

BEFORE THE
SURFACE TRANSPORTATION BOARD

FINANCE DOCKET NO. 34865

ARKANSAS MIDLAND RAILROAD COMPANY, INC.
--PETITION FOR DECLARATORY ORDER--
CADDO VALLEY RAILROAD COMPANY

REPLY COMMENTS

By Decision served May 12, 2006, the Board requested Comments regarding when, if ever, a stock sale triggers section 10907(h). Pursuant to the Board's request, Comments were filed by Caddo Valley Railroad Company ("CVR") and its four shareholders,¹ CertainTeed Corporation and its wholly-owned subsidiary, GS Roofing Products Company, Inc. (collectively referred to hereinafter as "CertainTeed"), and International Paper Company ("IP"). Arkansas Midland Railroad Company, Inc. ("AMR") did not file Comments, choosing instead to rest on the contentions voiced in its Petition for Declaratory Order filed April 14, 2006. No other party has filed Comments.

As was argued in CVR's Comments, the short answer to the Board's inquiry is that section 10907(h) is not triggered by a stock sale. Rather, the only time that this section would be triggered would be when a line, or portion of a line that was acquired pursuant to 49 U.S.C. § 10907, is sold or abandoned by the purchasing carrier. If the line is not abandoned or sold by the purchasing carrier, section 10907(h) is not triggered. Any other result would run afoul of the literal and unambiguous wording that Congress used when it enacted section 10907(h). In this

¹ CVR was incorporated in June 1997 for multiple purposes, which include (a) engaging in the operation of a short haul railroad, (b) conducting any other business enterprise not contrary to law, and (c) exercising all of the powers enumerated in the Arkansas Business Corporation Act. Its shareholders are Gina Garner, Tim Bean, Melanie Hall and Corey Thomason. Each shareholder holds the same number of shares.

respect, it is stressed that neither IP nor AMR has ever addressed the literal wording of section 10907(h). Moreover, they have deliberately disregarded the long-standing statutory distinction between asset sales and stock sales.

I. The Arguments Voiced by AMR and IP Disregard State Corporation Law.

It is well settled that ownership alone of stock of one corporation by another corporation does not create an identity of corporate interests between the two companies, or render the stockholding company the owner of the property of the other company. *Findanque v. American Maracaibo Co.*, 92 A.2d 311, 316 (Del.Ch. 1952) (citing, *Owl Fumigating Corporation v. California Cyanide Co.*, 24 F.2d 718 (D.C.Del. 1928). Or as stated in slightly different terms, when a corporation acquires the shares of another corporation:

the purchasing corporation has the status of a stockholder of the corporation whose shares it has purchased and nothing more. In other words, the purchasing corporation is not the owner of the assets of the other corporation, but is merely a stockholder with all the incidents of such.

Orzeck v. Englehart, 195 A.2d 375 (S.C.Del. 1963). The same result has been stated by the Supreme Court of Arkansas. *See, Lange v. Burke*, 61 S.W. 165 (Ark. 1901).

In this instance, CVR was established in order to insulate its owners from financial risk and to preserve rail service. The Board has previously recognized that both of these reasons are legitimate and substantial business reasons for employing the corporate structure. *Caddo Antoine and Little Missouri Railroad Company -- Feeder Line Acquisition -- Arkansas Midland Railroad Company Line Between Gurdon and Birds Mill, AR*, 4 S.T.B. 610, 635 (2000). What was legitimate in 1997 (when CVR was incorporated) continues to be legitimate today.

In the final analysis, the sale of CVR's stock to any other party is simply that -- a sale of stock to that party and nothing more. If and when Pioneer Railcorp ("Pioneer") purchases the CVR stock, the rail operations will continue to be conducted by CVR and the rail and other

assets will still be owned by CVR. Shippers on the line will receive needed rail service from CVR, which will be the entity legally responsible for rendering such service whether its shares are held by the current owners or by Pioneer or any other party.

II. IP's Arguments are Unsubstantiated, Irrelevant and Immaterial.

As the Board will discover, IP never discusses the literal wording of section 10907(h). Instead, it focuses on unsupported allegations that service provided to it for the past five years has not been as good as the service that it allegedly received from AMR prior to the forced sale of the line. Not only are such allegations unsupported by any specific allegations, but they are irrelevant, especially given the background which underlies this proceeding.

