

**BEFORE THE
SURFACE TRANSPORTATION BOARD
WASHINGTON, D.C.**

STB EX PARTE NO. 575 (Sub-No. 1)

DISCLOSURE OF RAIL INTERCHANGE COMMITMENTS

**COMMENT OF THE AMERICAN SHORT LINE AND REGIONAL
RAILROAD ASSOCIATION**

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The American Short Line and Regional Railroad Association (“ASLRRA”) respectfully submits its Comments concerning the Board’s proposed interchange commitment disclosure rules. These comments are submitted in response to the October 29, 2007 Decision by the Board soliciting public comment on the proposed rules.

Statement of Interest

ASLRRA represents approximately 455 class II and class III railroads in the United States, Canada and Mexico as well as numerous suppliers and contractors to the short line and regional railroad industry. ASLRRA thanks the Surface Transportation Board for inviting the comments of interested parties.

COMMENTS

The Proposed Rules Should Be More Narrowly Focused

ASLRRA respects the Board's interest in fostering more transparency with regard to interchange commitments. From written and oral Comments made in other proceedings before the Board it is clear that there are some serious misconceptions in the shipper community concerning the terms of and reasons for interchange restrictions. Limited disclosure of how these arrangements work along with a better understanding of the waiver and appeal process set up by the Railroad Industry Agreement may help reduce or eliminate those misconceptions and at the same time alleviate the mistrust and suspicion which some shippers appear to harbor about interchange commitments. While these are desirable goals, the Board's proposed disclosure requirements demand more than is necessary to reach them.

In its proposal for disclosure of existing interchange commitments in proceedings involving either reasonableness of provisions related to rail carrier sale or lease agreements (section 1114.30), the Board calls for the disclosure not just of the provisions setting forth the terms of the interchange commitment, but a "confidential, complete version of the agreement" containing the provisions of interest upon application by a party and Board approval. ASLRRA believes that because these are necessarily bilateral contractual agreements which are predicated upon the usual confidentiality which typically accompanies acquisition contracts, disclosing provisions other than the interchange commitments would potentially give the inquiring party a commercial advantage by allowing it access to information which, even under the rationale for this

disclosure obligation, that party has no legitimate right to see. Required disclosure should be limited to any provisions in an agreement containing or directly referring to interchange commitments. If more information is needed to understand the interchange commitment than appears on the face of the contractual provision containing or directly referring to it, the inquiring party can always make a motion to the Board to require broader disclosure. That measure of due process would at least give the railroad the opportunity to explain why the additional disclosure is either unnecessary or unfairly damaging to it.

Similarly, the disclosure rules pertaining to proposed acquisitions at sections 1121.3, 1150.33, 1150.43 and 1180.4(g)(4) require the production of a “confidential, complete version of the document(s) containing or addressing that provision or agreement”. While shippers must move the Board to obtain access “to the confidential documents”, the rule does not propose to limit the moving party’s access only to portions of the disclosed documents which pertain to the interchange commitment. The rule merely contemplates steps to assure that the interested party maintains confidentiality. The problem is that the “interested party” is most likely the one from whom sensitive commercial terms should be kept confidential, and asking that party to assure confidentiality is akin to asking the fox to guard the hen house once he is comfortably inside its walls.

The problem is particularly acute with regard to pending sales and acquisitions because a broad disclosure tool becomes a truncheon in the hands of a party more interested in disrupting a transaction than in understanding the interchange commitments contained in it. First, it delays the transaction as the disclosure of unrelated provisions

spawn further requests for disclosure or form the basis for additional motions to delay or revoke previously approved sales and acquisitions. Second, it discourages new transactions altogether by raising the risk of unpredictable delays and disruptions arising from procedural maneuvers completely unrelated to interchange commitments. While delay may be a consequence of the disclosure rules when used legitimately to illuminate an interchange commitment, a broader than necessary rule that needlessly exposes transactions to risks wholly unrelated to the purpose of the rule is both unfair and punitive when the public policy goal can be achieved with a more narrowly drafted requirement. In addition, as in the case of existing interchange commitments, the disclosure of commercially sensitive information beyond the terms of the interchange commitment gives the recipient a negotiating advantage in dealing with the railroad which is a wholly unintended consequence of disclosing the “complete document”. These uncertainties and delays will have and indeed already have had a chilling effect on the creation of transactions with great potential benefit both to the participants and - as the last twenty-five years have demonstrated - to the shipping public as well.

In the broadest sense, it is another step toward rolling back deregulation of the industry to the point where the notice exemption process begins to look more and more like the voluminous application that all railroads filed in every transaction during the era of full regulation in which all details of a transaction were publicly examined – with glacial deliberation. The Board can protect functional deregulation and still achieve its narrow, stated policy goal by limiting what must be disclosed under this rule at least to only those portions of sale and acquisition agreements which relate directly to interchange commitments.

