receivable	325,000.00
Start-Up Costs/Commitment Fee	96,732.25
Other Current Assets	44,060.57
Total Current Assets	675,048.98
Fixed Assets	
Railroad Assets	2,626,000.00
Accumulated Depreciation	(18,389.16)
Total Fixed Assets	2,607,610.84
TOTAL ASSETS	3,282,659.82
LIABILITIES & EQUITY	
Current Liabilities	
Accounts Payables	70,173.58
Property Taxes-RRA	37,462.86
Note Payable-LaSalle	1,567,500.00
Other Current Liabilities	54,386.36
Total Current Liabilities	1,729,522.80
Equity-LLC Member Contributions	1,625,000.00
Net Income	(71,862.98)
TOTAL EQUITY	1,553,137.02
TOTAL LIABILITIES & EQUITY	3,282,659.82

ARIZONA RAILROAD GROUP LLC
CONSOLIDATED PROFIT & LOSS
NOVEMBER 1 - DECEMBER 31, 2003

Nov-Dec 03

Ordinary Income/Expense

Income	
Revenue	62,629.66
Total Revenue	62,629.66
Expense	
Administration	19,474.72
Maintenance of Way	8,052.48
Transportation	22,082.16
Overheads	50,231.41
Depreciation/Amortization	22,124.98
Total Expense	121,965.75
Net Operating Income	(59,336.09)
Net Operating/Expense	
Interest Expense	12,526.89
Net Income	(71,862.98)

ARIZONA RAILROAD GROUP, LLC
CONSOLIDATED BALANCE SHEET
DECEMBER 31, 2004

ASSETS

CURRENT ASSETS

Cash and cash equivalents	\$ 6,319
Accounts receivable - trade	152,812
Materials and supplies	7,346
Prepaid expenses	29,559

Total current assets 196,036

NOTE RECEIVABLE - MEMBER

42,713

PROPERTY, PLANT AND EQUIPMENT, NET

2,765,767

OTHER ASSETS

Loan fees, net of accumulated amortization of \$6,806 10,694

\$ 3,015,210

LIABILITIES AND MEMBERS' EQUITY

CURRENT LIABILITIES

Current portion of long-term debt	\$ 367,500
Accounts payable	58,596
Accrued expenses	
Payroll and payroll taxes	4,276
Property taxes	40,728
Other	3,828

Total current liabilities 474,928

LONG-TERM DEBT

1,200,000

MEMBER'S EQUITY

Member capital contributions	1,625,000
Undistributed members' loss	(284,718)

1,340,282

\$ 3,015,210

See Notes to Consolidated Financial Statements

ARIZONA RAILROAD GROUP, LLC**CONSOLIDATED STATEMENT OF OPERATIONS AND MEMBER'S EQUITY
FOR THE YEAR ENDED DECEMBER 31, 2004****REVENUE**

Freight	\$ 489,290
Other	87,950
	<u>577,240</u>

OPERATING EXPENSES

Transportation	185,343
Mechanical	7,317
Maintenance of way	31,460
Administrative personnel	39,749
Overheads	239,749
Depreciation	111,178
Amortization	5,833
	<u>620,629</u>

OPERATING LOSS(43,389)**OTHER INCOME (EXPENSES)**

Interest expense	(72,584)
Miscellaneous	4,834
	<u>(67,750)</u>

NET LOSS\$ (111,139)**MEMBER'S EQUITY, beginning of year**

\$ 1,451,421

Net loss

(111,139)**MEMBER'S EQUITY, end of year**\$ 1,340,282*See Notes to Consolidated Financial Statements*