In the first place, IP conveniently ignores the other statutory provisions of section 10907(c)(1)(A) and (B) (emphasis added) that required the Shippers, in order to prevail, to show that AMR "refuse[d] within a reasonable time to make the necessary efforts to provide adequate service to shippers who transport traffic over such line" and that "the transportation over such line [was] inadequate for the **majority of shippers who transport traffic over such line.**" In short, even if IP may have been receiving exemplary service from AMR prior to the sale of the line to CVR, the quality of the service rendered to that particular shipper was and is immaterial with regard to the statutory provisions of 10907. As the Board found, "AMR appears to provide adequate service to IP on the southernmost portion of the line, but that does not permit a finding that AMR's overall service on the entire Norman Branch was adequate." *Caddo Antoine and Little Missouri Railroad Company -- Feeder Line Acquisition -- Arkansas Midland Railroad Company Line Between Gurdon and Birds Mill, AR*, 4 S.T.B. 326, 337 (1999).

Second, IP's generalized bellyaching provides no grounds for finding that the sale of CVR's stock should provide AMR with the right of first refusal to cherry pick CVR's assets.

Without belaboring the issue, the Board should note that IP has largely regurgitated its earlier submission to which CVR responded as follows:

The last complaint that CVR received about car supply was in September 2004.² At that time, the shortage of centerbeams and boxcars was a nationwide problem. Furthermore, while IP is now attempting to blame CVR for the lack of equipment, IP is well aware that the UP/CVR [Cooperative Marketing Agreement] included a provision that prevented CVR from leasing cars without first obtaining a waiver from UP. Although UP agreed to waive that provision in order to assist IP, and although CVR diligently attempted to locate additional cars in order to assist IP, no cars were available from either UP or from various car manufacturers and leasing companies.

Moreover, if IP truly believed that CVR had failed to provide the type or quantity of cars or a level of service to which IP is entitled, why did it fail to speak up at any time prior to the onset of the well documented rail car supply crisis that prompted the Board to request the major trunk lines to submit operational strategies to meet the peak demand? In this regard, CVR has no record of ever having received any formal complaints about the level of service that it provided to IP between the time it assumed responsibility for operations over the Norman Branch [in September 2000] and the late Summer of 2004, when the car supply shortage became acute nationally.

Furthermore, although CVR was requested by the undersigned to keep a record of any subsequent complaints about the service being provided to IP, no complaints about service have been received since the car supply shortage abated in the early part of 2005. Instead, IP personnel who are located at IP's Gurdon facility have expressed the view that service has been satisfactory. In addition, CVR is informed and believes that IP recently acknowledged to Pioneer that things are "pretty good" in terms of rail service at its Gurdon facility.³

It is telling that despite being alerted to CVR's position, IP did not identify any specific or recent complaint with regard to the "pretty good" service it has consistently received from

² Copies of contemporaneous correspondence between counsel for IP and CVR are attached. The correspondence plainly shows that (i) CVR made reasonable efforts to obtain additional equipment, and (ii) that no equipment was available at that time.

³ CVR, Reply To Pleading Filed By International Paper Company, Inc., Or In The Alternative, Motion To Strike, pp. 2-3, May 9, 2006.

CVR. More importantly, IP was unable to overcome the fact that, since paying the constitutional minimum value for the line (which value was set by the Board) more than three years ago, CVR, unlike AMR, has provided adequate transportation service to *all* of the shippers on the line.

Nor did IP identify any specific grievance that it may have with Pioneer, which is likely to purchase CVR's stock and thereafter exercise control of CVR's operations over the Norman Branch line. Indeed, IP's position appears to be based on the hope that, by supporting AMR, it will be restored to a position where it will once again receive favored service that is superior to that received by its much smaller competitors which are located on the northern end of the Norman Branch line.

Third, IP's Comments are riddled with factual errors, including the baseless statement that "it is the line that AKMD previously serviced that is being sold, not the stock."⁴ IP also errs when it says that "when this line was originally acquired using the forced sale provisions of §10907, the acquiring company was owned by five shippers who were located at the northern end of the branch line that was being acquired."⁵ There is no evidence whatsoever to support IP's contention. IP's further comment that "the only remaining owner of CVR are the Bean Companies" is also baseless.⁶ Although the sole shareholders are members of the Bean family that controls Bean Lumber Company and Curt Bean Lumber, it is incorrect to claim that the Bean Companies own CVR. They do not.⁷

⁴ IP Comments at p. 2.