More Guidelines Short of General Rules Would Be Helpful

ASLRRA understands and agrees with the Board's reluctance to adopt a "single rule of general applicability". Each interchange commitment agreed upon between two railroads is a product of the unique circumstances of geography, customer base and railroad operations. If those circumstances are to be examined, ASLRRA believes that it is least harmful to avoid a rigid standard against which every situation will be measured. We also commend the Board's attempt at the same time to "provide general guidance regarding factors the Board will consider in determining the reasonableness of individual interchange commitments". This raises a very fine line on which the Board must walk: meaningful guidance requires some illumination of standards, but too many a priori standards become the equivalent of a "rule of general applicability".

Mindful of that danger, ASLRRA nevertheless believes that a fuller disclosure of the factors the Board will consider in determining the lawfulness of disclosed interchange commitments will be beneficial, especially with regard to new proposed commitments disclosed in connection with proposed rail line acquisitions. Without significant prior guidance, ASLRRA fears that the prospect of a protracted review of interchange commitments the ultimate validity of which is highly uncertain will have a chilling effect on the kinds of transactions small railroad operators will be willing to attempt. Creative but untested or uncertain arrangements will never see the light of day because the transactional costs cannot be justified if the participants cannot reasonably predict the likelihood of consummating the deal.

It appears that the Board has identified four factors it will consider: (1) does the interchange commitment cause or potentially cause, a violation of the Interstate Commerce Act or is it contrary to a particular statute under whose mandate approval is being sought; (2) is it part of a lease or line sale; (3) what is the duration of the restriction; (4) in what ‘manner’ does the interchange commitment discourage interchange with other carriers. The Board notes with apparent disapproval that perpetual or complete bans on interchange with third railroads will get particular scrutiny. This leads ASLRRRA to conclude that in at least those situations, the Board has an inclination about validity related to duration and scope which prospective acquiring lines would be advised to understand before taking the time and expense to negotiate acquisition terms. Similarly, if the ‘manner’ by which an interchange agreement discourages interchange is relevant to the Board, then it would be illuminating and efficient for parties to know which ‘manners’ are disfavored. As another example, the Board indicates that whether the transaction involves a lease or a sale of a line is a relevant factor. If the Board believes that is relevant to the lawfulness of an interchange transaction, then it would be both helpful and efficient to explain how that difference might affect the Board’s view of the interchange commitment.

Besides the desirability of a predictable and reliable guidepost to what interchange commitments the Board would approve, the Board should let the public understand the full range of factors it will consider so that interested parties may suggest additional criteria. ASLRRRA believes that there are other factors which also should be considered, the most important of which is an examination of potential negative consequences the regulatory prohibition against an interchange restriction will have on

the long term level of rail service customers may experience. Conventional wisdom has it that removal of an interchange commitment can only improve service by introducing a second or third interchange partner for the otherwise bound originating or terminating railroad. That conclusion assumes that the carrier operating under the interchange commitment will continue to operate the line, but now with more choices. That assumption may be wrong if the original carrier decides to undo the spin off. Acquiring railroads operating under interchange commitments often seek and regularly obtain waivers of those commitments under the Railway Industry Agreement and thus are able to offer alternative routings to customers, but if the original carrier takes back the line it will assuredly not offer alternative routings, and the customer will ultimately experience both price increases and reduced service alternatives.

Discourage Fishing Expeditions

ASLRRA is concerned that the proposed disclosure rules may be subject to abusive tactics in which shippers or other interested parties use the rules to disrupt pending transactions through “fishing expeditions” which are not based in an actual controversy over service or rates but instead seek a problem to apply to a ready-made remedy. Each of the rules pertaining to proposed acquisitions would allow shippers or other affected parties to obtain access to confidential documents concerning interchange agreements that have been filed with the Board “for use in a proceeding before the Board”. ASLRRA believes it is important to limit parties to obtaining access to confidential documents in *existing proceedings*. In other words, shippers should be required to file an action *before* bringing a motion to obtain confidential interchange

commitment documents for two reasons. First, the small but significant step of filing an action puts the Board and the railroad on notice that an actual claim or controversy exists. This at least reduces the ‘fishing expedition’ potential misuse of the discovery process as a remedy looking for a wrong to justify it. Second, it puts the speed at which the process moves back into the hands of the Board.

The current proposed rule does not make clear whether a proceeding must be filed before or after the motion for disclosure is filed. If the disclosure motion may be brought before an action is filed, the rule does not and probably cannot require a time period during which the shipper must file an action after obtaining the confidential documents. Thus, a shipper has complete control whether or when to bring an action based on the disclosed documents. Meanwhile, the uncertainty surrounding the ultimate validity of the interchange commitment can put the entire transaction on hold while the railroad waits to see what, if anything, the interested party chooses to do with the documentary information. A party interested in foiling a transaction might never need to bring an action to achieve its goal; it can just file a motion requesting the confidential documents and the ensuing uncertainty will have the desired chilling effect. In many cases either a seller or an acquirer will back away if they cannot reasonably predict when – or if- the transaction will close. By clarifying that the disclosure motion must be brought in an *existing* action, the Board can assure that the Railroad has notice that a specific controversy exists, not just a fishing expedition to see what may turn up, and the Board can keep the entire process moving by requiring any motions based on the disclosures be brought within a reasonable time period.

