

BEFORE THE  
SURFACE TRANSPORTATION BOARD

Finance Docket No. 35799

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RAPID CITY, PIERRE & EASTERN RAILROAD, INC.  
-ACQUISITION AND OPERATION EXEMPTION  
INCLUDING INTERCHANGE COMMITMENT-  
DAKOTA, MINNESOTA & EASTERN RAILROAD CORP.

**REPLY IN SUPPORT OF PETITION FOR REVOCATION OF EXEMPTION**

The Brotherhood of Maintenance of Way Employees Division/IBT, Brotherhood of Railroad Signalmen, and International Association of Sheet Metal, Air, Rail and Transportation Workers/Mechanical Division (“Unions”) respectfully submit this reply in response to the reply filed by Rapid City Pierre & Eastern Railroad, Inc. (“RCP&E”) in opposition to the Unions’ petition for revocation of the exemption from 49 U.S.C. §10901, invoked by RCP&E. As is explained in the Unions’ motion for leave to file this reply, the Unions will respond to RCP&E’s assertion that the Unions’ petition is precluded by the ICCTA amendments to Section 10901; RCP&E’s mischaracterization of the Unions’ argument as a contention that the creation of RCP&E was a sham and that RCP&E is the alter ego of Genesee & Wyoming Industries (“GWI”); RCP&E’s argument that GWI’s statements describing the holding company and carrier subsidiaries as integrated or consolidated entities are irrelevant to the issues before the Board; and RCP&E’s claim that its use of the so-called “two step” acquisition and control transaction process and the so-called indicia of independence test is dispositive of the issues raised by the Unions. The Unions also respond to RCP&E’s request that the Board expedite its handling of the Unions’ petition and issue a decision before its planned start of operations on or shortly after June 1, 2014, notwithstanding the substantial issues raised in the petition.

1. RCP&E asserts that the Unions' petition is foreclosed by the ICCTA's amendments to Section 10901 which codified STB precedent applying Section 10901 to non-carrier acquisitions of rail lines (Section 10901(a)(4)), and which barred imposition of employee protections in such cases (Section 10901(c)). RCP&E contends that because of the amendments to Section 10901, the history, purpose and policy rationale for the treatment of acquisitions of rail lines by corporate affiliates of existing rail carriers as Section 10901 transactions is irrelevant, and that the Unions' petition is improper because revocation of the exemption on the grounds asserted by the Unions would mean that the transaction could only be effected subject to imposition of employee protections. RCP&E reply at 3, 10, 14, 15.

But the ICCTA amendments to Section 10901 only codified ICC policies and precedent holding that actual non-carrier acquisitions are covered by that provision, and that employee protections should not be imposed in such cases. Neither change in the Act bars the Union's petition. The ICCTA did not mandate treatment of an acquisition of a line by new entity affiliated with a carrier or carriers as a Section 10901 transaction when the acquisition is effectively one by the corporate parent or a group of affiliated carriers. Yes, in the case of a true, independent, new entrant to the industry Section 10901(a)(4) requires that transaction be handled under Section 10901 with no employee protection imposed. But Section 10901 as amended does not preclude a challenge to a transaction on the basis that it is not actually one governed by Section 10901; nor does it foreclose the STB from finding that a transaction that is presented as a non-carrier acquisition is actually an acquisition by a group of carriers subject Section 11323. The Unions contend that the substantial body of evidence they provided shows that the acquisition of the CP/DME lines is really an

acquisition by a group of carriers.<sup>1</sup>

Because the Unions do not argue that a true new entrant acquisition is governed by Section 11323, RCP&E is wrong in arguing that the history and rationale for the ICC's treatment of subsidiary acquisitions of rail lines as 10901 transactions is irrelevant to the Board's decision. Since treatment of the RCP&E acquisition as a non-carrier acquisition is not mandated by the Act, but would be based on continuation of ICC policy choices, it is certainly relevant to the Board's decision in this case that the ICC's policy was developed in response to the specific circumstances of the railroad industry at the time the ICC decisions were issued— the industry was in a free fall, rail lines were being abandoned, certain acquisitions were the only alternatives to abandonment, the financial prospects for the acquired lines were uncertain, the sales of lines to preserve service were generally to independent new entrants to the industry that were lightly capitalized, and handling of the transactions under Section 11343 with imposition of employee protections was seen as likely to lead to termination of the acquisitions. But, as is shown in the Unions' petition and in the petition of the International Association of Machinists and Aerospace Workers District 19 ("IAM"), the circumstances of the industry relied on by the ICC as its policy basis for treatment of acquisition of lines by affiliates of carriers as new carrier acquisitions are no longer present. The industry as a whole is now doing quite well. And as the Unions and IAM also demonstrated, GWI and its subsidiaries have been doing very well, the line in question is not remotely abandonable, and imposition of employee protections would not cause termination of the transaction and cessation of

