

SURFACE TRANSPORTATION BOARD

DECISION

Docket No. FD 35449

TENNESSEE SOUTHERN RAILROAD COMPANY, PATRIOT RAIL, LLC, PATRIOT RAIL HOLDINGS LLC, AND PATRIOT RAIL CORP.—CORPORATE FAMILY TRANSACTION EXEMPTION—SACRAMENTO VALLEY RAILROAD, LLC AND PIEDMONT & NORTHERN RAILWAY, LLC

Decided: March 6, 2012

Digest:<sup>1</sup> This decision denies Sierra Northern Railway's request to revoke the Board's authority that allowed Patriot Rail, LLC to restructure its corporate family.

BACKGROUND

On November 22, 2010, Patriot Rail, LLC (PRL), Patriot Rail Holdings, LLC (PRH), Patriot Rail Corp. (Patriot), and Tennessee Southern Railroad Company (Tennessee Southern) (collectively, Patriot Rail),<sup>2</sup> filed a verified notice of exemption (2010 Notice) under 49 C.F.R. § 1180.2(d)(3) to permit a corporate family restructuring. Under that restructuring, two rail carrier subsidiaries of Patriot, Sacramento Valley Railroad, Inc. (SAV) and Piedmont & Northern Railway, Inc., would be converted from corporations into limited liability companies and placed under the direct control of Tennessee Southern. In its verified notice of exemption, Patriot Rail indicated that the proposed transaction would allow PRL and its corporate family to make use of certain tax benefits, thereby improving the financial viability of the corporate family. Notice of the exemption was served and published in the Federal Register on December 8, 2010 (75 Fed. Reg. 76,520), and the exemption took effect on December 22, 2010.

At the time of the filing of the 2010 Notice, Patriot was involved in litigation in federal district court against Sierra Northern Railway (SERA), and SERA's parent company, Sierra Railroad Company (Sierra). This litigation, which remains ongoing, involves, among other

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<sup>1</sup> The digest constitutes no part of the decision of the Board but has been prepared for the convenience of the reader. It may not be cited to or relied upon as precedent. Policy Statement on Plain Language Digests in Decisions, EP 696 (STB served Sept. 2, 2010).

<sup>2</sup> PRL directly controls PRH (a noncarrier), which in turn directly controls Patriot (also a noncarrier). Patriot directly controls Tennessee Southern, a class III railroad, as well as several other class III railroads.

things, a claim concerning continued rail service over approximately seven miles of rail line in McClellan Business Park (MBP), an industrial park (formerly McClellan Air Force Base) in Sacramento County, Cal. SERA previously operated the line until MBP terminated SERA's licensing and operating agreement.<sup>3</sup> MBP subsequently sought bids for continued rail service and ultimately awarded PRL the right to provide rail service in MBP. Prior to PRL's submitting its bid, Sierra and PRL were engaged in negotiations for PRL's purchase of Sierra and SERA. In the court litigation, Sierra claims that PRL, in partial reliance on the proprietary financial and operating data obtained during negotiations, organized SAV so that it could "improperly and unlawfully deny SERA the ability to render service as a rail carrier"<sup>4</sup> in MBP. Sierra seeks more than \$15 million in compensatory damages, statutory treble damages, punitive damages, and the return to SERA of the right to provide rail service in MBP. That ongoing litigation is scheduled for trial in July 2012.

On December 7, 2011, SERA filed a petition to "nullify" Patriot Rail's corporate family exemption pursuant to 49 U.S.C. § 10502(d) and 49 C.F.R. § 1180.4(g)(ii). SERA asserts that the 2010 Notice contained false or misleading information—specifically, that the purpose for Patriot Rail's corporate family restructure was not, as the notice stated, to gain certain tax advantages, but rather to secure greater protection of Patriot Rail's assets under the Delaware Limited Liability Company Act in anticipation of a judgment against Patriot Rail in the pending federal court action.

On December 27, 2011, Patriot Rail replied to SERA's petition, asserting that SERA had not shown that the 2010 Notice contains false or misleading information or that regulation is needed to carry out the rail transportation policy under 49 U.S.C. § 10101. Patriot Rail also contends that the purpose of its corporate family exemption was indeed, as the notice stated, to obtain certain tax benefits and to maximize the financial strength of all members of its corporate family, not to shield its assets from a speculative judgment in favor of SERA in the court litigation. With its reply, Patriot Rail supplied a verified statement from Bennett Marks, Executive Vice President and Chief Financial Officer of PRL.