Set Time Limits for Decisions

By the same token, within an existing proceeding once the party obtaining the confidential documents does bring a timely motion based upon the disclosed documents, ASLRRA asks the Board to include in its disclosure a reasonable time limit within which it will rule on that motion. In that way the Railroad will have some certainty about when the controversy will be resolved and can make an informed decision whether the transaction can withstand the delay. As ASLRRA has repeatedly stressed in this Comment, delay and uncertainty are deadly twins when a railroad is attempting to consummate an acquisition or expansion project. Given the delays that will be inherent in the discovery process, ASLRRA suggests that in the case of a motion based on discovery obtained in a notice exemption proceeding for a change of control, the Board should adopt a rule that requires a decision within thirty additional days. Decisions delayed beyond that period (following the other delays resulting from the disclosure procedures) will more than likely kill the transaction without a ruling on the merits of the motion. At the very least railroads filing notice exemptions should have a right to know the substantive reason a notice exemption is denied or revoked before the transaction dies on its own from inaction by the Board.

Measure the Effects of the Proposed Rules on the Rail Industry

In its Comments ASLRRA has attempted to explain how and why the Board's proposed disclosure rules can be narrowed and focused to achieve the Board's public policy goals and still preserve the deregulated environment the Staggers Act and the Interstate Commerce Commission Termination Act created for the small rail industry. At the same

time ASLRRRA greatly appreciates the Board's own explanatory comments which appear to support the value of private, arms length negotiations which result in interchange commitment agreements. They also demonstrate that the Board has heard and understood the rail industry's explanation of the legitimate role of interchange commitments in the contemporary rail era. However, ASLRRRA cannot conclude these Comments without noting its members' growing unease that the Board's action in this matter, limited though it is, does add one more brick to the growing regulatory wall that is rising around the rail industry in a manner that is particularly hurtful to the heretofore burgeoning small railroad industry. Though it is a small step and a small wall, by its rulemaking here the Board does prepare the way to insert itself further into the private negotiations that have been an important part of the free market-based rail renaissance.

ASLRRRA believes that these disclosure rules will have real, measurable and substantive consequences, and alarmingly no one, including ASLRRRA, can predict with certainty what those consequences will be until they have been in effect for a reasonable period of time. For Example, a particular concern to the small railroad industry is the impact the proposed rules will have on existing *lease* arrangements that involve an interchange commitment. As the Board is well aware, many interchange commitments were established in conjunction with long-term leases between class I railroads (as the lessors/owners of the rail lines) and class II and class III railroads that serve the shippers on the leased lines. ASLRRRA believes the proposed disclosure rules will encourage class I railroads to allow longstanding, existing leases that have been renewed for decades to terminate in order to avoid the cost, disruption and uncertainty which scrutiny of the interchange commitments by self interested third parties will bring. Consequently, the

class II and III railroads that operate these leased lines will be less likely to invest in upgrading them, since there is little certainty that they will be able to recoup their capital investments. That in turn would create the opposite result that the Board intends: a likely deterioration in the service provided to shippers. Further, if the class I railroads allow the leases to terminate and take back the lines, shippers will no longer have access to alternative routings under the Railway Industry Agreement, as discussed above. ASLRRRA anticipates that class II and class III railroads and shippers will suffer as a result of these unintended consequences of the proposed rules.

This reversionary scenario should not be dismissed as an unlikely hypothetical. From the small railroad perspective these proposed rules can be seen as regulatory steps to exert disproportionate control over the franchises of small railroads, which are less able to fend them off than the powerful class I corporations. In an environment where leased or subcontracted portions of their systems seem more vulnerable to regulatory taking and control than their wholly owned and operated core franchises, the class I railroads will react accordingly to draw those parts of their networks back into the safety of class I ownership, where they can be defended aggressively.

In addition, ASLRRRA is particularly uneasy about the potentially chaotic and unpredictable legal and operational effects of attempts by the Board to undo or remake interchange commitments that are currently in place and operative. ASLRRRA can find little evidence in the record that the Board has made an in depth analysis of the legal or operational issues it would confront. The Comments of the AAR reveal that the large railroads share the concern that the Board has not adequately addressed the consequences

of regulatory changes to existing interchange commitments, many of which are now long-standing.

In light of its concerns ASLRRRA makes three requests. First, it asks the Board to refine and focus its disclosure rules as ASLRRRA has suggested in these Comments. Second, it urges the Board to commit to a full review of the effects of these rules on the small railroad industry and the service shippers receive after they have been in effect for that reasonable period of time. Finally, it requests that the Board complete its thorough review of what consequences have been unleashed before considering adding more bricks to the regulatory wall ASLRRRA believes is slowly but surely rising. The consequences to rail transportation are too significant to sacrifice a well developed understanding of the effects of these new rules at the altar of regulatory activism.

Respectfully submitted,

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