ARIZONA RAILROAD GROUP LLC
CONSOLIDATED BALANCE SHEET
AS of JUNE 30, 2005

ASSETS	June 30, 05
Current Assets	
Checking/Savings	141,228.72
Accounts Receivable	60,345.91
Notes Receivable	43,349.70
Commitment Fee	7,777.80
Other Current Assets	21,387.08
Total Current Assets	274,089.21
Fixed Assets	
Railroad Assets	2,799,735.70
Accumulated Depreciation	(186,119.83)
Total Fixed Assets	2,613,615.87
TOTAL ASSETS	2,887,705.08
LIABILITIES & EQUITY	
Current Liabilities	
Accounts Payable	73,814.76
Note Payable-LaSalle	1,347,500.00
Other Current Liabilities	36,017.60
Total Current Liabilities	1,457,332.36
Equity-LLC Member Contributions	1,625,000.00
Retained Earnings	(284,111.60)
Net income	89,484.32
TOTAL EQUITY	1,430,372.72
TOTAL LIABILITIES & EQUITY	2,887,705.08

ARIZONA RAILROAD GROUP LLC
CONSOLIDATED PROFIT & LOSS
June 30, 2005

	<u>1 Month Ending June 30,05</u>	<u>6 Months Year to Date June 30,05</u>
Ordinary Income/Expense		
Income		
Revenue	58,692.72	420,901.21
Total Revenue	58,692.72	420,801.21
Expense		
Administration	6,867.07	42,197.58
Transportation	38,776.62	163,843.27
Maintenance of Way	13,496.35	35,903.98
Overheads	25,442.82	110,844.87
Depreciation/Amortization	9,910.85	59,488.10
Total Expense	94,493.71	412,275.80
Net Operating Income	(35,800.99)	8,625.41
Other (Income)/Expense		
Interest Expense	7,200.54	45,816.66
Gain on Sale of Land	-126,675.57	-126,675.57
Net Income	83,674.04	89,484.32

ATTACHMENT 4

traffic in the future. Parkinson V.S. at 2-3. SPROC is working with Chemical Lime to build a transloading facility along its line at Curtiss to allow Chemical Lime to transload inbound coke to trucks for transportation to its plant at Paul Spur. In addition, Chemical Lime plans to use truck transportation to transload and haul inbound coal from the BNSF Railway, Inc. at Deming, NM, to the Paul Spur plant. SPROC does not anticipate that Chemical Lime will oppose this abandonment. See Parkinson V.S. at 3.

Mr. Parkinson's statement describes the service that SPROC has provided over the line during 2004 and 2005 to date as well as the financial results of providing that service. Mr. Parkinson's testimony establishes that SPROC incurred an out of pocket loss of \$220,337 for 2004. For the year 2005, Mr. Parkinson notes that SPROC has an estimated opportunity cost of approximately \$840,000.³ Mr. Parkinson also stated that SPROC would need to invest approximately \$600,000 in track, right of way, and bridge repairs to maintain the subject line in a minimally serviceable condition. Parkinson V.S. 2-4.

In support of its request, SPROC submits as Exhibit C hereto a copy of a draft Federal Register notice as required by

³ SPROC calculated this estimated opportunity cost by multiplying the net liquidation value of the property, \$6 million, by the nominal rate of return, 14%. See Mississippi Tennessee Holdings, LLC-Abandonment Exemption-in Union, Pontotoc, and Chickasaw Counties, MS, STB Docket No. AB-868X, Petition for Exemption, p. 13-14.

ATTACHMENT 5

Curtiss. Motor carrier service is available to meet the needs of Chemical Lime and any other potential rail users. Local copper mining and smelting activities, which traditionally provided much of the local freight business, ceased some years ago. Our efforts as well as those by local officials at attracting new industry to the area have been unsuccessful. I am unaware of any prospects for new rail shippers.

SPSR does not anticipate that Chemical Lime or any other party will oppose this abandonment. SPSR has discussed abandonment of the line with Chemical Lime officials. Chemical Lime has indicated an intent transload to truck coal moving inbound to its Paul Spur plant from the BNSF Railroad at Deming, New Mexico. SPSR intends to move inbound coke for Chemical Lime from Benson (UP interchange) to a transload facility at Curtiss where it will be loaded into trucks for movement to Paul Spur.

