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June 11, 2008

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The Honorable Anne K. Quinlan, Acting Secretary  
Surface Transportation Board  
395 F Street, S.W.  
Washington, D.C. 20423

Re: Finance Docket No. 35130. *Central Oregon & Pacific Railroad, Inc. -  
Coos Bay Rail Line*

Dear Secretary Quinlan:

We write on behalf of RailAmerica, Inc. ("RailAmerica") and the Central Oregon & Pacific Railroad, Inc. ("CORP") regarding the replies filed in the above-captioned proceeding on June 3, 2008 by the State of Oregon (the "State") and the Oregon International Port of Coos Bay (the "Port"). RailAmerica and CORP are mindful of the Board's prohibition against a "reply to a reply." See C.F.R. § 1104.13(c). However, the replies of the State and the Port contain material misstatements with respect to facts that may be important to the Board's analysis of the issues raised by the April 11, 2008 *Show Cause Order*. In the interest of fairness and the development of a full and accurate record, RailAmerica and CORP respectfully request that the Board accept this letter, which addresses only the most significant of the misstatements of fact set forth in the reply filings.<sup>1</sup>

First, in arguing that CORP has failed to act within a reasonable period of time either to restore service on the Coos Bay Line or to seek to abandon the line, the State asserts that CORP has indicated only that "it *may* seek authority to abandon the line" and that "the railroad is willing, however, to repair the line and restore services, rather than to formally abandon the line, *but only if* the other interested stakeholders will agree to fund a major \$23 million upgrade to the line." State Reply at 3 (emphasis in original). See also *id.* at 27 ("the railroad still does not intend to abandon the line"). These statements misrepresent CORP's clearly-stated intentions.

CORP's most recent proposal for a partnership with the State to finance the repair of the tunnels and to offset continuing operating losses on the Coos Bay Line was rejected by Governor

<sup>1</sup> The replies of the State and the Port are likewise replete with misstatements regarding the governing law and precedents, not the least of which is the Port's suggestion that the common carrier obligation requires a carrier immediately to repair an embargoed rail line whether or not the line has sufficient traffic and revenues to support such repairs. However, RailAmerica and CORP confine this letter to correcting the most egregious factual misstatements in the replies.

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Kulongoski on April 21, 2008. *See* Response of RailAmerica and CORP filed May 12, 2008, Exh 9. Shortly thereafter, at the hearing in *Ex Parte No. 677* on April 24, 2008, UP stated — for the first time — that it would not participate in any cooperative effort to restore service on the Coos Bay Line. As Mr. Lundberg testified, upon receiving those responses, CORP promptly “made a decision following the hearings in *Ex Parte No. 677* to seek to abandon the Coos Bay Line” and “instructed our counsel to file the required notice of abandonment and a formal application seeking authority to abandon the Coos Bay Line at the earliest time permitted under the Board’s regulations.” *See* RailAmerica/CORP Response, V.S. Lundberg at 12. CORP amended its system diagram map on May 8, 2008 to indicate its intent to abandon most of the Coos Bay Line, and it completed the necessary publication and service of its amended system diagram map on May 14, 2008.<sup>2</sup> Under the Board’s regulations at 49 C.F.R. § 1152.13(c), CORP may not file its abandonment application until at least 60 days after that publication requirement was satisfied. In order to comply with the Board’s regulations, CORP will file a notice of intent to file its abandonment application on or about June 16, 2008, and will file the abandonment application on or about July 14, 2008. Thus, the State’s assertions that CORP has indicated only that it “may” seek to abandon the Coos Bay Line, and that CORP “still does not intend to abandon the line” if other parties provide \$23 million to upgrade the line, are not correct. To be clear, CORP will file an application seeking Board authorization to abandon the Coos Bay Line at the earliest time permitted under the Board’s regulations. CORP is no longer pursuing participation by other parties in funding repairs to the tunnels on the line.

As RailAmerica/CORP’s response to the *Show Cause Order* demonstrates, their efforts between September 2007 and April 2008 to seek a solution short of abandonment were clearly reasonable, and did not give rise to an unlawful abandonment. Indeed, “the State does not take issue with the railroad’s conclusion that the conditions of tunnels 13, 15 and 18 on its Coos Bay Line are unsafe nor its decision to cease service.” State Reply at 8 (emphasis added). Moreover, the State explicitly acknowledges that “railroads may look for creative ways, including public-private partnerships, to maintain or upgrade their facilities, and [CORP] was entitled to wait a reasonable period for a reaction to its funding proposal.” State Reply at 22 (emphasis added).

Second, both the State and the Port present inaccurate (and unsupported) estimates of the revenues generated by traffic on the Coos Bay Line. The State alleges that the revenues generated by the Coos Bay Line were approximately \$3.8 million in 2005 and \$3.6 million in 2006. *See* State Reply at 28. The Port contends that the Coos Bay Line generated gross revenues “somewhere in the vicinity of \$2 million to \$3.5 million.” *See* Port Reply at 41. These estimates are overstated. Indeed, the documents submitted by the Port with its Reply indicate that the freight revenues generated by the line are between \$1.9 million and \$2.2 million. *See* Port Reply, Exhibits 4, 37, 38. The State’s revenue estimates appear to be based upon incorrect traffic data. The actual number of carloads on the portion of the Coos Bay Line affected by the embargo (and the subject of CORP’s forthcoming abandonment application) was 5,408 cars in 2004 (down from 7,574 carloads in 2003 - *see* V.S.

<sup>2</sup> The fact that CORP had not placed the Coos Bay Line in Category #1 prior to that time demonstrates that CORP did not intend to abandon the line until it became apparent that its efforts to forge a partnership among interested stakeholders to save the line would not be successful.

