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SERVICE DATE – JULY 16, 2007

SURFACE TRANSPORTATION BOARD

DECISION

STB Docket No. AB-534 (Sub-No. 3X)

LAKE STATE RAILWAY COMPANY–ABANDONMENT EXEMPTION–  
RAIL LINE IN OTSEGO COUNTY, MI

Decided: July 13, 2007

By petition filed on March 28, 2007, the Lake State Railway Company (LSRC) seeks an exemption under 49 U.S.C. 10502 from the prior approval requirements of 49 U.S.C. 10903 to abandon 4.15 miles of rail line in Otsego County, MI (the Line). The Line is the northernmost portion of the carrier's Mackinaw Subdivision main line, extending from milepost MP 116.8 (where the Line crosses East McCoy Road) to the end of the main line at milepost MP 120.95. Notice of the petition was served and published in the Federal Register at 72 FR 19229 on April 17, 2007.

Opposing comments were filed by Northern Energy, Inc. (NEI), a shipper on the Line; by the City of Gaylord, MI (City); and by the Otsego County Economic Alliance (Alliance). The State of Michigan Department of Natural Resources (Department) filed a request for imposition of a public use condition and for issuance of a notice of interim trail use (NITU). LSRC filed a reply to the City's comments.

As explained below, we will deny the petition because the record is inadequate for us to determine that an abandonment exemption is warranted.

BACKGROUND

Petition

LSRC, a Class III rail carrier, was formed in 1992 and was authorized to lease from the Detroit and Mackinaw Railway Company (D&M) and operate approximately 275 miles of D&M's rail lines in Michigan, including the Line proposed for abandonment here.<sup>1</sup> In 1997,

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<sup>1</sup> See Lake State Railway Company–Lease and Operation Exemption–Detroit and Mackinac Railway Company, Finance Docket No. 32012 (ICC served Feb. 27, 1992).

LSRC purchased the Line together with the other lines that it had been operating under lease from D&M.<sup>2</sup> In its petition LSRC states that it is now seeking to abandon the Line because of insufficient traffic levels. LSRC asserts that abandonment will permit it to rationalize its system in the area, in which it now provides service over a new rail spur.

LSRC points out that, in May 2006, it lost a substantial amount of traffic in the area when Georgia Pacific Wood (GP) closed its plant in Gaylord. Although the GP plant was located on a segment of the Mackinaw Subdivision main line, just south of the Line at issue here, GP had received 507 carloads in 2005, which contributed to the viability of the adjoining Line. Following closure of the GP facility, LSRC attempted to impose a \$300 per-carload surcharge on all traffic moving into Gaylord to offset some of the cost impact associated with the plant closure; it states that the shippers would not pay the surcharge.

Also in 2006, LSRC joined state and local government entities in constructing a 2.5-mile spur track through GP's property to serve the scrap facility of A&L Iron and Metal, Inc. (A&L). The new spur branches from LSRC's main line immediately south of milepost 116.8, the southernmost point on the Line proposed for abandonment. According to LSRC, the newly constructed spur adjoins over 1,200 acres of property that has potential for development on the southwestern outskirts of Gaylord.

LSRC currently serves four shippers via the Line: NEI, Superior Well Services (Superior), Halliburton (Halliburton), and Magnum Solvents, Inc. (Magnum). The carrier asserts that shipments destined for Superior, Halliburton and Magnum are currently being transloaded to trucks for delivery to those shippers' facilities in the vicinity of Gaylord. LSRC states that, after abandonment, those shippers could continue to receive truck deliveries from transloading points that would be relocated to other sites on LSRC's system, including the new rail spur. The remaining shipper, NEI, receives its shipments directly by rail and does not use transload service; LSRC suggests that NEI could use the new spur by establishing a transloading operation for delivery of its products. The carrier claims that the highway system in and around Gaylord is adequate to permit the delivery of the traffic received by its current customers and any additional traffic that would be delivered to NEI.

#### Shipper and Community Interests

NEI, a distributor of commercial and industrial lubricants, states that it currently receives 90% of its lubricants directly by rail at its facility in Gaylord. NEI indicates that its rail traffic has increased from 24 carloads in 2004 to 41 carloads in 2006 and states that, in 2006, it constructed a 6,000 square-foot warehouse after being assured by LSRC that LSRC would

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<sup>2</sup> See Lake State Railway Company—Acquisition and Operation Exemption—Detroit & Mackinac Railway Company, STB Finance Docket No. 33372 (STB served Mar. 28, 1997).

continue to provide rail service to Gaylord for the foreseeable future. NEI expects to increase its traffic and expects to receive 50 carloads in 2007, a 22% increase over its 2006 traffic volume.

NEI asserts that it is rail-dependent and would suffer serious economic harm if it lost rail service. The shipper says that its lubricants are not susceptible to transloading from railcars to trucks. If its current rail service were lost, NEI states that it would have to receive lubricants by truck and would have to pay an additional \$456,000 per year in freight charges. It claims that truck transportation would not be an economically feasible alternative.