Recently, through our own inspections, and those of state and federal railroad inspectors, we have found that certain bridge repairs on the line segment would be required in order to continue long-term safe operation of the railroad. Timber bridges between milepost 1040.15 and milepost 1097.3 will require repairs estimated to cost in excess of \$500,000 in the next two years to sustain operations on this section of the railroad. The track is in FRA class I condition between milepost 1040.15 and 1041.15, adequate for 10 mph speeds. Beyond milepost 1041.15 to the end of present operations at Paul Spur, the line is in an "excepted track condition." I estimate that \$600,000 worth of work would be required to upgrade this track to class I track conditions. The balance of the track is barely operable under any conditions.

ATTACHMENT 6

Mail :: INBOX: Re: Your Nov. 15 communication

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INBOX

Move Copy This message to

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Print

Date: Tue, 25 Jan 2005 16:38:07 -0600

From:

To:

Subject: Re: Your Nov. 15 communication

Dave:

For you to get an idea, our weakest gateway is Mexicali/Calexico, where we interchange close to 10,000 cars annually. This gateway had a very significant increase in 2004 with 34%. At one time, we were considering closing this gateway because of the low volume but after last year's increase we think we can further develop this border. The next border, Nogales, interchanged almost 46,000 cars in 2004.

I think that it is a good idea to liquidate the land that connects to our track in Naco. I anticipate that there will be problems to open the gateway there and would be easier to get government's approval farther out from the city.

I hope the above gives you a better idea. Let's keep in touch.

Regards,

Rogelio

dave@arizonarg.com wrote:

> Rogelio: Thank you for the status report. Of course, we are disappointed that >FerroMex cannot move ahead with Naco at this point. I have two questions that >will help our future efforts:

> 1. What approximate level of traffic would it take to interest FerroMex in >reopening the Naco Crossing?
> 2. Given the current situation we will likely liquidate the property on the US >side of the border leading to your rails in the center of Naco. That still >leaves us the option to connect east of Naco, which is more politically >acceptable should we wish to pursue the crossing in the future. Are you ok with >that? Best Regards, Dave

>Quoting Rogelio Velez Lopez de la Cerda <rvelez@ferromex.com.mx>:

>>Dave:

>>At this time, we are not considering the opening of a new gateway at >>Naco because the potential volume does not justify investment and >>operating expenses. As you may know, we have just reopened that gateway >>at Ojinaga/Presidio to begin interchanges with the Texas Pacific and >>until we determine success we will not consider another gateway. >>Apache has been in touch with us and we are trying to resolve their >>problems with UP. I have meetings with UP on Jan. 25 and this item is in >>the agenda.

>>I understand that this decision is not what you are expecting but at >>this time this is our position. Let's keep in touch and with an open >>mind to opportunities.

>>Best regards,

>>Rogelio

>>

>>dave@arizonarg.com wrote:

>>

>>

>>

<http://64.92.112.127/horde/imp/message.php?index=642>

1/26/05

ATTACHMENT 7



June 6, 2005

Bridge Inspection Report

SAN PEDRO & SOUTHWESTERN RAILWAY

Main Line

INTRODUCTION

During the week of May 9th of 2005, a bridge inspection was performed for the San Pedro & Southwestern Railway. Eighty-three structures comprised of timber, steel and concrete were inspected on the Main Line between Benson and Forrest, Arizona. This inspection was performed by Greg Grumke, Bridge Inspector/Engineer and Kevin Trickle, Bridge Inspector of Osmose Railroad Services, Inc. The purpose of this inspection was to identify structural deficiencies within the bridges and to determine the extent of internal decay in the timber members.

This report summarizes the defects found, describes our inspection techniques and provides a prioritized listing of repair recommendations. Individual inspection reports are included for each structure. For your reference, we have also provided you with our timber boring records for each bridge inspected. These boring records illustrate the cross sectional boring data taken at sampled locations on the timber trestles.

SUMMARY OF FINDINGS

In general, the bridges inspected were found to be in fairly good condition. The inspection did reveal varying degrees of decay deterioration in some of the timber members. The most immediate concern is the Priority 2 & 3 repairs.

Our recommended priority rating is a measure of the level of importance associated with repairing defective members or conditions found at the time of the inspection. An explanation of this priority system can be found on page 3 of this report as well as on the blue sheets included with the priority listings. Dimensions of all members shown in the inspection records should be field verified before commencing repairs.