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Lundberg at 5), 5,158 cars in 2005, 5,356 carloads in 2006 and 4,026 carloads in 2007. In any event, the suggestion (by both the State and the Port) that the cost of tunnel repairs can be borne by CORP simply because the gross freight revenues generated by traffic on the Coos Bay Line are equal to or greater than the cost of such repairs is nonsensical. The ordinary costs of operating and maintaining the line (even without the extraordinary expenditure required to repair the tunnels) far exceed the revenues earned by CORP from traffic on the line. Indeed, the Port's Exhibits 37 and 38 show that the line is generating operating losses in excess of \$1 million annually.

Third, in responding to CORP's showing that the terms of the agreement under which CORP operates the Coos Bay Line do not permit it to take pricing actions that would assist it in raising capital to upgrade its facilities, the State attributes to UP's Vice President – Law, Michael Hemmer, the statement (purportedly made at the recent hearing in *Ex Parte No. 677*) that UP and CORP are currently renegotiating the terms of that agreement. *See* State Reply at 25 and n. 48. This is not true. The statement attributed by the State to Mr. Hemmer was actually made by RailAmerica's Mr. Lundberg. *See* *Ex Parte No. 677, Common Carrier Obligation of Railroads*, April 25, 2008 Tr at 115 (testimony of Paul Lundberg). Mr. Lundberg's statement did not refer specifically to the status of the CORP-UP agreement. Rather, Mr. Lundberg offered the general observation that any short line carrier that operates under a "handling line carrier" arrangement that restricts its ability to raise capital might approach the Class I carrier on whose behalf it operates an unprofitable rail line to seek renegotiation of the terms of that arrangement. *See id.* at 113-115. Neither Mr. Lundberg nor Mr. Hemmer testified that UP and CORP are currently renegotiating the terms of their agreement – indeed, no such discussions are taking place.

Fourth, both the State and the Port assert (incorrectly) that CORP's public/private partnership proposals would have required other stakeholders to "guarantee" that CORP earned a "profit" from operating the Coos Bay Line. *See* Port Reply at 8 (CORP has "demanded guaranteed profits in the form of an ongoing subsidy"), 32 (CORP seeks a "multi-million dollar commitment from the state to cover all of CORP's operating expenses and guarantee a profit"); State Reply at 3 (CORP seeking a "guaranteed profit subsidy"). These assertions are simply not true. Under its various public/private partnership proposals, CORP sought a subsidy to offset any operating losses that it incurred in providing service over the Coos Bay Line. Both the State and the Port are fully aware of that fact. *See* Port Reply, Exhibit 31, Letter dated February 12, 2008 from Governor Kulongoski to P. Lundberg (acknowledging that CORP sought "an ongoing subsidy for operating losses on the line").

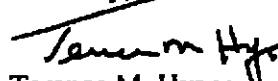
Fifth, the Port's claim that CORP declined to participate with the Port in a joint application for funding to rehabilitate the Coos Bay Line tunnels (and to clear them for double-stack trains) is incorrect. In particular, CORP's Mr. Hawksworth has no recollection of a conversation with Port witness Callery regarding participation by the Port in such an application, nor did Mr. Hawksworth tell Mr. Callery that the tunnels "were in good condition and did not need significant rehabilitation." *See* Port Reply, V.S. Callery at 2. Indeed, the amount of funding mentioned by Mr. Callery (\$3.5 million) would not have been nearly enough to cover the cost of such tunnel clearance work. As the 1994 Shannon & Wilson report submitted by the Port indicates, the cost of rehabilitating and

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clearing the tunnels on the Coos Bay Line for double-stack operations would have been \$8 million even in 1994. *See* Port Reply, Exhibit 5 at 3

Finally, the Port's assertion that there has been "sustained and substantial public investment in CORP" in recent years, and that CORP's failure to repair the Coos Bay Line tunnels "[has] deprived the community and the state of an honest return on their already-generous investment in the railroad" (Port Reply at 22) is likewise incorrect. The public grants cited by the Port in support of this allegation were, in almost every instance, provided to parties other than CORP for projects that primarily benefited those parties (and which generated, at best, peripheral benefits for the railroad). For example, the Port refers to approximately \$16 million in funding that it has received to repair and upgrade the rail bridge that crosses Coos Bay. Port Reply at 19-20. As the Port acknowledges, that bridge is owned by the Port, not CORP, and the primary beneficiary of that funding was the Port itself. Likewise, the construction of the North Spit spur line in 2004-2005 was funded with public money provided to the Port, not CORP. *Id.* at 20. While that project helped to generate a modest amount of additional rail traffic for CORP, it was primarily an economic development project for the benefit of the Port and local businesses. Indeed, as the Port's Reply indicates, the only direct public funding provided to CORP for purposes related to the Coos Bay Line during this period were two State of Oregon grants for track and tie work, one for \$300,000 in 2003 and another for \$400,000 in 2005. *Id.* CORP's more recent application (under the "ConnectOregon" program) for funding to address required track, tunnel and bridge work on the line was not approved.<sup>3</sup>

Sincerely,



Terence M. Hynes  
*Counsel for Central Oregon & Pacific  
Railroad, Inc. and RailAmerica, Inc.*

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cc: Parties of Record

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<sup>3</sup> The Port's assertion that CORP's most recent ConnectOregon application was denied "presumably because such work was considered maintenance or ongoing operations" (Port Reply at 15) is utter speculation. The State did not provide any indication to CORP that its decision was based upon such a rationale. Rather, CORP was advised verbally (without explanation) that the State was approving one of the two ConnectOregon applications that CORP submitted in 2006. The Port's assertion is belied by the fact that, in the same year, the Milton-Freewater Railway (which operates in northeast Oregon) was awarded \$372,000 in ConnectOregon funding for projects that included rehabilitation of a bridge.