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<sup>1</sup>RCP&E contends even if the transaction is viewed as a GWI acquisition, it would still be a non-carrier acquisition. Reply at 13. But such a transaction would still be governed by Section 11323 since GWI controls carriers (*see* Sections 11323 (a)(4) and (5) and (b)(2) and (c)). Furthermore, the Unions contend that the transaction is actually an acquisition of rail lines by a group of carriers all controlled by GWI.

service.<sup>2</sup>

2. RCP&E has mischaracterized the Unions' arguments in asserting that the Unions contend that the transaction is a sham and that RCP&E is the alter ego of GWI. RCP&E Reply at 4,14. RCP&E then attempts to take apart its strawman argument by showing that RCP&E is a lawfully constituted corporation organized for the legitimate purpose of acquiring the CP/DME lines. But the Unions do not contend that the transaction is a fake or illegitimate; nor do they contend that RCP&E is the alter ego of GWI or that there was some illegality or impropriety in the creation of RCP&E. Indeed the Unions expressly stated that it was not necessary for the Board to find that the transaction is a sham or that RCP&E is the alter ego of GWI for the Board to hold that the acquisition of the CP/DME lines is not a Section 10901 transaction but a Section 11323 transaction. The Unions contend that while there may be valid business reasons for creation of a subsidiary corporation to purchase the CP/DME lines, that cannot control the STB's decision on whether the transaction is properly handled as a Section 10901 transaction. The point is that for regulatory purposes, the STB has to look past the creation of separate entities within the corporate family and determine the actual nature and effect of the transaction-- which is that a group of commonly controlled, substantially integrated and interrelated carriers is acquiring the lines of another carrier, so the transaction is

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<sup>2</sup> RCP&E's reliance on *GW Switching Services L.P.—Operation Exemption Lines of Southern Pacific Transp. Co.*, F.D. 32481 (August 7, 2001), 2001 WL 885607 (Reply at 15) does nothing to advance its argument. The passage from that decision cited by RCP&E (slip op. at 6, WL at \*3) rejected the contention that the expedited class exemption mechanism was only available in cases involving lines in danger of abandonment. Here the Unions do not challenge RCP&E's use of the class exemption; rather, they challenge the assertion that an exemption (or approval) of this transaction may be effected under Section 10901. Rather, the Unions argue in part that the ICC's non-carrier Section 10901 cases, and the decisions allowing newly formed entities affiliated with carriers and controlled by entities that controlled carriers to acquire lines under Section 10901 were driven by the circumstances of the industry, concerns about continuation of service, and worries that lines would be abandoned or service discontinued or reduced if the sales were covered by Section 11343 and subject to employee protections. That issue was not addressed by *GW Switching*.

subject to approval or exemption under Section 11323, not Section 10901. This does not require a finding of illegality or impropriety, or that RCPE is not a real corporation. Consequently, it does not matter for regulatory purposes that GWI had legitimate business reasons for creating RCP&E, such as separating the holding company from risk. The issue is not whether GWI was motivated by bad intent, but whether the transaction is in actuality a Section 11323 transaction and not a Section 10901 transaction, regardless of the corporate devices used

. Furthermore, the Unions demonstrated that a substantial body of Supreme Court precedent holds that the predecessor to Section 11323 was actually directed at abuses flowing from the holding company-subsidary system; and that the agency must consider the reality of a transaction, and can not let corporate forms or the manner in which a transaction is structured or presented to the agency dictate its application of the Act.