The City expresses concern that the abandonment would have a serious effect on the continued viability of other businesses in the area and on the future of the community by eliminating the Line as an economic tool to attract new companies. The City also notes that the Chamber of Commerce and the Gaylord Otsego Tourist & Convention Bureau have held discussions about reestablishing tourist-based passenger rail service to the area over the Line. Regarding LSRC's assertion that transloading locations could be established for NEI and other shippers, the City points out that the carrier has not indicated locations it owns that could accommodate these facilities and has not responded to requests for assistance to build access roads to proposed transloading sites. The City notes that it has supported the railroad and worked with it to rebuild street crossings at no cost to the railroad. According to the City, there are significant opportunities for new traffic to develop on the Line, and several properties near the Line are available to be developed for commercial uses. The City is concerned about the closure of businesses in the area and points out that several companies are in discussions about acquiring the GP facility.

The Alliance also expresses concern that abandonment of the Line would adversely affect businesses in the area. The Alliance notes that there are several sites along the Line that are available for development, and that the new spur could stimulate increased business. The Alliance views the potential sale of GP's facility as possibly generating additional traffic for LSRC.

The Alliance notes the improvements made by NEI to its facility and indicates that Superior entered into a multi-year lease and invested in leasehold improvements to create an unloading facility, with both shippers having been assured by LSRC that rail service would continue over the Line. The Alliance states that Halliburton and Magnum have indicated that they would receive rail service from another carrier near Kalkaska, MI, and truck their products into Gaylord. Responding to LSRC's assertion that the shippers could be accommodated elsewhere on its system, the Alliance says that one site to which LSRC referred is located in a residential area and is not available for industrial or commercial use and other sites do not have adequate track space. It points out that LSRC has not taken steps to acquire or make available alternative unloading sites, or to relocate any of the Line's current users.

Traffic, Revenue And Cost Information Supplied By LSRC

To support its assertion that continued operations over the Line would be unprofitable, LSRC submitted the verified statement of Wilford Gamble, LSRC's Vice President–Operations. According to Mr. Gamble, in 2005 the carrier handled 145 carloads over the Line for the four shippers, realizing revenues totaling \$130,567, and incurring operating and maintenance costs totaling \$176,742, resulting in a net operating loss of \$46,175. In 2006, the carrier handled 142 carloads on the Line and realized revenues totaling \$159,032. Mr. Gamble did not report avoidable costs incurred by LSRC in 2006, indicating that audited costs were not available. For the purposes of calculating opportunity costs, Mr. Gamble estimated a net liquidation value (NLV) of track, track materials and land totaling \$1,086,464.

According to Mr. Gamble, the Line currently does not meet Federal Railroad Administration (FRA) Class 1 track safety standards.<sup>3</sup> Mr. Gamble submitted a statement from Armond Cassil Railroad Construction, Inc., estimating that rehabilitation of the 4.15-mile Line would cost \$489,968.72 to meet FRA Class 1 standards. According to LSRC, its projections of available traffic on the Line indicate that future revenues would not meet anticipated costs.

NEI and the Alliance criticize Mr. Gamble's statement in numerous respects. They note that Mr. Gamble used historical data, basing his analysis on revenues and costs for 2005. They contend that Mr. Gamble should have provided forecast year data based on a projection of revenues and costs for the 12-month period commencing in the month in which the petition was filed and reflecting the increased revenues and traffic that would be generated by NEI and Superior.

NEI and the Alliance also point out that the costs used in Mr. Gamble's analysis are outdated and do not reflect current operations on the Line. In 2005, LSRC operated the Line 3 days per week. Following closure of GP's plant in 2006, LSRC apparently reduced operations to once per week or less. NEI and the Alliance note that some of the claimed costs, such as employee wages, locomotive fuel, and locomotive maintenance costs, were not properly reduced to reflect current (once per week) service levels, and they challenge the 6-hours per trip figure to service the Line. They also question whether the administrative costs and indirect Train and Enginemen (T&E) costs (for example, safety shoes and lanterns used by LSRC personnel) qualify as avoidable costs of abandoning this line.

NEI and the Alliance assert that the maintenance costs claimed by LSRC are not supported. In particular, they note that a substantial amount of LSRC's maintenance costs are attributable to snow removal. Apparently, to accommodate the use of the right-of-way as a snowmobile path, LSRC uses grooming devices to prepare the path, which plow snow near or

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<sup>3</sup> Under the FRA guidelines, Class I standards require that track be maintained at levels that permit safe freight operations at speeds of up to 10 miles per hour. See 49 U.S.C. 213.9.

onto the track. Mr. Gamble has calculated labor and equipment costs associated with snow removal as occurring 3 times per week for 16 weeks per year. NEI and the Alliance criticize the snow removal costs as excessive and not reflecting current operations of once a week or less on the Line. They also indicate that the Gaylord area averages 8-10 weeks of significant snowfall per year, not 16 weeks. And NEI challenges as unsupported and unreasonable the inspection time used in calculating maintenance costs.