⁵ *Id.*

⁶ *Id.*

⁷ In any event, IP's factual quibble is irrelevant to the issue here, which is the proper construction of section 10907. Nothing in that section requires that the entity purchasing a line in a directed sale be owned by all affected shippers or by any of them at all. That is yet another reason why the Board should hold that any *subsequent* changes in the stock ownership of that purchaser are of no moment under § 10907.

Last, IP repeats the baseless assertion that it is “being required to cross-subsidize service being provided to shippers on the northern end of the line.”⁸ As CVR previously noted:

That claim is false and highly misleading. Because the rates for all shippers on the line are set by the Union Pacific Railroad pursuant to a Cooperative Marketing Agreement (“CMA”), and not by CVR, there is no basis for IP’s suggestion.⁹ In fact, if all the other shippers on the line were to cease shipping, IP would likely pay the same, if not higher, rates. In any event, the issue is wholly irrelevant to the narrow issue that is before the Board.¹⁰

In short, IP’s Comments add nothing of value to the debate and should be disregarded as not being responsive to the narrow issue of when, if ever, a stock sale triggers section 10907(h). In any event, if IP has any real grievance regarding the rail service it is receiving, there are statutory remedies available to it.

III. AMR’s Arguments are Repudiated by the Statutory Wording Of 10907(h).

At a much earlier stage of the protracted controversy over the Norman Branch line, then Commissioner Simmons made the following observation that is equally apt today: “[a]fter failing in its responsibilities for most of the Norman Branch, AMR now attempts to manipulate the feeder line process and frustrate the self-help initiative of the shippers.” *Caddo Antoine and Little Missouri Railroad Company -- Feeder Line Acquisition -- Arkansas Midland Railroad Company Line Between Gurdon and Birds Mill, AR*, 10 I.C.C.2d 323, 328 (1994). As was the case nearly twelve years ago, AMR’s Petition for Declaratory Order simply represents yet another “attempt to undermine the shippers’ efforts after repeatedly ignoring their desperate appeals for service.” *Id.* at 327.

⁸ *Id.* at p. 3.

⁹ See Letter to Edward D. Greenberg from Richard H. Streeter, dated September 10, 2004, at p. 2.

¹⁰ CVR, Reply To Pleading Filed By International Paper Company, Inc., Or In The Alternative, Motion To Strike, *supra*, at pp. 1-2.

What is most striking about AMR's position, other than its decision not to file Comments, is its failure to address the actual wording of section 10907(h). That language cannot be ignored. The fact of the matter is that when it enacted section 10907(h), Congress limited its application to the sale or abandonment of the line. AMR's silence on this critical point must be attributed to the simple, undeniable fact that nothing in the literal wording of section 10907 triggers the right of first refusal in the case of a stock sale. Moreover, there is no extrinsic or intrinsic evidence to suggest that Congress intended any other result.

Consequently, in seeking to have the Board interfere with the orderly sale of the CVR stock, AMR had to ignore the fact that CVR would not be abandoning the line or any portion thereof. AMR was also forced to disregard the fact that CVR would not be selling the line or any portion thereof as a result of the proposed transaction by which CVR's shareholders would sell their stock to new owners.

What appears to trouble AMR is that if CVR will itself be sold to new shareholders who have extensive expertise with regard to short line operations, AMR will not be able to regain the line and then take advantage of the current high price that it could fetch for the sale of the steel upon abandonment of the line or a portion thereof. In other words, AMR's officious intermeddling was most likely prompted by the hope that if it could delay and prevent the sale of CVR, the current shareholders might be forced to abandon the line -- at which point, AMR would be in a legitimate position to demand its statutory right of first refusal.

The Board should not have tolerated this flagrant abuse of its procedures. Instead, the Board first concern in construing the remedial provisions of the feeder statute should be the shippers on the line who are dependent upon CVR for rail service and who, based on their past

experience, cannot expect AMR to provide them with adequate rail service. As CertainTeed has correctly observed at page 4 of its Comments:

Even if the plain words of section 10907(h) were not so clearly limited to line sales or abandonments, expansion of the first-refusal right to include stock sale proposals would be a peculiarly bad idea because of the business context in which directed sales under the feeder program typically occur. Lines conveyed under the feeder program are inherently more likely to be troubled properties because of neglect by the prior owner who was directed to sell the line – certainly the case here when AKMD owned the Norman Branch.