The Unions also demonstrated that it is commonplace for Federal agencies and courts to ignore distinctions among affiliated corporations in order to properly administer and apply Federal statutes without “piercing the corporate veil” or finding that creation a new corporation was not valid under State law or was for an illegitimate or improper purpose. Agencies and courts routinely hold that even if creation and use of a separate corporation is legitimate under State law and the corporate form is accepted for State law purposes, the application of federal law can not be evaded or controlled by use of holding companies, affiliated corporations or subsidiaries.

3. RCP&E’s principal argument relies on precedent upholding use of the so-called two step process (the acquisition is handled under Section 10901, and the continued control of the subsidiary effecting the acquisition is handled as an entirely separate transaction under Section 11323) and on application of the so-called “indicia of independence test” that was developed by the ICC in very different circumstances. RCP&E asserts that this transaction satisfies those tests so the Unions’

petition should be denied. Reply at 3,16, 17-26.

But the Unions respectfully submit that the Board should not continue to use the two step process and indicia of independence test to determine whether acquisition of a rail line by a corporate affiliate of a carrier is properly handled under Section 10901. As the Unions demonstrated in their petition, the two step process and legitimate business purpose/indicia of independence test are not mandated by the statute but are agency constructs based on policies developed by the ICC in circumstances that no longer exist. And as is explained in the IAM's petition (at 12-14) the STB is free to depart from those constructs.

The Unions also demonstrated that the very history and development of the GWI group of carriers shows that the indicia of independence test is not a useful method classifying transactions as covered by Section 10901 or Section 11323, and that the two step process ignores the reality of these transactions. GWI acknowledges that it has created a network of interrelated railroads organized into regional units with key management, administrative and other core business functions performed by another GWI subsidiary. GWI candidly admitted that it has put together multi-carrier regional railroads through acquisitions of lines by newly formed subsidiaries that each passed the indicia of independence test, where the acquisitions were actually designed to create integrated systems. GWI's financial reports and presentations now acknowledge that it used the two step process and indicia of independence test to create what were in actuality regional networks, even though GWI denied that purpose when the transactions were presented to the ICC. While the ICC found that acquisitions of various rail lines by newly created GWI subsidiaries passed the indicia of independence test, it is now obvious (and admitted) that the subsidiaries actually function as collections of carriers. The STB is under no obligation to continue to allow subsidiaries and parents like RCP&E and GWI to utilize the two step process and indicia of independence test as a basis for

treatment of a transaction under Section 10901 when the reasons for their development are gone, GWI today is a very different entity from those for whom the process and test were originally developed, and experience (particularly that of GWI) shows that line acquisitions that were treated as Section 10901 transactions were really line acquisitions by carriers or groups of carriers.

4. While RCP&E asserts that facts it cited under the indicia of independence test show that it has autonomy and authority in certain areas so the transaction truly is an acquisition by a new, independent, non-carrier entity, the evidence adduced by the Unions demonstrates that it is not. GWI does not merely have technical control over its subsidiaries because it owns their stock, GWI **controls** its subsidiaries with respect to their most fundamental decisions and actions. The notion that the RCP&E is somehow similar to a true non-carrier, new entrant as described in ICC decisions from the 1980s and should be treated the same way for purposes of application of Sections 10901 and 11323 is absurd. True, separate, non-carrier, new entrants do not have parent and affiliated entities provide core business and rail carrier functions for them; and they are not part of regional units. True, separate, non-carrier, new entrants do not have billion dollar revenue parent corporations that provide access to credit and consolidated purchasing and combine their overhead costs with corporate affiliates. True, separate, non-carrier, new entrants do not have billion dollar revenue parent corporations that guarantee their obligations under their acquisition agreements and assure customers that they will receive high quality service because they are part of a conglomerate of established carriers. And true, separate, non-carrier, new entrants do not have their employment policies determined by others, and do not have codes of ethics rules and corporate cultures imposed on them.

