

SURFACE TRANSPORTATION BOARD

DECISION

Docket No. FD 35491

SANTA CRUZ REGIONAL TRANSPORTATION COMMISSION—PETITION FOR
DECLARATORY ORDER

Decided: August 22, 2011

On April 8, 2011, Santa Cruz Regional Transportation Commission (Santa Cruz), a noncarrier, filed a petition for declaratory order (Petition) asking the Board to determine that it does not have regulatory authority over Santa Cruz's proposed acquisition of the Santa Cruz Branch line (the Line). The Line, which is owned by Union Pacific Railroad (UP), is approximately 30.957 miles long. It runs between milepost 0.433, near the east boundary of Salinas Road, and milepost 31.39, near the Highway 1 crossing at Davenport, Cal. in Santa Cruz County, Cal.

Santa Cruz states that it is a public agency created under the laws of the State of California and that it is not, and does not wish to become, a carrier. However, Santa Cruz wants to preserve freight rail service on the Line and to allow the development of tourist excursions and other public uses of the Line. To that end, Santa Cruz claims that, under the proposed transaction, it would acquire the physical assets of the Line, while UP would retain the common carrier obligation. At closing of the sale, UP would simultaneously transfer its retained easement to Sierra Northern Railway (Sierra), which currently leases the line from UP. Sierra N. Ry.—Lease & Operation Exemption—Union Pac. R.R., FD 35331 (STB served Dec. 17, 2009). Sierra filed a verified notice of exemption, which is now effective, to acquire the easement. Sierra N. Ry.—Acquis. & Operation Exemption—Union Pac. R.R., FD 35490 (STB served April 21, 2011).

Santa Cruz submitted copies of the transaction documents to the Board as an attachment to its petition. Santa Cruz would acquire the physical assets of the Line pursuant to a Purchase and Sale Agreement¹ and Quitclaim Deed² with UP. The Quitclaim Deed reserves for UP what Santa Cruz describes as a perpetual, exclusive easement for the purpose of conducting freight rail operations on the Line. The Purchase and Sale Agreement provides that UP would assign its easement to Sierra. UP would assign the easement to Sierra through the Assignment of Freight

¹ Santa Cruz Pet., Attach. 2.

² Santa Cruz Pet., Attach. 2, Ex. D.

Easement.³ Santa Cruz and Sierra would enter into an Administration, Coordination, and License Agreement (ACL Agreement)⁴ that would govern their relationship.

In the Petition, Santa Cruz claims that, if the transaction were consummated, it would acquire only the physical assets underlying the Line. Santa Cruz further claims that it would not acquire either the right or the obligation to provide common carrier freight rail service and that it would not hold itself out to provide, and is incapable of providing, such service. Santa Cruz states that, upon completion of the transaction, Sierra would possess the easement to provide freight rail service on the Line. Therefore, Santa Cruz requests that the Board declare that the transaction does not require the Board's authorization and that Santa Cruz would not become a common carrier as a result of the transaction. In support, Santa Cruz cites Maine Department of Transportation—Acquisition & Operation Exemption—Maine Central Railroad (State of Maine), 8 I.C.C. 2d 835 (1991), and a number of cases in which the Board found that the transfer of rail assets did not involve the transfer of a common carrier obligation.

The question presented is whether the Board's regulatory approval is required for Santa Cruz to acquire the assets of the Line, including the right-of-way, track, and physical assets. The acquisition of an active rail line and the common carrier obligation that goes with it ordinarily require Board approval. Where the acquiring entity is a noncarrier, the standard for approval is set out in 49 U.S.C. § 10901. However, State of Maine and its progeny hold that the sale of the physical assets of a rail line by a carrier to a state or other public agency does not constitute the sale of a railroad line within the meaning of § 10901 when the selling carrier: (1) retains a permanent, exclusive freight rail operating easement giving it the right and common carrier obligation to provide freight rail service on the line, and (2) has sufficient control over the line to carry out its common carrier operations. When the seller retains the common carrier obligation and control over freight rail service, our precedent holds that ownership of the railroad line remains with the selling carrier for purposes of § 10901(d)(4). For a transaction to fall within that precedent, however, the terms of the sale must protect the seller from undue interference by the purchaser with the provision of common carrier freight rail service. Mass. Dept. of Transp.—Acquis. Exemption—Certain Assets of CSX Transp., FD 35312, slip op. at 5 (STB served May 3, 2010), aff'd sub nom. Bhd. of R.R. Signalmen v. STB, 638 F.3d 807 (D.C. Cir. 2011). The seller may transfer its easement to a third-party operator as long as the third-party operator obtains the common carrier rights and obligation along with sufficient contractual rights to meet that obligation. Mass. Coastal R.R. – Acquis. – CSX Transp. Inc., FD 35314, slip op. at 3-5 (STB served Mar. 29, 2010). Therefore, in determining whether Santa Cruz would become a rail carrier if the transaction were completed, the Board will look to whether Sierra would obtain a permanent, exclusive easement and would have sufficient interest in and control over the Line to permit it to carry out the common carrier obligation.