INSPECTION

Bents are numbered from decreasing mileage to increasing mileage, starting with Bent 1. Piles are numbered facing increasing mileage from left to right.

Several inspection techniques were utilized during this inspection:

- Visual - A visual survey of all timber, steel and concrete components and their surrounding areas was conducted on each bridge.
- Hammer Sounding - Areas along the perimeter of the timber caps, piles and stringers were hammer sounded to help ascertain the presence of internal decay voids.
- Boring - Drilling 3/8" diameter holes in suspect areas of decay at locations found suspicious during hammer sounding and at various bearing areas of the caps, piles, stringers and sills. These holes were inspected, using a shell and void indicator, to confirm the presence of internal decay and evaluate the remaining sound wood. The inspection holes were plugged with a treated wooden dowel.

Particular attention was paid to decay vulnerable areas such as the groundline, waterline, brace bolt connections and bearing areas of the members. The size and location of internal voids were recorded, along with any visual observations. Concrete and steel bridges were examined in areas which commonly develop structural deficiencies, such as bearing areas and connection points.

This inspection used subjective inspection techniques and also relied heavily upon human judgment. It is possible that some deficiencies may not have been discovered. However, we are confident that all of the critical visible defects and critical internal wood fiber deterioration have been found. This inspection did not include underwater members, excavation of buried members or a rating of the structures.

Substandard timber components are classified as REJECT or POSSIBLE REJECT. A "reject" is defined as a timber component that has either failed, been damaged, or decayed to the point where it can no longer safely carry the load to which it is being subjected. A "possible reject" refers to a timber component not decayed or damaged sufficiently to be classified as a reject, but is deteriorated enough to be considered for replacement.



RECOMMENDATIONS

In the following three sections of this report (*Recommended Repairs by Bridge*, *Recommended Repairs by Priority*, and the *Summary Inspection Sheets*), we have outlined our repair recommendations.

Our priority rating system is a measure of the level of importance associated with repairing defective members or conditions found at the time of the inspection. Substandard conditions that are left unchecked can become worse over time and could lead to other structural problems. **Osmose strongly recommends that Priority 1 repairs be made immediately and Priority 2 repairs be accomplished as soon as possible.**

The priority ratings are as follows:

- PRIORITY 1 - Emergency.** Stop operation over structure and perform repairs immediately. *No items were found during this inspection that required Priority 1 repairs.*
- PRIORITY 2 -** Condition is unsafe and could cause failure at any time. Repair as soon as possible. Condition must be monitored continually until repairs have been completed.
- PRIORITY 3 -** Condition could become unsafe and should be monitored frequently. Repair in the near future.
- PRIORITY 4 -** Condition is substandard and should be monitored. Condition may require repairs within 1 to 5 years.
- PRIORITY 5 -** Either no defects or only minor defects were found. Repairs not recommended at this time, but condition of structure should be monitored.

*Recommendations and priorities are based on conditions present at the time of this inspection, utilizing industry standards and information made available to us by the Owner. They are based on defects found that may limit the original capacity of the structure. No rating of the structure has been performed. Conditions and standards can and do change, so frequent re-inspection and evaluation is recommended. For whatever reasons if only **partial** Priority 1, 2 and 3 recommended repairs are made to any one or all bridges listed in that category, Osmose accepts no liability. Bridge components are interactive with each other structurally; therefore, substandard members can affect the overall structural integrity of a bridge.*



RECOMMENDATIONS (continued)

Internal and Groundline Preservative Treatment

All of the timber bridges that contain over 20% decay should be in-place preservatively treated to control the existing decay and help reduce costly future repairs. Once decay is established, it continues to grow at an accelerated rate, subsequently leading to substantial section loss and eventual failure. Service records to date have shown that in-place preservative treatment is effective in controlling decay and prolonging the life of timber structures.

Osmose.

DATE: August 1, 2005

FAX

TO: Dave Parkinson

PAGES (including cover): 3

San Pedro & Southwestern RR Co.

Osmose Railroad Services, Inc.
P.O. Box 501
Kearney, MO 64060

PHONE:

FAX: 707-251-8891

FROM: Dave Franz / Dennis Dolan

FAX: (816) 903-9999

PHONE: (800) 784-5282

MESSAGE:

Repair estimates attached per your request.