Moreover, as the Unions demonstrated, in statements everywhere but the STB, GWI acknowledges that it sits atop an integrated group of carriers, the carrier subsidiaries are actually

parts of an interrelated network of carriers, the carrier subsidiaries within various geographic areas are actually regional systems, and the RCP&E acquisition is effectively an acquisition by the GWI group of carriers. RCP&E dismisses the Unions' reliance on GWI's annual reports and statements to financial analysts by saying that statements by GWI that refer to the holding company and subsidiaries collectively, or that refer to "we" or "us", or that say that "we" or GWI or G&W signed an agreement with CP or acquired the CP/DME lines do not prove anything. RCP&E asserts that the apparent meaning of such statements is somehow negated by explanations or disclaimers in the annual reports that say its use of the words "we" or "us" refer to GWI and its subsidiaries; and that securities laws require the use of the words "we", "us" and "our" when referring to related corporations. Reply at 25-26. This argument provides no support for RCP&E.

That the annual reports define the terms "we" and "us" as GWI and its subsidiaries does not undercut the effect of GWI describing the parent company and subsidiaries as a consolidated or integrated entities. And the assertion that securities laws require related corporations to use the words "we", "us" and "our" actually supports the Unions' arguments, demonstrating that under other statutory regimes, corporate forms and structures do not control application of Federal law. Furthermore, some of the most significant statements describing GWI and its subsidiaries as a single entity or a carrier conglomerate, or that "we" made the acquisition from CP/DME, were not in annual reports or 10K reports but were statements by GWI CEO Hellman and CFO Gallagher in presentations to financial analysts. And RCP&E ignores their statements that did not merely refer to the GWI companies collectively, but discussed imposing GWI rules and "culture" on the subsidiary railroads and cited replacement of general managers of former RailAmerica railroads as illustrating how GWI improves the performance of the subsidiaries.

RCP&E's reply does not in any way refute the Unions' showing that the RCP&E-CP/DME

transaction is really an acquisition of a carriers rail lines by a group of carriers.

5. RCP&E asserts that the Unions have not demonstrated that there is a basis for revocation of the exemption it invoked in this case. Reply at 8-9. However, the Unions demonstrated that RCP&E seeks to effect the acquisition under an exemption from Section 10901 when the transaction is one that may only be effected by approval under, or exemption from approval under, Section 11323. Use of an exemption to consummate a transaction without lawful approval or exemption from approval under the governing section of the Act is certainly grounds for revocation of an exemption.

6. While RCP&E seeks a quick decision so it can begin operations on or after June 1, 2014 without any question about whether Section 10901 applies (Reply at 7), there is no valid basis for a rushed decision on the Unions' petition. RCP&E may have assumed that no petition for revocation would be filed so it could consummate the transaction and begin operating in June without uncertainty about the validity of its notice of exemption, or risk that the exemption might be revoked. But that does not mean that RCP&E is entitled to quick decision when there is a substantive challenge to the notice. The very nature of the exemption subject to revocation process creates a situation where parties can invoke expedited process, but they use it at the risk of subsequent revocation. *See also GWI Switching Services, supra.* at \*3- the class exemption process was designed to “grant exemptions and rely on ‘after the fact’ remedies including revocation to correct any abuses”. *Id.* at \*3, citing and quoting *Class Exemption –Acq & Oper. Of R Lines*, 1 ICC 2d 810, 811 (1985).

RCP&E faults the Unions for filing their petition a week before a petition for a stay was due. *Id.* But parties opposed to a transaction are not required to file for a stay in order to seek revocation. In any event, the Unions and IAM managed to file full scale petitions to revoke within the time frame

allowed for stays. Furthermore, given the volume of material in the GWI/RCPE filings, and the changes in GWI over the last two years the Unions were certainly not dilatory in taking several weeks to file their petitions. And the union filings were not mere pro forma oppositions to the transaction; rather they were detailed petitions with extensive presentations of independently developed facts with extensive case citation. The suggestion that the Unions unreasonably delayed their filing and that RCP&E is entitled to issuance of a decision within several weeks after the petitions for revocation were filed is specious and should be rejected by the Board.

Finally, the Unions renew their request for oral argument. The Board should not simply continue the policies devised by the ICC in very different circumstances to a very different subsidiary new corporation/holding company arrangement without close consideration of whether those policies continue to effectuate the Act and without engagement with the facts and legal arguments presented by the Unions, IAM and the SMART Transportation Division.

Respectfully submitted,

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**CERTIFICATE OF SERVICE**

I hereby certify that I have caused to be served one copy of the foregoing Reply in Support of Petition for Revocation of Exemption by First Class Mail, to the offices of the following:

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