Finally, NEI challenges LSRC's rehabilitation and opportunity cost estimates as being unsupported and unreasonable. In particular, NEI questions the tie replacement cost as excessive in calculating the rehabilitation cost. And NEI contests the valuation of the rail for purposes of calculating the NLV of the Line to determine opportunity costs. NEI also claims that LSRC has failed to show that it has marketable title to the land, and it argues that LSRC therefore cannot include any value for land in its NLV.

### DISCUSSION AND CONCLUSIONS

Under 49 U.S.C. 10903, a rail line may not be abandoned or service discontinued without our prior approval. In considering whether to approve an abandonment application under section 10903, the Board balances the interests of affected shippers, the community, the carrier, and interstate commerce generally.<sup>4</sup> The Board will examine both the current and likely future need for rail service on the line, as well as the burden on the carrier (of continuing to maintain and operate the line) and on interstate commerce (through tying up valuable resources in less productive uses).<sup>5</sup> The railroad has the burden of demonstrating that the continued operation of the line it proposes to abandon would be an unjustified burden on the carrier and on interstate commerce.<sup>6</sup>

Under 49 U.S.C. 10502, we must exempt a transaction or service from regulatory procedures and requirements when we find that: (1) continued regulation is not necessary to carry out the rail transportation policy of 49 U.S.C. 10101; and (2) either (a) the transaction or service is of limited scope, or (b) regulation is not necessary to protect shippers from the abuse of market power. Use of the exemption process, which is designed to minimize regulatory burdens, is appropriate only when the information provided is sufficient, under the circumstances, for us

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<sup>4</sup> Purcell v. United States, 315 U.S. 381, 384 (1942).

<sup>5</sup> Colorado v. United States, 271 U.S. 153, 168-69 (1926).

<sup>6</sup> Illinois v. United States, 666 F.2d 1066, 1070 (7th Cir. 1981).

to reach an informed decision. Where, as here, there is an inadequate record on which to reach an informed decision whether to grant an abandonment exemption, the petition will be denied.<sup>7</sup>

There is not sufficient information on the record before us to permit us to adequately assess the Line's future financial viability or the burden that continued operation of the Line would impose on the carrier and its shippers on other lines that are dependent on its service. While LSRC has provided evidence of past operational costs and revenues on the Line, it has not adequately addressed its current costs, nor clearly limited its costs to rail operations. For example, LSRC's snow removal costs appear to be questionable and may be excessive, as they apparently include costs that facilitate recreational snowmobiling along the right-of-way but that may not directly relate to the maintenance of the Line for rail service. Ordinarily, snow removal costs should be included only to the extent they are incurred for rail operations on the Line, and only for the length of time that snow removal is required for efficient rail service, not to accommodate snowmobiling.<sup>8</sup>

Most importantly, LSRC has presented only the revenues and costs for operations on the Line during 2005 to show that it is incurring a loss on continued operation of the line. Thus, its figures reflect the costs associated with operating three trains per week over the Line in 2005, even though LSRC apparently now operates over the Line only once a week at most. Nor do we have evidence comparing projected costs to the projected revenues expected to be derived from the Line that would be lost to the carrier if the Line were abandoned.

Also, although LSRC estimates that it would cost approximately \$500,000 to bring the Line up to FRA class 1 standards, it has not adequately supported its estimate. Similarly, LSRC has not adequately supported its NLV estimate for purposes of calculating opportunity costs.

Finally, petitioner argues that NEI can continue to use rail service by transloading its shipments of lubricants from truck to rail. NEI, however, asserts that it is unable to conduct transloading operations. We do not have enough information on the record to sort through this factual dispute.

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<sup>7</sup> See Boston and Maine Corp.—Abandonment Exemption—In Hartford and New Haven Counties, CT, STB Docket No. AB-32 (Sub-No. 75X) et al., slip op. at 5 (STB served Dec. 31, 1996).

<sup>8</sup> Inclusion of extra costs to accommodate snowmobiling might be appropriate if LSRC receives compensation for permitting its right-of-way to be used for a snowmobile path; if so, such compensation would properly be included as miscellaneous income in LSRC's cost projections.

In sum, LSRC has based its case on a set of facts that differ substantially from the situation as it exists today, and which will exist in the immediate future. A shipper on the Line has challenged the presentation made by petitioner.<sup>9</sup> That challenge has gone unrefuted. We simply cannot grant the petition on the strength of this record.

For these reasons we are denying LSRC's petition for an abandonment exemption.<sup>10</sup> Denial of this petition is without prejudice to LSRC seeking a new request for abandonment authority (under a new docket sub-number) that contains a more complete presentation and addresses the concerns identified here.

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

It is ordered:

1. LSRC's petition for exemption is denied.
2. This decision is effective on the date of service.

By the Board, Chairman Nottingham, Vice Chairman Buttrey, and Commissioner Mulvey.

Vernon A. Williams  
Secretary

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<sup>9</sup> Indeed, NEI and the Alliance have alleged that two of the shippers on the Line were induced to make significant capital investments in reliance on representations that LSRC would continue to provide service on the Line.

<sup>10</sup> Our denial of LSRC's petition moots labor protection issues and environmental issues, including the Department's request for imposition of a public use condition and for issuance of a NITU.