*The information contained in this document is **CONFIDENTIAL**.
If you receive this document in error, please return it to the sender at the address indicated above.
If you did not receive all pages, please call the sender of this document at the number listed above.*

Osmose® Railroad Services, Inc.**San Pedro & Southwestern Railroad Company****Priority 2 & 3 Bridge Repair Estimates MP 7 to MP 67.9**

<u>Bridge Number</u>	<u>Estimated Repair Cost</u>
7.58	\$ 2,500
7.70	\$ 16,500
8.10	\$ 18,000
9.97	\$ 500
10.44	\$ 5,000
11.30	\$ 220,000
13.50	\$ 17,000
13.70	\$ 7,000
14.16	\$ 5,000
14.67	\$ 11,000
16.23	\$ 15,000
18.10	\$ 105,000
18.94	\$ 5,000
30.45	\$ 20,000
31.00	\$ 5,000
31.20	\$ 500
31.70	\$ 4,000
33.80	\$ 4,000
34.60	\$ 10,000
36.95	\$ 12,000
37.80	\$ 4,000
38.20	\$ 14,000
38.70	\$ 18,000
40.00	\$ 25,000
40.90	\$ 21,000
41.90	\$ 21,000
42.50	\$ 2,500
43.30	\$ 6,000
44.50	\$ 4,000

Bridge Number (cont.)**Estimated Repair Cost (cont.)**

45.70	\$ 29,000
46.40	\$ 7,000
46.90	\$ 6,000
47.30	\$ 7,000
47.75	\$ 1,000
48.40	\$ 4,000
49.10	\$ 19,000
49.50	\$ 3,000
51.40	\$ 6,000
52.90	\$ 8,000
58.80	\$ 15,000
59.10	\$ 11,000
65.44	\$ 6,000
66.41	\$ 5,000
67.58 (M & S)	\$ 6,000
TOTAL ESTIMATED COST	\$ 731,500 (not including mobilization costs)

ATTACHMENT 8



DAVID L. PARKINSON
Chairman and Chief Financial Officer

1109 Jefferson Street
Napa, CA 94558

TEL 707-251-8673
FAX 707-251-8691
CELL 916-717-0106
E-mail dave@arizonarg.com

June 30, 2005

Mr. Mark Jeszli
Vice President, Logistics & Business Development
Chemical Lime
5601 Bridge Street, Suite 200
Fort Worth, TX 76112

Dear Mark:

This letter formalizes our offer to compensate Chemical Lime for certain costs incurred last year to reinstate rail service to your Paul Spur, AZ plant.

The San Pedro & Southwestern Railroad knows of no contractual agreements, written or verbal, committing us to maintain rail service to the plant. We do have a common carrier obligation which has been interrupted by a forced embargo of the line. Under these circumstances we are justified in seeking abandonment due to the economic infeasibility of repairing the bridge. Furthermore, we believe the financial justification for abandoning the line is overwhelmingly in our favor.

In consideration of Chemical Lime not opposing our STB request for an abandonment exemption, we agree to pay Chemical Lime a sum of \$50,000.00 cash. This offer is on the table unless Chemical Lime files opposition to the exemption petition at the STB. If you chose to do so, the offer is withdrawn.

I hope we can settle this matter amicably. Both companies have suffered financially as a result of the recent unfortunate events. I look forward to your response,

Sincerely,

A handwritten signature in dark ink, appearing to read "David L. Parkinson". The signature is fluid and cursive, with a long horizontal stroke extending to the right.

David L. Parkinson
Chairman

cc: John Heffner, PLLC

ATTACHMENT 9



U.S. Department
of Transportation

**Federal Railroad
Administration**

1120 Vermont Ave., N.W.
Washington, D.C. 20590

JUN 10 2005

Mr. David L. Parkinson
Chairman and Chief Financial Officer
San Pedro Southwestern Railroad Company, Inc.
1109 Jefferson Street
Napa, California 94558

Dear Mr. Parkinson:

The Federal Railroad Administration (FRA) is conducting an assessment of the manner in which the San Pedro Southwestern Railroad (SPSR) assures the structural integrity and safety of its railroad bridges. The assessment, which began in February of this year, is being performed by the Area Bridge Safety Specialist of the FRA Office of Safety, and Track Safety Inspectors from FRA and the Arizona Corporation Commission. They were accompanied by representatives of SPSR, to whom they provided findings of the assessment as it progressed.