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<sup>3</sup> On December 7, 2011, Sierra and SERA filed a complaint with the Board pursuant to 49 U.S.C. §§ 10702(2) and 10704(b) asserting that SAV, MBP, and the County of Sacramento engaged in unreasonable practices by preventing SERA from operating in the business park and failing to seek adverse discontinuance of SERA's operating authority there. See Sierra R.R. & Sierra N. Ry. v. Sacramento Valley R.R., McClellan Bus. Park, & Cnty. of Sacramento, NOR 42133. On December 27, 2011, SAV answered Sierra's complaint and on January 17, 2012, filed a motion to dismiss, which is currently pending.

<sup>4</sup> Sierra Pet. at 4.

## DISCUSSION AND CONCLUSIONS

Although referring to its petition as one to “nullify” the exemption, Sierra cites the standards for revoking a petition under 49 U.S.C. § 10502(d) and 49 C.F.R. § 1180.4(g)(ii). Thus, we will consider Sierra’s petition as a petition to revoke. Under 49 U.S.C. § 10502(d), the Board may revoke an exemption, in whole or in part, if it finds that regulation is necessary to carry out the rail transportation policy (RTP) of 49 U.S.C. § 10101. When, as here, an exemption has become effective, a revocation request is treated as a petition to reopen and revoke, and, under 49 C.F.R. § 1115.3(b), must state in detail whether revocation is supported by material error, new evidence, or substantially changed circumstances. See New York Cent. Lines—Aban. Exemption—in Montgomery & Schenectady Cntys., AB 565 (Sub-No. 14X) (STB served Jan. 22, 2004). The party seeking revocation has the burden of showing that the criterion is met. See 49 C.F.R. § 1121.4(f). Petitions to revoke must be based on reasonable, specific concerns demonstrating that reconsideration of the exemption is warranted and that more detailed scrutiny of the transaction is necessary. See Consol. Rail Corp.—Trackage Rights Exemption—Mo. Pac. R.R., FD 32662 (STB served June 18, 1998). In addition, under 49 C.F.R. § 1180.4(g)(ii), the Board “shall summarily revoke” an exemption containing false or misleading information that is brought to the Board’s attention. See 49 C.F.R. § 1180.4(g)(ii). As the party seeking revocation, SERA has the burden of demonstrating that the exemption authority should be withdrawn.

As discussed below, we find that SERA has failed to demonstrate that the 2010 Notice contained false or misleading information. Further, SERA has failed to demonstrate, through a showing of material error, new evidence, or substantially changed circumstances, that revocation of the exemption is necessary to carry out the RTP. Moreover, the record does not provide a sufficient basis to persuade us that further proceedings are warranted.<sup>5</sup> Thus, SERA’s petition to revoke will be denied.

First, SERA has not shown that the 2010 Notice contained false or misleading information. SERA claims that Patriot Rail’s real purpose for filing the 2010 Notice was not to obtain certain tax benefits but to provide greater protection of Patriot Rail’s assets in anticipation of a judgment against Patriot Rail in federal district court. That assertion is based on (1) the fact that Patriot Rail’s notice was filed during the pendency of the court litigation; and (2) unsupported speculation about what Patriot Rail allegedly “knew” about what SERA claims would be the effect of the restructuring on Sierra’s ability to collect on a speculative future judgment in its favor in the federal court action. SERA does not dispute that the restructuring would have the tax benefits that Patriot Rail claimed in its notice or that Patriot Rail has, in fact, reaped those benefits. Nor has SERA provided any support for its assertion that there was another motive for PRL’s corporate restructuring. On the other hand, Patriot Rail has provided a

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<sup>5</sup> Pursuant to 49 U.S.C. § 10502(d), the Board must decide whether to begin a revocation proceeding within 90 days of the filing of the petition for revocation.

verified statement of PRL's Vice President and Chief Financial Officer, Bennett Marks, representing that (1) the restructuring of some of Patriot Rail's carriers, including SAV, was implemented in order to take advantage of certain tax benefits available from the sale of tax credits under a limited liability structure; (2) obtaining those tax benefits was the sole reason for reorganizing those Patriot Rail railroads, including SAV; and (3) as a result of the reorganization, Patriot has, in fact, sold tax credits.

Second, SERA has not demonstrated that the notice of exemption should be revoked to carry out the RTP under 49 U.S.C. § 10101. Here, SERA has not attempted to identify any relevant aspect of the RTP that would be fulfilled through revocation or explain why applying an exempted statutory provision to this corporate family transaction is necessary. SERA also does not articulate any reasonable, specific concerns demonstrating how more detailed scrutiny of the transaction is needed, nor has it been shown that revocation is supported by material error, new evidence, or substantially changed circumstances. To the contrary, as discussed above, SERA's assertions are founded only upon unsubstantiated speculation, which, in the face of sworn evidence to the contrary, is insufficient to warrant further scrutiny.

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

It is ordered:

1. SERA's petition to revoke is denied.
2. This decision is effective on its date of service.

By the Board, Chairman Elliott, Vice Chairman Mulvey, and Commissioner Begeman.