

SERVICE DATE - JUNE 23, 1997

SURFACE TRANSPORTATION BOARD

DECISION

STB Finance Docket No. 33350

SOO LINE RAILROAD COMPANY—PETITION FOR DECLARATORY ORDER

Decided: June 19, 1997

Soo Line Railroad Company (Soo) filed a petition for a declaratory order to determine if its acquisition of a 33⅓% ownership interest in I&M Rail Link, LLC (I&M) requires approval under 49 U.S.C. 11323, *et seq.* Soo indicates that its petition addresses issues that the Board had deferred ruling on in *I&M Rail Link, LLC—Acquisition and Operation Exemption—Certain Lines of Soo Line Railroad Company D/B/A Canadian Pacific Railway*, STB Finance Docket No. 33326 (STB served Apr. 2, 1997) (*I&M Acquisition*).

BACKGROUND

In STB Finance Docket No. 33326, I&M, a newly-created noncarrier limited liability company, filed a notice of exemption under 49 CFR 1150.31 to acquire from Soo and to operate approximately 1,109 miles of rail lines and 262 miles of trackage rights in the States of Minnesota, Wisconsin, Illinois, Iowa, Kansas, and Missouri. In STB Finance Docket No. 33327, a directly related notice of exemption under 49 CFR 1180.2(d)(2) was filed by Dennis Washington, Dorn Parkinson, Mort Lowenthal, William H. Brodsky, J. Fred Simpson, and Thomas J. Walsh (Washington Organization) seeking authority to continue in control, through stock ownership and management, of both I&M and Montana Rail Link, LLC (MRL), an existing Class II carrier, following I&M's acquisition of the Soo lines. In that notice, the Washington Organization stated that Mr. Washington would be the majority owner of both I&M's parent, I&M Holdings, LLC (Holdings), and MRL, and that the other individuals named in the notice would act as officers and/or directors of both I&M and MRL.¹ As part of the transaction, Soo acquired a 33⅓% membership interest in I&M from Holdings for \$18,333,333.² Soo's membership interest in I&M was placed directly into an irrevocable voting trust, pending the Board's decision on whether Soo's 33⅓% interest constitutes control of I&M. The remaining 66⅔% interest in I&M is held by Holdings, which is wholly owned by Mr. Washington.

According to Soo, the rights and obligations of I&M's membership interest holders are contained in a Members Agreement and an Operating Agreement executed by Soo and Holdings. Under those agreements, Holdings has the right to nominate five of the seven members of I&M's Board of Managers, and Soo may nominate the other two members.³ The Operating Agreement provides that "the Board of Managers shall have the sole right and authority to exercise the powers of the Company, and to manage, control and make all decisions affecting the business and affairs of the Company," and that "[Soo] shall not be involved in the operations or management of the Company."

Soo indicates that the agreements also contain provisions to protect its interest as a minority owner in I&M. The agreements relating to I&M's organization specify that six extraordinary corporate actions by I&M would require approval by a supermajority of six board members. These

¹ In STB Finance Docket No. 33328, MRL filed another directly related notice of exemption under 49 CFR 1180.2(d)(2) seeking authority to control I&M. MRL's notice was subsequently dismissed as moot.

² Apparently, a "membership interest" in a limited liability company such as I&M is equivalent to ownership of common stock in a corporation.

³ The Board of Managers of a limited liability company is the equivalent of the Board of Directors of a corporation.

extraordinary actions are: (i) the acquisition by I&M of an additional rail line for more than \$5 million; (ii) a major corporate reorganization by I&M involving the sale, purchase or lease of assets valued at more than \$50 million; (iii) a financing or refinancing by I&M exceeding \$50 million; (iv) any “insider” transaction between I&M and the Washington Organization (or its affiliates); (v) any major change in the policy regarding distributions by I&M to its members; and (vi) dissolution of I&M. In addition, neither Holdings nor Soo may transfer its interest in I&M without the consent of the other party. Finally, Soo says, the Operating Agreement gives it a preemptive right to acquire a share of any additional membership interests issued by I&M proportionate to Soo’s current percentage interest, and prohibits I&M from issuing additional ownership interests (or other rights) that would have the effect of diluting Soo’s ownership percentage. Soo indicates that these contractual provisions protect it by prohibiting (without Soo’s consent) extraordinary actions by I&M’s management that might jeopardize Soo’s \$18 million investment in I&M.