The assessment revealed that the condition of one bridge in particular, at Milepost 11.3 on the line segment between Fairbank and Benson, Arizona, has degraded to the extent that it presents an unacceptable risk of causing a train accident from structural failure. Bridge 11.3 is a timber pile trestle of eleven spans, with a total length of 154 feet. A detailed investigation of the bridge on February 17, 2005, revealed five of the eleven pile bents have insufficient sound piles to assure their capacity to carry railroad traffic, and that the stringers in ten of the eleven spans are likewise lacking in capacity. The details of the FRA observation report correspond closely with the report of the last inspection by Osmose Wood Preserving Company, which you provided to FRA on June 5, 2005.

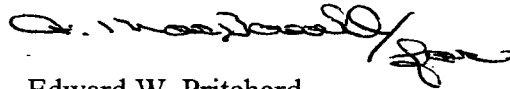
FRA does not have regulations governing the structural condition of railroad bridges, in part, due to the fact that railroad bridge owners have nearly always taken appropriate corrective action when serious bridge deficiencies have been noted by FRA or their own inspectors or engineers. However, FRA has published a policy statement on the safety of railroad bridges. The policy, which contains guidelines, is located in the Federal Track Safety Standards, Title 49, *Code of Federal Regulations*, Part 213, Appendix C, "Statement of Agency Policy on the Safety of Railroad Bridges." While the guidelines found in Appendix C are advisory in nature, please note that the Federal Railroad Administrator has emergency authority to order restrictions and prohibitions necessary to abate any unsafe condition or practice that involves a hazard of death or personal injury. See 49 U.S.C. Section 20104.

FRA bridge safety personnel have determined that the condition of Bridge 11.3 presents that level of unacceptable risk, and that appropriate action should be taken to restrict the operation of trains on the bridge until those conditions are corrected. I therefore recommend that SPSR should voluntarily cease the operation of trains on Bridge 11.3 until the conditions noted to you by FRA have been corrected, and the bridge has been evaluated and found suitable for operation by a Registered Professional Engineer who is competent in the field of timber railroad bridge analysis and rating.

I further request that SPSR provide this office with a copy of the Engineer's evaluation, bearing the embossed seal of the Engineer, when the bridge is returned to service. The evaluation should include the Engineer's recommendation for maximum loads and any operating conditions necessary to ensure the long-term safety and serviceability of the bridge.

Please advise this office no later than Wednesday, June 15, 2005, of the action taken by SPSR to ensure the immediate safety of Bridge 11.3. If you have any questions in this regard, please feel free to contact Gordon A. Davids, P.E., Chief Engineer - Structures, or Theresa M. Galloway, P.E., Structural Engineer, in the FRA Office of Safety. Their telephone numbers are respectively (202) 493-6320 and (202) 493-6220, and their Email addresses are gordon.davids@fra.dot.gov and theresa.galloway@fra.dot.gov.

Sincerely,

A handwritten signature in black ink, appearing to read "E. Pritchard", followed by a stylized flourish or slash.

Edward W. Pritchard
Director, Office of Safety
Assurance and Compliance

VERIFICATION

STATE OF CALIFORNIA) SS
CITY OF NAPA)

DAVID L. PARKINSON, being duly sworn according to law,
hereby deposes and states that (s)he is authorized to make the
Verification, has read the foregoing document, and knows the
facts asserted therein are true and accurate as stated, to the
best of (her)his knowledge, information and belief.

Paul C. Palmer

Subscribed and sworn to before me, a Notary Public, in and for
the City of Napa in the State of California this 2nd
day of August 2005

Jonit Meyer

Notary Public

My Commission expires:

03.30.2008