In this instance, the Board specifically authorized the shippers to incorporate a new corporation that would hold title to the line. *Caddo Antoine, supra*, 4 S.T.B. at 231. That decision was only reached only after the Board concluded that AMR had not provided adequate service to the majority of shippers on the line and that AMR had refused to make the necessary efforts to provide adequate service. Plainly, given the history of the line, AMR's proposed construction of section 10907(h) would place the current shareholders in an absurd and impossible situation. Having determined that management changes are necessary to address the accumulated problems on the Norman Branch, they would have to offer the CVR shares to AMR, the very party who brought the problems on the line to a crisis point in the first place, *before* offering the company to new shareholders who have the known expertise to operate and rehabilitate the line so as to save it from abandonment.

Last, CVR also agrees with the reasoning expressed by CertainTeed regarding the relationship of 10907(g) with 10907(h). After noting that 10907(g) permits any person operating a railroad line acquired under this section to elect "to be exempt from any of the provisions of this part," CertainTeed correctly states (Comments at 5-6) that:

It is highly improbable that Congress, having just granted feeder line operators this extraordinary degree of regulatory freedom under section 10907(g)(1), would turn around in section 10907(h)

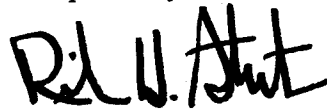
and impose a *sui generis* encumbrance on stock sales of feeder line operators that does not exist for stock sales of any other rail carriers under ICCTA. As illustrated by the situation here, such an encumbrance would frustrate the objectives of the feeder program in several ways – (i) by limiting the options available to feeder-line operators who determine that a management change is necessary to maintain service on the line after its directed sale; (ii) by empowering the former owner to recapture the very line it mismanaged if the buyers in a directed sale “guess wrong” in their initial selection and structuring of line management; and (iii) by enabling that same former owner to dampen the interest of prospective replacement managers who want an equity interest in the feeder line operator.

Given the unambiguous statutory language of section 10907, coupled with the fact that Congress (as well as the Board and its predecessor) has repeatedly differentiated between stock sales and asset sales, it is respectfully submitted that the Board should not seek to plow new ground. Instead, the Board should find that it is consistent with the overall objectives of the feeder development provisions to allow the sale of the stock of a corporation, whose assets include a line of railroad acquired pursuant to the feeder provisions, to new owners without providing a right of first refusal to the former owner who was previously found unable to provide adequate rail service to all but one of the shippers on the line. This is especially the case when the new owners have a recognized expertise in the rehabilitation and operation of short line carriers.

Conclusion

For all the above-stated reasons, the Board should determine that section 10907 is not triggered by a stock sale and forthwith discontinue this proceeding. Because the very pendency of this proceeding is interfering with the sale of CVR’s stock and the ultimate rehabilitation of the Norman Branch line, the Board should serve a discontinuance decision in an expedited fashion. Any other result would simply reward AMR for its disingenuous attempt to further manipulate and frustrate the feeder line process.

Respectfully submitted,

A handwritten signature in black ink, appearing to read "R.H. Streeter", written in a cursive style.

Richard H. Streeter
Barnes & Thornburg LLP
Counsel to Caddo Valley Railroad Company

Dated: June 29, 2006

CERTIFICATE OF SERVICE

I hereby certify that on this 29th day of June, 2006, a true copy of the foregoing was served by e-mail or first class mail, postage prepaid, upon the following:

William C. Sippel
Thomas J. Litwiler (tlitwiler@fletcher-sippel.com)
Fletcher & Sippel LLC
29 North Wacker Drive
Suite 920
Chicago, IL 60606-2832

Daniel A. LaKemper (lakemper@mtco.com)
General Counsel
Pioneer Railcorp
1318 South Johanson Road
Peoria, IL 61607

Mark J. Andrews (Mark.Andrews@strasburger.com)
Strasburger & Price, LLP
1800 K Street, N.W.
Suite 301
Washington, D.C. 20006

Edward D. Greenberg, Esq. (egreenberg@gkglaw.com)
Galland, Kharasch, Greenberg, Fellman & Swirsky, P.C.
1054 Thirty-First Street, NW
Washington, D.C. 20007-4492


Richard H. Streeter