³ Santa Cruz Pet., Attach. 4.

⁴ Santa Cruz Pet., Attach. 5.

There are two aspects of the transaction documents that potentially run afoul of the State of Maine precedent and thus could disqualify Santa Cruz from invoking it.

First, as noted above, a State of Maine transaction requires the seller to retain a permanent, exclusive freight rail operating easement, which, as here, may be transferred to a third-party operator. However, language in this easement suggests that the property interest created under the transaction would be neither permanent nor exclusive. For one thing, the easement does not contain any language indicating that it is exclusive; rather, the easement is explicitly “made subject to the unrecorded [ACL Agreement] The [ACL Agreement] includes terms and conditions governing . . . expiration and termination of the [ACL Agreement].”⁵ Moreover, the easement is not permanent; rather, the ACL Agreement that governs the easement, by its terms, expires after 10 years and may be terminated for default or for nonuse of the freight easement.⁶ To be consistent with State of Maine, the expiration of its operating agreement cannot impair the permanence of the freight rail operating easement. Moreover, it must be set up so that the easement cannot be abandoned or freight rail service permanently discontinued without Board approval.

Second, a State of Maine transaction requires the carrier to have sufficient control over the line to carry out the common carrier obligation and to be protected from undue interference with common carrier operations. Language in the ACL Agreement, however, indicates that Santa Cruz could have the ability to unduly interfere with common carrier operations. Section 6.2 states that

Sierra may, at its cost and expense, modify or improve the Freight Easement Property and Railroad Facilities as needed to accommodate its Freight Service or Tourist Service; provided, however, that Sierra first obtains [Santa Cruz’s] written approval of Sierra’s plans for such modifications and improvements, which approval may be granted or withheld in [Santa Cruz’s] sole and absolute discretion.⁷

Thus, Santa Cruz apparently could deny Sierra the ability to modify or improve the rail property, even when doing so is necessary to accommodate freight service. In addition, Section 6.3 states that “[t]he parties agree that Sierra will need to identify and construct additional maintenance and storage locations on the Property, which Sierra may do as needed, subject to applicable law and [Santa Cruz’s] prior written consent, which consent may be granted or withheld in [Santa Cruz’s] sole and absolute discretion.”⁸ Section 6.3 is objectionable for the same reason as Section 6.2.

⁵ Santa Cruz Pet., Attach. 2, Ex. D (emphasis added).

⁶ Santa Cruz Pet., Attach. 5, § 8.1, 8.2.

⁷ Santa Cruz Pet., Attach. 5, § 6.2 (emphasis added).

⁸ Santa Cruz Pet., Attach. 5, § 6.3 (emphasis added).

Other provisions also appear to vest significant control in Santa Cruz. Sections 4.1 and 4.2 provide that any agreements concerning the operation of the railroad facilities, such as track agreements, grade crossing agreements, and other operating agreements, are “subject to [Santa Cruz’s] prior written consent and [are] to be documented by Sierra using forms approved by [Santa Cruz].” Similarly, section 7.1.2 states that

[t]he parties agree that Sierra will need to identify such temporary laydown locations on the Property, which Sierra may do as needed, subject to applicable law and [Santa Cruz’s] prior written consent. Sierra shall also notify [Santa Cruz] of the expected duration of each such use. If subsequently [Santa Cruz] reasonably objects to any specific use of laydown space by Sierra or its shipper, Sierra shall as soon as practicable discontinue that use of such laydown space.

Sections 4.1, 4.2, 6.1, 6.2, and 7.1.2 of the ACL Agreement appear to give Santa Cruz the ability to unduly interfere in freight operations.

Santa Cruz’s efforts to maintain service over the Line are commendable. In furtherance of those efforts, Santa Cruz may submit a modified Quitclaim Deed and ACL Agreement by September 7, 2011, that removes, revises, or clarifies the language discussed above that calls into question the permanence and exclusivity of the freight rail operating easement and appears to give Santa Cruz the ability to unduly interfere with operation of the Line. Should Santa Cruz choose not to submit a modified Quitclaim Deed and ACL Agreement by September 7, 2011, or a request to extend the filing date, the Board will render a decision based on the existing record.

If Santa Cruz desires assistance in addressing the potential concerns noted in this decision, the Board’s Office of Public Assistance, Governmental Affairs, and Compliance may be contacted at (202) 245-0238.

It is ordered:

1. Santa Cruz may submit a Quitclaim Deed and ACL Agreement by September 7, 2011.
2. This decision is effective on its service date.

By the Board, Joseph H. Dettmar, Acting Director, Office of Proceedings.