In *I&M Acquisition*, the Board denied petitions by United Transportation Union (UTU), the Transportation•Communications International Union (TCU), and the City of Ottumwa, IA, joined by UTU officials Patrick C. Hendricks and Joseph C. Szabo, (Ottumwa) (jointly, respondents) to revoke the exemptions for I&M’s line acquisition and Washington Organization’s control of I&M. The Board also rejected arguments by UTU, TCU, and Ottumwa that the section 10901 class exemption did not apply to I&M’s line acquisitions. Additionally, the Board disagreed with their contention that Soo’s option to acquire a minority interest in I&M and enter into commercial arrangements with I&M rendered the line sale transaction a “sham” and should be regarded as a transaction under 49 U.S.C. 11323. However, the Board deferred ruling on the control implications of Soo’s acquisition of a minority interest in I&M. The Board indicated that Soo had promised that it would request a declaratory order addressing the control issue, which would enable all interested persons to submit pertinent evidence and argument.

DISCUSSION AND CONCLUSIONS

Under the Board’s authority in 5 U.S.C. 554(e) and 49 U.S.C. 721, a proceeding is instituted to resolve the controversy here. A procedural schedule is set forth below. Soo has essentially filed its opening statement with its petition. Soo has requested an expedited procedural schedule, suggesting that responsive evidence and argument from interested parties be due 20 days after service of the Board’s decision instituting the proceeding, and that Soo’s reply be due 10 days later.

UTU, TCU, and Ottumwa object to the proposed schedule. UTU and TCU do not object to the 20-day limit for responding, but they are opposed to having Soo file a reply. They contend that a filing by Soo is unnecessary and is comparable to a reply to a reply, which is not permitted by 49 CFR 1104.13(c). Ottumwa contends that the 20-day reply period is inadequate, particularly if there is extensive discovery.

Soo’s recommended procedural schedule will be adopted. Allowing Soo to close the record is not a reply to a reply, but a rebuttal. Soo’s pleading would be confined to a rebuttal of respondents’ evidence. *See* 49 CFR 1112.2. A rebuttal by Soo is reasonable and necessary to develop a complete record. Moreover, a 20-day limit for filing replies is reasonable, notwithstanding Ottumwa’s mention of a possible need for discovery. As noted in *I&M Acquisition*, the respondents have already engaged in discovery and submitted argument and evidence on Soo’s possible control of I&M in that proceeding. Indeed, UTU has already filed its reply to the petition for declaratory order. In addition, other respondents have had the benefit of receiving copies of Soo’s opening statement well in advance of this decision. Under these circumstances, the 20-day limit appears to be an adequate amount of time to prepare and file a reply.

A copy of this decision will be served on all parties in STB Finance Docket No. 33326.

This action will not significantly affect either the quality of the human environment or conservation of energy resources.

It is ordered:

1. A declaratory order proceeding is instituted. This proceeding will be handled under the modified procedure. All parties must comply with the Rules of Practice, including 49 CFR 1112 and 1114.

2. Reply comments are due by July 13, 1997. By that date, UTU may supplement, if it wishes, the reply that it filed on June 18, 1997.

3. Soo's rebuttal comments are due by July 24, 1997.

4. This decision is effective on its service date.

5. A copy of this decision will be served on all parties in STB Finance Docket No. 33326.

By the Board, David M. Konschnik, Director, Office of Proceedings.

Vernon A. Williams
Secretary